



**BALANCED INVESTMENT STRATEGIES**

FINANCE ♦ BALANCE ♦ LIFE

## **Market Returns**

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**Balanced Investment Strategies**

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## Our Licence

In August 2007, after a lengthy application process Balanced Investment Strategies (BIS), our financial planning arm, was granted an Australian Financial Services Licence. This enabled our qualified staff to provide financial advice without the influence of a large licensed institution or any financial product provider.

## Our Philosophy

### Fees

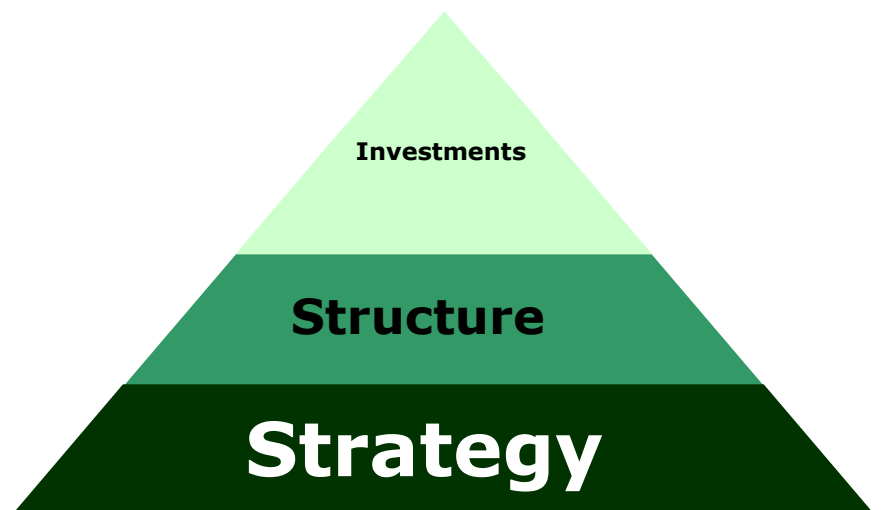
Our philosophy as a licensee has been that we should charge our clients an appropriate fee for the service we provide and not accept commissions from the products we recommend. By their nature commissions create a conflict of interest and the true cost of commissions are often hidden in paperwork.

### Strategy & Structure

Our philosophy has also included the idea that it is important to firstly develop a sound strategy for our clients and secondly, structure their affairs correctly. This ensures any financial plan has a solid foundation, and with regular monitoring, can deliver on expectations. The benefits of this include reducing costs, saving tax and improving cashflow.

### Investments

When building our clients investment portfolios we take a cautious approach, with the emphasis on long term results.. However in the last few years we developed a clearer approach to investing, more consistent with our philosophy of Strategy, Structure and Investment.



## Asset Class Investing

After much investigation and research we are convinced that Asset Class Investing is a more sound approach to building wealth over the long term while incorporating tolerance for risk. Asset Class Investing is based on spreading investments over differing asset classes, whether it be fixed interest or equities, domestic or international – providing diversity to create a portfolio built for all climates.

### Why are we convinced?

- Studies have shown that 90% of investment returns are generated through asset allocation - only 10% comes from the individual stock selection;
- Active investment managers, who market themselves as investment experts, are often expensive and regularly underperform the market after their costs are taken out; and,
- An Active manager who outperforms the market in one year rarely repeats this in ensuing years.

Successful investing means capturing the risks that will provide your expected return and reducing risks that do not. We want to ensure our clients capture the returns that the market gives over time.

We realise that you cannot control markets, so we seek to manage the things that can be controlled: fees and taxes.

When the investment mix is accurate, your portfolio will then:

1. Reflect your investment time frame and tolerance to risk
2. Provide the correct level of liquidity and
3. Provide you with the expected return.

Benefits of this approach include:

1. Reduction in investment fees
2. Potential Capital Gains are better managed
3. A far greater understanding of the hows and whys of investing
4. Less reliance on a "wonderboy" fund manager picking this years winner
5. Far greater liquidity
6. Greater investment discipline and better results

## **Dimensional**

Dimensional are a funds manager that specialises in "Asset Class Investing". Their approach is to:

1. minimise investment costs by only transacting on their terms and not triggering tax events unnecessarily; and,
2. reduce risk through diversification.

We will be using Dimensional for our clients who feel "Asset Class Investing" is the right approach for them. This is not to say other investments such as direct shares, investment properties or other funds managers cannot be used in the mix. However, it will be important to ensure that the amount of risk in a portfolio is aligned with the level of risk that is acceptable to our investors.

## **Market Returns**

Market Returns will be replacing the Monthly Market Review and is intended to inform you of the sources of investment returns and give you an understanding of what can and can't be controlled. Our approach is an admittedly unsexy story that is at odds with the gung-ho stock picking approach still dominant in the Australian and New Zealand market.

This month's Market Returns is part of an article written by Jim Parker

However, we hope you find Market Returns interesting and if you would like further information on Asset Class Investing please don't hesitate to contact Renee, Justin or Brian.

## Sovereign Risks by Jim Parker

Eighteen months ago, markets were fretting about the huge debts carried by major banking institutions. Now the worry is over the huge debts carried by the governments who bailed the banks out! So what's an investor to do?

This crisis-driven transfer of large private sector debt obligations from wounded banks to public sector balance sheets is certainly the talking point "du jour" in financial market and media circles. There is little doubt that the financial crisis and subsequent recession in many developed economies have placed a heavy burden on the fiscal positions of those nations. The IMF, for instance, has forecast that general government gross debt in the advanced countries will rise, on average, from 75% of GDP at the end of 2007 to about 110% of GDP by the end of 2014.

The news story out of this is that the financial crisis hasn't really gone away; it's just been transformed from a banking crisis to a potential sovereign debt crisis. This has many people asking where the safe havens will be for investors if even sovereign borrowers are judged as too risky. There are a few observations to make in answering that question. The first is to observe that no investment is totally risk free. Even sovereign borrowers with the power of the printing press at their disposal can and have defaulted.

The second observation is that markets already have made a judgement about rising sovereign risk, as reflected in prices. Spreads — or the margin that investors demand for investing in government securities perceived as riskier than the top-rated 'AAA' debt — have blown out as concerns have mounted. The third point is to reflect on the fact that not all sovereign borrowers are equally challenged in terms of their public finances. Most attention in recent weeks has been on Greece and other southern European states like Portugal. But the debt of other major developed nations — including the US, Japan and Australia — is relatively unaffected.

Just as in equity markets, investors in fixed income markets demand a greater expected return for taking on additional risk. That is why the spreads on Greek government debt blew out so much in recent times. And, of course, these relative prices can quickly adjust to new information as it comes to hand, which is why spreads retraced a little on speculation of a European rescue package for Greece.

As no-one knows what the future will hold, fixed income investors can deal with the uncertainty by holding a diversified portfolio spread across a wide range of sovereign, supra-national and corporate issuers, by limiting exposure to any single issuer and by restricting the eligibility of certain countries of risk. For those who want a more conservative strategy, they can restrict their investments to only top-rated borrowers and in short-term instruments. Also, there is no compulsion to diversify globally if the risks of doing so are not commensurate with the returns.

To the claims being made in some quarters that sovereign debt will start to behave more like corporate debt, the answer is the same: No investment is risk-free and markets will make their instantaneous judgements on relative creditworthiness — whoever the issuer - which means all investors need to do is diversify around risks they are willing to take. So the message is the same — markets are quick to price in new information, risk and return are related, diversification is the antidote to country or company specific risk and, in considering a fixed income strategy, investors should take note of a range of risks — including default risk.

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