Your Wealth Bulletin

August 2009

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Hi,

Welcome to the August issue of Your Wealth bulletin.

There is more to life than increasing its speed (Mahatma Gandhi)

Active Management Underperformance

Work harder, earn less

As kids, we're taught that the harder you work at something, the more rewards you get. It's so true in many facets of our life.

However, numerous academic studies show that the more 'work' you do at sharemarketing investing (ie. trading), then the risks are evident that you will underperform the market itself.

Think of it this way. Some of the smartest people in the world are recruited by global financial corporations. After years of education, training and experience, the best and the brightest are then empowered with the corporations resources to buy and sell stocks every day.

The resources at their disposal is enviable. They have research staff worldwide, highly intelligent analysts as well as the ability to contact company CEO's and Directors to ascertain up to the minute information.

So these people are genuinely at the forefront of information and you would think, the ability to predict which way a company's share price is going to move.

Wrong. Over the long term, after fees and expenses, the majority of actively trading fund managers underperform the market in any one year.

What about the bad times then?..........if the market is diving off a cliff and has fallen by over 50%, then won't the smart fund managers be putting their money in cash and staying out of the market altogether?

It seems the answer is 'no' again.

Recent research from Morningstar has shown that the assumption that active fund managers will perform better in a depressed market may be under threat, with results from a survey of 47 fund managers revealing less than half of active fund managers outperformed the Australian market index in 2008.

Out of 29 active fund managers included in the survey, only 13 achieved returns above the benchmark in 2008.

The research also confirmed that only a minority of active fund managers have been able to outperform the market in the long term. Less than one-third of all active fund managers outperformed over a three, five and seven-year timeframe up to March 2009.

"The argument made by the proponents of active management - that bear markets strongly favour active managers since indexes are sure to follow as markets head south - simply did not hold up in 2008," the report said.

On average, active management did more harm than good, the report said.

Of interest, we have been analysing our DFA and Vanguard portfolios. While we typically do not reference our short term performance, the recent outperformance of these funds against that of the peer Morningstar Benchmarks (for Growth and Balanced Portfolios) has been showing very significant numbers.

In the past 18 months we have recommended investors 'stay in their seats' wherever possible. When markets return sharply, just like they have in recent months, then you can capture the market return. The rewards on offer over time are attractive, the key is patience and discipline.

Sticking to the Plan

A lesson from sport

It's probably no secret that i'm an avid follower of the St.George-Illawarra Dragons. So when a story crosses my desk about the coach Wayne Bennett, it's a sure bet that i'm going to read it.

The interview with the coach reviewed his keys to success. There was one point that he has echoed in his own biographies and other interviews.

Bennett states " The biggest problem with most leaders today is they don't stand for anything. Convictions provide that direction. If you don't stand for something, you fall for everything."

He continues, "Follow your beliefs and don't give in to yourself".

These comments have significant relevance for investors.

Having an investment philosophy that you believe in, and will adhere to no matter the economic commentary and media noise, is likely to the number one determinant on whether you will have a successful investment experience or not.

Your determination to remain steadfast to reaching your goal, and belief in how you will achieve it is likely to be more influential on your outcome, than the underlying investments themselves.

I have mentioned to many clients that a significant 'value add' that we provide is in our role to ensure that investors adhere to the plan, no matter how boring the investment philosophy may be.

Managing 'greed' and 'fear' is part of our role with investors. This is human nature.

But we can provide you with the knowledge and confidence of an investment methodology that has been proven to work over decades and decades of market rises and declines.

Once you have that confidence and awareness, it's inevitable that times will come when you start to doubt yourself. Particulary when the media is shouting from the rooftops that we're approaching a financial armageddon.

As Warren Buffett has stated in the past, "market falls are times when money moves from weak hands to strong hands." It makes sense as research has shown that investors typically enter the market when it's high, and sell out when it's low.

If you're confident in your investment philosophy, then stick to the Wayne Bennett saying, "Follow in your beliefs and don't give in to yourself".

Wayne Bennett interview

If you have any queries about this month's newsletter or would like to discuss your financial situation in more detail, please feel free to email or call our office on 1300 78 55 77. If you would like to forward this email to a friend, click on the forward email link below.

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