

Are your investments too “gao”?

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In our part of the world, ordering a drink is almost an art that has to be passed down from generation to generation. There's Kopi, then there is:

*Kopi Peng
Kopi Siu Dai
Kopi O
Kopi Di Low
Kopi Gah Dai
Kopi C
Kopi Tarik
Kopi Poh
Kopi Gao
Kopi Kosong*

The list goes on with more permutations and combinations...

Coffee drinking is a serious business! The phrase that I learnt most recently was Kopi Dilow, which translates to Coffee Direct Pour. It is definitely not a drink for the faint hearted as it's a shot of coffee with very little excess water, giving you a stronger Kopi kick than that of a Kopi Gao.

Discussion

• Portfolio Diversification

Personally, I find anything beyond a Kopi Gao a bit too strong for me. For some people, excess caffeine can affect your sleep and cause heart palpitations. I like a Kopi that just perks me up and help keep me alert throughout the day.

Like Kopi, your investment portfolio should have a good balance of different ingredients. However, investors often want a quick fix and most ended up choosing a very concentrated investment portfolio. I have heard many investors tell me that they placed their hard-earned money into one or two very safe bonds with a high yield to collect a good income. What they may not realise is - this is a very concentrated, or “Gao” approach. Should something adverse happen to one of the bonds, the investor will lose half of his portfolio. The Kopi that you initially thought to be low risk and satisfying turned out to be a bitter cup that most will find hard to swallow.

A better and safer way to invest is through a diversified portfolio of income generating assets, spreading the risk across many positions so that even if adverse events occur, only a portion of the portfolio will be affected. In my own portfolio, I invest across equities, bonds and alternative assets, which lowers the overall risk of my savings and helps me sleep better at night. In the case of a bull market, the equities in my portfolio tend to outperform other asset classes, boosting the returns of the portfolio. On the other hand, when facing a bear market, I know that bonds are less volatile and reduce losses, helping me worry less and ensures that I stay invested in the market.

Does this mean that we must invest in multiple assets from different countries?

Although those are possible investment strategies, I think that you do not necessary have to aim to invest in multiple investment vehicles from multiple countries. Let's take investing in stocks in Singapore as an example.

Many companies in Singapore are listed and they do offer stocks for people to invest in. These stocks can belong to companies of varied sectors such as telecommunications, oil & gas, financial, aviation, consumer service sector and more. Also, many Singapore-listed companies not only have businesses in Singapore - some have overseas presence and they have high growth potential. Thus, the performance of these companies will also be affected by their overseas counterparts which also helps investors achieve their aim of diversification with higher returns.

In addition, I personally think that income generating equities that pay consistent and growing dividends appeal more to me. Dividends are a good signal of the ability and willingness of a company to pay its shareholders. In the long run, as dividends can only be paid out of operating cash flow, dividend paying stocks are likely to be businesses that are strong in financial health. This trait can be seen in Singapore-listed companies as shown in Figure 1.

Dividends also demonstrate that the company's management is focused on rewarding shareholders, rather than engaging in value-destroying projects or acquisitions to benefit themselves.

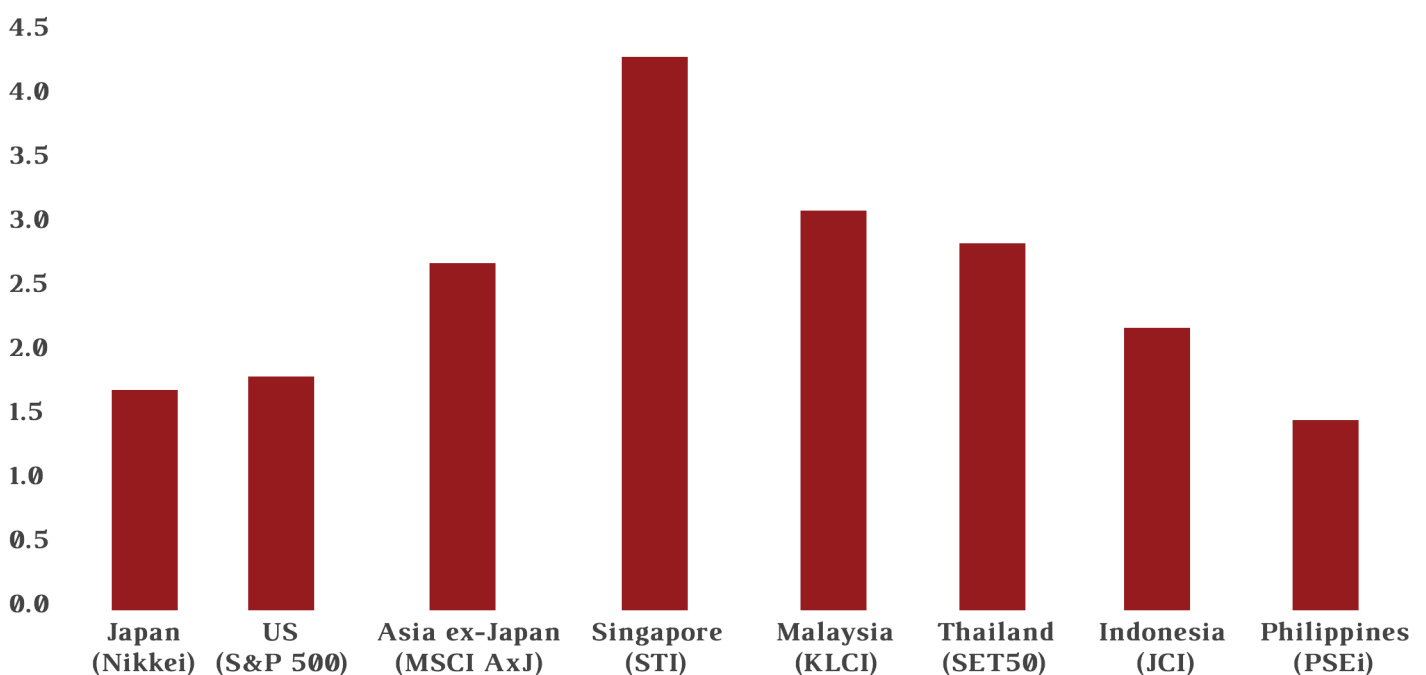


Figure 1: Dividend Yield (%) of global and regional markets

Source: PCM, Bloomberg (August 2018)

Besides, I also prefer companies that are growing their dividends instead of paying out everything. This demonstrates to investors that the company is not in an industry with structural growth issues or is in secular decline. Companies that reinvest some of their cash into projects to boost the company's future cash flow and allowing it to pay out even higher dividends in the future is extremely attractive.

There is a Chinese proverb 众人拾柴火焰高, which translates to “when working hard together, the flames rise high”. Here, the word 高 is also pronounced as “gao”, but unlike the “gao” in “kopi gao”, it is enunciated with a rising pitch and means “high” in Mandarin. Similarly, a diversified portfolio of investments working together can help your savings rise high. You will more likely be sitting at the Kopitiam enjoying your morning Kopi, savouring your investment gains knowing that your money is relatively safe.

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