PRUDENTIAL **INSIGHTS**

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INVESTMENT MANAGERS

Prudential Investment Managers

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Bonds: A boring asset or a boost to your investments?

Bonds might seem ‘boring’ to some investors, particularly when compared to other asset classes, but they have two important roles to play in your portfolio – reducing risk and delivering steady income. In addition, South African bonds are currently offering compelling returns similar to that of equities, which means that investors now have the added benefit of lowering their portfolio risk while enhancing their investment returns.

The traditional rule of thumb is that the higher the potential return for an investment, the higher the potential risk. When you invest in equities for example, which are on the higher end of the risk-return spectrum, you’re likely to receive better returns compared to other asset classes over time, but with this potential comes significantly more volatility. With bonds, on the other hand, there is a set return (or coupon) that you’ll be paid at predetermined intervals over time (usually semi-annually), and your capital will be returned to you intact, except for in the case of extreme circumstances such as the issuer becoming insolvent and not being able to fulfil its repayment obligations. In a world filled with uncertainty, a relatively safe bet can often be a great source of returns.

Risk versus returns

Usually, we think of bonds as a diversifying asset that can lower risk within a portfolio, and understand that with that lower risk will come lower returns overall. But local bonds are currently proving this isn't always the case – you're getting the benefit of lower risk but with equity-like returns. This is a great opportunity to potentially boost your investments.

The current environment has made way for bonds to buck the trend of solely providing predictable returns. They certainly have their place in an investment portfolio, but while there is a great opportunity, as with any investment, it's important to understand what you're investing in, which we have explained simply, in our guide to investing.
Cautious investors should be aware that risks do exist when investing in bonds. For example, inflation is one risk: if interest rates are exceptionally low and inflation is rising, you may not receive an adequate above-inflation (real) return. This has happened in recent years in developed economies like Europe. Another risk is that the bond issuer could default on what is owed to you; however, this is rare, particularly for government bonds.

While they do come with some volatility, bond returns can be rewarding and can boost your investment portfolio overall while increasing diversity. Currently, SA government 10-year bonds are yielding around 9.5%, which is a real return of around 4.5% when taking into account long-term average inflation of around 5% in South Africa. Bonds may seem complex to some investors, so consider working with a financial adviser to help you.

Investing in bonds with Prudential

At Prudential we utilise bonds across a range of our multi-asset and fixed-income portfolios, primarily as a means to reduce risk and enhance investment returns. While our lower-risk funds, such as the Prudential Income and Money Market Funds, make use of shorter-dated bonds with lower yields, the Prudential High Yield Bond Fund typically invests in bonds with longer tenors and is suited to investors who require a high level of income from their capital investment, but with relatively low risk. The fund invests in a diversified portfolio of South African high-yield bonds. Try our Fund

Selector tool to find out which of our funds are best suited to your investment needs.

Keep in mind that our brand name and funds will be changing to M&G before the end of the year, but the mandates of our funds and the way we manage them will remain unchanged.

For more information, please feel free to contact our Client Services Team on 0860 105 775 or email us at query@prudential.co.za.