

# Successful Investing



Issue 1 - 2009

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## Economic Update

Leading indicators for US growth suggest further deterioration ahead. The continued losses in the labour market are quite alarming. The latest data also suggests consumers have cut back real spending at the fastest pace in decades, while the decline in housing activity showed signs of accelerating. Interest rates look likely to be kept low for an extended period of time. President Barack Obama is expected to deliver further fiscal stimulus aimed directly at domestic demand. It is more likely to come in the form of tax cuts.

The European economy is in recession. Recent survey data suggests that further deterioration is expected in the coming quarters. The manufacturing sectors have undergone a deep retrenchment, particularly impacted by the slowdown in external demand. Domestic consumption is also slowing at an alarming rate.

In a similar situation to Europe, slowing foreign demand and stalled domestic demand have brought the economy to a halt in Japan. Leading economic indicators suggest that the economy will continue to contract in 2009.

China is becoming the most aggressive country in an attempt to stimulate its economy. The magnitude of the recent monetary and fiscal policy stimulus has overwhelmed most market observers. Economic growth is still expected to slow to 8% in 2009.

For New Zealand, consumers will start to feel poorer as house prices fall and unemployment rises. The Government has responded by announcing a number of measures. These include guarantees for banks and other approved deposit takers, provisions for massive spending including infrastructure and assistance for people made redundant. John Key has even raised the prospect of a tax payer funded bailout for ailing New Zealand companies. This, coupled with massive interest rate cuts from the RBNZ amount to an unprecedented and massive monetary easing. Notwithstanding this, recession is the consensus forecast.

Fortunately, New Zealand has room for further monetary easing via interest rate cuts. The RBNZ is of the view that we can weather this storm better than many others, and that recession may be shallower and shorter.

*Source: Aviva and Professional Investment Services (NZ) Ltd*

## Surviving the Bear Market



The past 18 months have dealt a blow to investors' confidence in the sharemarket. The sharp downturns in most equity prices has left many investors wondering whether they should reduce their exposure to equities, or sell out altogether. Fuelled by media speculation and warnings of doomsday scenarios, investors are questioning if their resilience to the bear market will be rewarded.

Yet, as we explain in this article, a bear market can be an opportune time to take advantage of deflated prices in order to further diversify your portfolio. We also provide you with some strategies to help you fend off the bear.

The most common definition of a bear market is a twenty per cent downturn in the sharemarket's value. Bear markets may occur in only portions of the market, or vary in severity and duration from one segment to the next.

### So where are we now?

The New Zealand sharemarket – as measured by the NZX 50- peaked at a record high of 4,333 in May 2007 after an outstanding four and a half year run.

How quickly can things change. For the calendar year 2008 the value of the New Zealand sharemarket dropped by 32% Correction?

Unfortunately not. What we are officially experiencing is a bear market.

### Where to now?

It's not as bad as it may first appear.

Facing a bear market is simply a natural part of the investment cycle. History shows us that on average, we experience a bear market every six or seven years.

The good news is that bear markets typically last around 15 months, and can sometimes run their course as quickly as one quarter. While there is no certainty about how long this current market will endure, there are a few strategies investors can adopt to ride out the storm.

### Quick definitions

**Correction** - A change in momentum, typically at least a 10% reversal that stops short of signalling a bull market to a bear, or vice versa. Corrections occur when investors feel the market is over or undervalued. A bull market could feature several corrections without becoming a bear market.

**Bear market** - The most common definition of a bear market is a 20% downturn in share prices.

**Recession** - A recession requires two consecutive quarters of negative economic growth as measured by the country's gross domestic product (GDP). Because GDP is a backward-looking measure, recessions aren't known until they have begun. Recessions are typically economy-wide and impact all sectors.

### Whatever you do, don't panic.

It is often only through the experience of a bear market that many investors truly develop an appreciation for the benefits of diversification.

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## What should I do?

First and foremost, don't panic. We've encountered bears before, and we'll most certainly meet them again.

There are few ways to deal with the impact of a bear market - quite similar to the way you would react if you were to run into a bear in the wild.

