CPF: Low risk with comparatively high returns, says new study

The returns are comparable to those from riskier investments, but without the downsides, according to a recent study on the Central Provident Fund.

Dylan Loh
***Channel NewsAsia*, **8 December 2014

SINGAPORE: It is rare to find a low-risk investment fund that generates comparatively higher returns, but Singapore's Central Provident Fund (CPF) does exactly that - according to a new study by the Institute of Policy Studies and professional services firm Towers Watson.

The study sought to assess the value of returns provided to the average CPF member and compare it with alternative investment portfolios.

Within the CPF, the Ordinary Account - which can be used to pay for homes or education - currently gives a guaranteed interest of 2.5 or 3.5 per cent for balances up to S$20,000. This is significantly higher than deposit rates offered by the banks.

Mr Christopher Gee, a research fellow with the Institute of Policy Studies at the Lee Kuan Yew School of Public Policy, said: "The Government's guaranteed minimum rates that are offered in the CPF actually provide a strong benefit to the CPF member. And the calculations in the framework that have been provided by Towers Watson have shown that this is actually about 1.4 per cent per annum additional to what would have been the case if those minimum rates did not exist."

CPF monies are invested in Special Singapore Government Securities, which are guaranteed by the Government and have been given the top 'AAA' credit rating by all three major global ratings agencies - Standard and Poor's, Moody's and Fitch.

According to the study, the Government's unencumbered assets act as a buffer - allowing it to absorb volatility and satisfy CPF obligations. Therefore, Singaporeans are able to benefit from higher returns relative to the lower risks borne with CPF savings.

A key assumption of the study is that Singapore and global inflation will remain modest over time. If this is not the case and inflation gallops ahead, it will adversely affect the savings of Singaporeans. Keeping inflation and other factors constant, the study found that returns for a CPF member typically come within range of returns from a balanced but riskier investment portfolio of 60 per equities and 40 per cent bonds.

The study found that S$100 put into the CPF system today will be worth S$303 in 20 years, with no downsides since the Government bears the risks. The same amount put into a balanced portfolio will be worth S$315 - not that much more but with considerably greater risks associated with market investments.

Mr Peter J Ryan-Kane, the head of portfolio advisory for Asia Pacific at Towers Watson, explained how the Singapore Government is able to take substantially greater risk: "You need to distinguish between the lifespan of a typical member and the lifespan of the Singapore Government. So a typical member obviously has a human-type lifespan. The Government has a perpetual lifespan, so that enables the Government to take substantially more risk than any particular individual."

Researchers said potential CPF improvements could lie in investing monies in more market-related assets. which generate higher returns. However, that would also mean raising the risk level for investments.