

# Investment Update

September 2009

## The global investment cycle

Some of our recent *Investment Updates* have focused on the global financial crisis (GFC), the reasons underlying it and the outlook for recovery going forward. However, these occur as part of a larger economic cycle which moves through a series of distinct stages over time.

Here we look at how the economic cycle impacts on different types of investments and how NGS Super takes this into account when constructing and managing investment options for our members.

### The Economic Cycle

There are four main stages to the economic cycle – slow down, recession, recovery and boom – and they tend to occur in order returning to the first stage once the last has been reached.

The economic cycle tends to occur over a period of years and is influenced by a number of factors including share market performance, government policy and intervention, inflation and economic productivity (based on measures which include the unemployment rate, household income, investment spending and gross domestic product (GDP)).

Share markets and economies tend to work one place out of step with each other: share markets fall and economies follow. While the economy is heading downwards, share markets may already be starting to recover.

#### Stage 1: Slowdown (slump)

The slowdown stage involves a sustained period of decline. During this stage share markets drop in value, there are falls in the inflation rate, central banks make changes to interest rates and governments take action to try to stimulate the economy and avoid, or at least cushion, the impact of a potential recession.

Due to downward share market movements and increasing levels of volatility and uncertainty during this stage of the cycle, investors tend to seek safer, more defensive investments such as cash. This asset class is more likely to provide very small positive returns in an environment where other asset class returns are negative.

#### Stage 2: Recession

As a rule of thumb, a recession is measured by two or more quarters where GDP declines in value. Other measures that might indicate a recession are unemployment (which tends to rise) and trade (which tends to decline). A recession follows an economic slowdown and maintains some of the features of that previous stage, such as share market volatility, continuing government intervention, high unemployment and extensive economic uncertainty. Inflation tends to continue to slow as well. However, as mentioned earlier, share markets and economies work out of step with each other, so while the economy is in a recession, amid the volatility markets may be starting to show signs of emerging recovery. Such signs have been seen in Australian and global share markets since March 2009.





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During the recession stage of the cycle, asset classes such as bonds tend to provide a safe and defensive investment option with some potential growth during a time of share market volatility. Keep in mind that share markets may be starting to recover at this stage and remember that switching your investments to more defensive asset classes at this stage may mean missing out on sudden and unpredictable market improvements, as we have seen since March 2009.

### Stage 3: Recovery

Recovery follows a recession, with economic recovery starting to occur months after the share market has started to show more solid and sustained signs of growth. At this stage indicators and measures that had previously been showing more negative trends start to reverse. GDP will tend to go up over time rather than down. Inflation also starts to show an increase and there may also be some changes in employment rates.

During this stage shares tend to show significant growth which highlights the importance of making sure that you don't switch your investments around in response to negative financial market news.

### Stage 4: Boom

Over time as it becomes evident that the recovery stage is firmly entrenched, global economies stabilise and enter a period of significant growth. Inflation tends to rise, as do interest rates. GDP and employment rates improve and trade starts to stabilise and grow. Over a period of years, this growth continues to occur until it reaches a point that is unsustainable. Once this point is reached, share markets and, subsequently, economies, reach a tipping point that heralds the next market downturn and economic slowdown.

Share and property investments remain a source of strong growth over this period but investing in these asset classes becomes riskier as the boom moves toward its later and more precarious phase. Commodities and infrastructure also become important sources of investment growth in this stage as governments and private businesses start to spend more.

### What stage are we at now?

While the experience of the economic downturn in Australia was milder than that of overseas economies, we still saw the hallmarks of the slow down and recession stages of the cycle in the drop in the market and subsequent economic downturn across 2008 and early 2009. Since March 2009 share markets have shown increasingly stable signs of recovery. In recent months economic indicators are also starting to show a response to this recovery and as we move into 2010 we can expect to see the situation continuing to improve. Of course there may still be some volatility on the road to recovery.

### What does this mean for NGS Super investment options?

The NGS Super investment options are structured for the long term. We manage our asset allocation and work with our investment managers to ensure that the portfolio is best situated to meet the challenges posed by the differing economic cycles. In order to achieve the best possible performance for our members, we ensure that the risks of investing, including exposure to market and economic cycles, are managed effectively. At the same time we work hard to ensure that our members continue to receive reliable returns over the long term to ensure a comfortable future in retirement.

### Some definitions...

**Gross domestic product (GDP):** GDP refers to the total value of the goods and services a country produces per year and is based on a formula that includes factors such as consumer and government spending and the value of exports and imports.

**Inflation:** inflation refers to the price of goods and services within a given economy and the way this value changes over time. The Consumer Price Index is used as a measure of inflation.

## What if I have more questions?

Call our Customer Service Team on **1300 133 177** between 8 am and 6 pm, Monday to Friday (EST).

We're here to help you!

### Important Information

The information in this investment update is of a general nature. 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.