### 1. Remain calm. Don't panic or make sudden movements.

Veterans of previous bear markets know that the key to surviving is to act rationally, not emotionally, when making financial decisions.

Switching your investments to conservative portfolios with investment options heavily weighted to cash and bonds means that you will probably miss out on the gains when the sharemarket recovers.

History has shown that markets tend to recover just as quickly as they fall at the beginning of a bear market or correction. By switching your investments after a drop in market value, you're effectively locking in your losses by reducing your exposure to growth when the market recoups.

A look at the best 20 trading days in different markets over the past decade repeatedly shows that a high proportion of these days occur very shortly after the worst 20 trading days.

Therefore, it is difficult to be invested during the best days, and also avoid the worst days. Remember, it is impossible to time the market.

### 2. Never run from a bear.

Equity markets in the short-term are affected more by sentiment than they are by fundamentals. Prices are set by two groups - buyers and sellers - and whether they rise or fall is dependent upon whichever group holds more power at a particular time.

The key difference between fundamentals and sentiment is the speed with which they change. Economic fundamentals drive equity valuations in the long-term. Sentiment determines equity valuations in the short-term. Economic fundamentals change gradually, while sentiment can change dramatically very rapidly. This is why timing equity market is so difficult.

It is intuitively appealing to try and outrun the market, but it's like believing you can outrun an angry bear. The reality is more likely to be a mauling.

### 3. Don't just grin and bear it.

Opting not to sell equity holdings in a bear market does not mean that you should be a passive investor. On the contrary, this could be an important time for you to review your portfolio and long-term investment objectives to ensure the two are inline.



A prudent bear market strategy involves taking advantage of depressed prices to create a well-diversified portfolio; one that minimises risk and maximises the potential for returns when the market begins to rise again.

It is often only through the experience of a bear market that investors truly develop an appreciation for the benefits of diversification.

### 4. Prevent bear attacks.

**Wear protective gear:** When travelling in bear country, be prepared. A sound, well-diversified portfolio with a long-term focus will help protect you from bear attacks.

Surviving a bear market requires all your discipline and determination. You must follow through your long-term investment strategy despite market volatility. When the bear is breathing down your neck, the key to survival is staying calm.

### 5. Keep it in perspective. He's not that big and scary.

While being attacked by a bear in the wild is certainly something you could have bragging rights to with your mates, experiencing a bear market shouldn't be such a big event for the long-term investor. By looking at history, you should understand that a bear market - or any correction for that matter - is just a part of the topsy-turvy world of investing.

Twenty percent-plus falls in sharemarkets have been rare in recent years but are not that unusual in a long-term context.

Unfortunately further falls cannot be ruled out, and as shown, it sometimes takes a while to regain previous highs. Generally, such falls in sharemarkets are usually followed by a strong rally over the subsequent year.

Keep in mind that the markets always recover. Over the medium to long-term, despite the sometimes frequent ups and downs, equity investments always return a positive result.

### 6. Bears can be slow-moving creatures; give him time to move on.

Regardless of a down market's length, it can take longer for a market to recover to previous levels. This is because the market must rise further than it originally fell in order to breakeven.

Recovery takes longer if you don't participate in the whole market swing.

Remember, paper losses don't become real until you make the choice to sell. However, if you invest through the market cycle - that is, buying low - returns as markets reclaim their previous levels can excel the recovery of paper losses.

### Conclusion

Over the last 50 years there have been numerous examples of sharemarkets falling by 20% or more, but these are in the context of a long-term trend which remains up, with shares providing better long-term returns than most other assets.

As such, investing in shares should be seen as a long-term plan.

While there may well be further weakness ahead, trying to time the bottom is impossible so the best approach for long-term investors is to sit tight.

## Surviving the bear

### Remain focused in the long-term

Despite short-term volatility, successful investors should follow through with their long-term strategy in order to survive the bear.

### Don't let fear guide your investment decisions

Act rationally and resist the emotional aspects of investing. Basing your decisions on fear and panic won't do you any good in the long-term.

