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What we're doing to add value to the Phillip Money Market Fund in 2012

Steady appreciation is the name of the game

2011 proved to be a year of "first times" for the Phillip Money Market Fund. Firstly, the Fund achieved a new high of $870m in fund size, exceeding the $748m from October 2010. New flows came mainly from private banks and government institutions. Secondly, the annualised yield of the fund declined from about 0.70% in the beginning of 2011 to about 0.55% by December 2011, an all time low for the fund since its inception in 2001. Thirdly, and partly in response to the lower yields, we reduced the management fee on the fund from 0.50% to 0.45%; Essentially returning 5 basis points back to investors.

While the fund experienced 3 significant changes, other features remained consistent with the long-term objectives of the Fund. The fund maintained its 100% no-default track record on debt held, the fund continued to deliver a 100% positive month-on-month price change and, the Fund delivered a positive spread between short-term deposit rates and current account rates paid at Singapore banks.

Going forward for 2012, we are crafting our strategy with an eye on the large picture for interest rates, the policy landscape (BASEL III) inflation and fiscal challenges in the West as well as keeping the other eye on the profit outlook for Asia corporations. With regard to US and SIBOR rates, we expect them to stabilize around current levels for 2012.The US Federal Reserve Bank has signaled its intention to keep rates low "until at least 2014", the SIBOR in turn has historically referenced the US Fed Funds Rate. We don't expect this relationship to change in 2012. Stabilizing yields is likely to be balanced by more attractive rates on fixed deposits that banks are willing to pay us due to BASEL III capital requirements. In combination the net effect is likely to be gradually improving yields for the Fund.

With regard to the profit outlook for Asian corporations, we are anticipating steady growth, baring external shocks such as wars…etc. The profit profile of Asian companies as a whole is likely to be supported by the trend of Western funds moving into Asia and intra-Asian economic activity.

Properties and Banks are likely to retain significant allocations in our portfolio. While many property firms are currently experiencing shrinkage in earnings due to smaller development profits, their ability to remain free cash flow positive due to rental income should keep their creditors happy. Banks' non performing loans remain low and loan discipline remains intact despite strong demand for loans and historically low interest rates. Even when we factor in extreme assumptions of economic slowdown and earnings contraction, we do not expect problems meeting the obligations of their creditors, at least for 2012.

Managing liquidity is an important factor. On average, we meet between -$4m or +8m in redemptions or subscriptions everyday. This means, just based on "regular" fund flows alone, the fund may shrink or grow between 0.5% or 1% of its fund size everyday. In a normal period, we can use this information to optimize asset allocation; Hold more money market securities and less cash. However on non-average days, such as days surrounding Lehman's demise, redemptions may rise to many times 0.5%. In periods such as these, it is important to err on the safe side and raise cash holdings significantly above the allocation to money market securities. As mentioned above, we expect 2012 to be a year of steady growth, hence we are not positioning for a worst case scenario type of situation. We are comfortable with holding more than 50% in money market securities, with about 30% in fixed deposits, and less than 10% in cash.

Our dual objective with the Phillip money market fund has always been to preserve capital while generating a return higher than Singapore bank deposits. We will continue to focus on this dual objective by abiding by our tried and tested investment processes while keeping an eye on changes on the horizon. Our investment philosophy, which has served us well over the years, depends on deep primary knowledge of how Asian firms operate and managing the portfolio for safety.