



# Investment update

What's happening in the markets – and what it means for your super

After four years of extraordinarily high returns – producing a cumulative return in NGS Super's Diversified option of 71.2% – the past year has been one of extraordinary volatility. The result is that most super funds have produced poor annual results.

## Super is a long-term investment

Somehow, when super funds produce high returns, we are happy to accept them as an entitlement, and barely take notice. But when returns fall to low and even negative numbers, we feel a shock far greater than any excitement we might have felt about the high returns.

In both good times and tough times, it's important for us to keep things in perspective. Rather than exulting or worrying about the short term (this year's result), we need to focus on the long-term returns for our super. It's designed to grow over many years, not just one.

The average annual return for NGS Super's Diversified option for the five years to 30 June 2008 was 10.3% – well above the option's investment objective of exceeding the consumer price index by 3% per year. The fabulous returns of the last four years have helped balanced this year's –4.68% return. Although this is the lowest return for this option in twenty years, NGS Super's portfolios have performed very well relative to other funds. Most super funds have had their worst year ever.

## How did it happen?

Investment markets run through cycles. In good years, like 2003–2007, markets are growing, and investors believe the market is full of opportunities and feel enthusiastic about growth, so they are willing to pay higher and higher prices for financial assets. But good times are invariably followed by periods when the markets start falling. Some people lose confidence and want to sell their investments, while buyers are no longer willing to pay high prices, and optimism about growth turns to pessimism and uncertainty.

Sometimes these changes in market confidence happen because prices have just got too high. This was the case with the share market crash in 1987 and in early



## RETURNS FOR SUPERANNUATION INVESTMENT OPTIONS TO 30 JUNE 2008

Investment option	1 year %	Average per year over 5 years %	Average per year since inception %	Inception date
Diversified	-4.68	<b>10.30</b>	7.61	Sep 1999
Shares plus	-12.91	<b>11.76</b>	7.44	Sep 1999
High Growth	-6.22	na	na	June 2007
Conservative	-1.47	na	na	June 2007
Defensive	-1.69	<b>6.95</b>	6.70	Jan 2003
Australian Shares	-13.21	<b>15.10</b>	15.15	Jan 2003
International Shares	-14.74	<b>7.20</b>	8.10	Feb 2003
Green Shares	-12.73	<b>11.11</b>	5.98	Oct 2001
Property	-6.07	<b>11.80</b>	11.73	Aug 2002
Diversified Bonds	6.23	<b>5.43</b>	5.83	Sep 1999
Cash	5.39	<b>5.00</b>	4.81	Sep 1999

Past performance is not an indication of future performance. Your individual return might be different depending on, for example, when your contributions were received and whether you have switched investment options during the year.



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2000, after the prices of technology stocks had risen well beyond reason and collapsed in what's often called the 'tech wreck'. Sometimes the change is brought about by a sudden shock, such as the invasion of Kuwait in 1990 (though markets actually rallied once the Gulf War began) and the terrorist attacks on the United States in September 2001. In 2007–08 it was the sub-prime crisis in the United States that started to turn the markets.

Today, globalisation gives us access to investment opportunities across the world, but it also means that a crisis in one market – especially one as big as the United States – can bring trouble for markets just about everywhere, including Australia.

### Strong economies, but falling markets

For all of the talk of a US recession – and its share market (the world's largest), fell by a massive 23% over the past year – the world economy enjoyed a year of strong growth, led by extremely strong economic conditions in much of the emerging world. Yet the global share index fell by 16% over the year.

Locally, the exceptional growth in China has been good for our economy. The huge growth in demand for our commodities has given Australia a record sixteenth consecutive year of economic growth. And our unemployment rate is the lowest it has been for 32 years. Share prices for our resource companies increased significantly over the year, but prices for many high-quality industrial companies and the banks fell by 30–40%. The Australian share index fell by almost 14% over the year – its worst financial year performance for 26 years.

### It's all about sentiment

This contradiction between what's actually happening in the world's economies and what's happening in investment markets shows that the past year's events are mainly the result of people's attitudes to the market (or *sentiment*) and what they think might happen in the future. It's a normal part of the way that markets function.

Usually, a dramatic change in sentiment in one financial market, such as the share markets, can be partially offset by improved performance in another market segment, such as fixed interest. But that hasn't happened this time because sub-prime is actually a fixed interest problem. And the bursting of a bubble of excess in one place (sub-prime in the United States) doesn't usually affect the whole world. But this time, it has. In part this is because the world's banking system has been particularly hard hit by the sub-prime crisis and has had to reduce lending. This means that companies that had been dependent on borrowing money or held large amounts of debt have also been severely affected. In Australia, some companies came close to collapse when they couldn't refinance or manage their debt.

The steep rise in oil prices over the past year has come at the worst possible time, further increasing the fear and uncertainty in markets.

### What's your Fund doing?

We continue to focus on the long term and to aim for strong long-term returns for our members. Volatility in investment markets presents both a challenge to long-term investors, like you and your super Fund, and opportunities. Many good-quality assets, both shares and fixed interest investments, are now much cheaper than they were a year ago. That creates an opportunity for us to buy good assets at low prices.

We also believe that the prices of some unlisted assets that aren't so easy to buy and sell, such as direct property and infrastructure, may not yet have fully adjusted to the new financial environment, so we have reduced the Fund's holdings where possible. And we won't be committing any new money to these asset classes at present.

### Looking ahead

We don't know what the immediate future holds. But the most successful of all investment strategies has always been to buy good-quality assets at cheap prices from the scared and fearful, and that is both the Fund's main challenge and opportunity for the coming year.

### About sub-prime

US financiers gave loans to people who could not get a mortgage from traditional lenders. These were riskier loans than usual, so borrowers had to pay higher than standard rates of interest. That meant these weren't high-quality loans for the lender – they were *sub-prime*. Thousands of loans were then bundled into investment products and sold to investors – with the promise of high returns with 'no risk' for the lender, as the investment was spread across so many borrowers. Most borrowers had been given low 'honeymoon' rates for the first couple of years of the mortgage so they could afford them, but when the honeymoon rates came to an end, borrowers could not afford normal repayments and they started defaulting on their loans. Forced sales saw house prices fall and, in the United States, people can walk away from a mortgage without penalty. Suddenly a significant part of the US mortgage industry was in crisis. But the real problem was that investors lost confidence in just about all mortgages and nearly all investment products with similar structures. It was this *contagion* effect that did the real damage to markets.

### Contact us

Your Customer Service Team can help. Just call 1300 133 177, Monday to Friday, 8 am to 6 pm (EST).

### IMPORTANT INFORMATION

This information is general information only. Any recommendations, statements of opinion or financial advice have been prepared without taking account of your personal circumstances, investment objectives, financial situation and needs. You should read the relevant *Product Disclosure Statement (PDS)* and assess your own situation before you make an investment decision based on this information.