### Diversify to soften the blow

It's critical to have a well-diversified and well-positioned portfolio to help cushion the impact of a sharp market downturn.

### Never try to time the market

Keep in mind that sentiment drives the market; and it can recover at any time.

### Stay invested

Don't miss your opportunity for financial gains by removing yourself from the market. You have to be in it to win it.

### Seek advice

Your financial adviser is there to help you weather the storm and stay on track.

Please speak with your financial adviser for more information.

Source: Russell Investments.

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## What does orange mean?

The next of the 'Many Colours of Professional Investment Services' to feature is Orange, chosen for its ability to stimulate ambition with energetic activity.

Orange is a visual vitamin that speeds up growth and allows for the development of a healthy and active mind.

Orange is also a great pick-me up colour, and can help you organise your goals and use energy constructively to be focused and productive. It is the perfect colour for assisting you to implement and concentrate on the personal strategies made with your financial adviser to achieve your financial goals in 2009 and beyond.

# From Little Things, Big Things Grow



With the state of investment markets being what they are, investing more of our money now is perhaps one of the furthest things from our minds.

Many of us have heard stories about the benefits of dollar cost averaging and compound interest. That is, building wealth for the long-term by investing small amounts on a regular basis. Of course, it was Albert Einstein who is attributed with having said "the most powerful force in the universe is compound interest".

I was recently reminded of a story of a successful accounting practice that had a large number of individual clients for whom they prepared annual tax returns. Rather than simply preparing tax returns, the principals of the firm decided they would turn their tax clients into investors.

When a client came into the office to have their tax return prepared, when clients received a tax refund, and when new clients visited the office for an interview, they were reminded of the benefits that could be achieved by establishing a regular investment plan. In fact, clients could establish a regular investment plan with as little as \$25 per week (two pizzas, garlic bread, and a bottle of soft drink). Clients could increase their monthly commitment at any time, or could reduce it if circumstances changed. They were not locked into a contractual arrangement.

Over time, many clients of the accounting practice participated in this program with quite a number increasing their regular savings commitment when they received a salary rise or a tax cut. The regular savings were channelled into a well managed diversified investment fund that gave exposure to a range of asset classes including cash, fixed interest securities, property and shares.

This simple strategy gave clients access to two of the great investment principles, dollar cost averaging and compound interest.

One of the advantages of a regular investment program is that once we set up an automatic facility to divert a regular amount from our bank account or salary, we adjust our spending habits accordingly and, after a couple of weeks, we don't miss the amount being saved.

The benefit of a regular investment program is that you don't need to have a large amount of money to start. A number of fund managers have plans available that can be commenced with as little as \$1,000 and regular contributions of \$100 per month.

Speak to your financial adviser today about starting a regular investment plan. With markets being in a depressed state, the opportunity to get in "on the ground floor" has never been better.

*Source: Peter Kelly - Professional Investment Services*

## Legislative Amendments

*Effective 1st April 2009*

New legislation was enacted for KiwiSaver in December. The changes take effect from 1st April 2009.

The Government is committed to keeping KiwiSaver and making it enduring and affordable for members, employers, and taxpayers. The Government believes that the necessary major changes have been made to ensure the scheme is sustainable and affordable, and will therefore leave the basic architecture of the scheme unchanged.

The main features of KiwiSaver are outlined below

### No changes to these KiwiSaver provisions

- The member tax credit of up to \$20 a week will not change.
- The kick-start payment of \$1000 will not change.
- The mortgage diversion and the first-home deposit subsidy and withdrawal provisions will not change, although Housing New Zealand still require member contributions of 4% to be eligible for the first home subsidy.

### Changes to KiwiSaver

- The minimum member contributions rate will be reduced to 2% down from 4%. The 2% will become the new default rate for new members from 1st April 2009.
- The fee subsidy of \$40 per annum will not apply to members joining after 1st April 2009, and will cease to be paid for other members after one or two further payments.
- Compulsory employer contributions will be capped at 2% from 1st April 2009.
- The employer tax credit will be discontinued from 1st April 2009.
- The exemption from Employers Superannuation Contribution Tax (ESCT) will be capped at the compulsory Employer Contribution of 2% from 1st April 2009 (previously 4%). ESCT will be deducted at 33% on Employer Contributions above 2%, unless your employer has selected to deduct ESCT at the reducing rate for lower paid employees.
- The KiwiSaver Act has been amended to make it clear that no employee can have their gross pay reduced as a result of employer contributions. This will ensure that KiwiSaver contributions from employers are a genuine addition to existing pay.

*Source: [www.kiwisaver.govt.nz](http://www.kiwisaver.govt.nz)  
14th February 2009, issued by the Trustees of the AonSaver KiwiSaver scheme.*

For more information, contact your PIS (NZ) financial adviser today.

# Trivia

Money isn't made out of paper; it's made out of linen.

At the height of its power, in 400 BC, the Greek city of Sparta had 25,000 citizens and 500,000 slaves.

Every person has a unique tongue print.

After spending hours working at a computer display, look at a blank piece of white paper. It will probably appear pink.

You share your birthday with at least nine million other people around the world.

The coldest temperature ever measured on Earth was -129 Fahrenheit (-89 Celsius) at Vostok, Antarctica, on July 21st 1983.

All gondolas in Venice must be painted black, unless they belong to a high official.

Caffeine is on the International Olympic Committee's list of prohibited substances. Athletes who test positive for more than 12 micrograms of caffeine per millilitre of urine may be banned from the Olympic Games. This level may be reached after drinking about five cups of coffee.

The Arctic Tern (*Sterna paradisaea*) may be a small bird, but it undertakes the world's longest migration each year when it travels almost from pole to pole. After breeding in the Arctic Circle, these birds migrate during the Northern Hemisphere winter to the border of the Antarctic ice pack. The round trip migration is almost equal to flying all the way around the earth - totalling approximately 35,000 kilometres.

Banana plants are the largest plants on earth without a woody stem. They are actually giant herbs of the same family as lilies, orchids and palms.

Colgate claims "Tooth Fairy" as a registered trademark.

The honeybee kills more people world-wide than all the poisonous snakes combined.

Great Britain was the first country to issue postage stamps. Hence, the postage stamps of Britain are the only stamps in the world not to bear the name of the country of origin.

Sources:

[www.corsinet.com/trivia/](http://www.corsinet.com/trivia/) and [www.funfunnyfacts.com](http://www.funfunnyfacts.com)

# Insuring your Key People



**Building up your business into what it is today has probably taken many years, lots of hard work, and no doubt quite a few risks along the way.**

You certainly wouldn't want to jeopardise the business in any way. You could be doing just that if you have not taken adequate steps to secure its future operation.

What would happen to your business, for example, if you or a partner in the business died suddenly, suffered a trauma or became permanently disabled?

You may have insured your individual situation with life insurance to help protect your family's lifestyle on your death or incapacitation, but it is also important to consider things in a business context.

In most businesses, beyond the physical equipment and machinery, it is the employees who ultimately keep things running. A senior employee, such as a manager, director or sales executive, may be considered a key person. These people are critical to whether or not a company makes a profit.

So if something was to happen to that key person in the business, you as the other owner may be left with a business without someone there to bring in the income. You may want to offset that risk by insuring the key person and providing a lump sum injection into the business to help during the transition/replacement phase.

## What is key person insurance?

Key person insurance involves the taking out of insurance on the lives of the people whose loss would cause your business to suffer.

Should your key person die, become disabled or suffer from a serious trauma, a lump sum benefit

would be paid to the business. In this way, key person insurance helps protect your business from the impact that the loss of this key person would have.

Without key person insurance, a business may suffer from the potential loss of key clients, reduced business growth and development, and the loss of goodwill. Furthermore, the business will need to replace the key employee and most likely have to train the replacement.

## Features of key person insurance

Key person insurance will help protect a business by paying a benefit to compensate for loss of production and subsequent loss of revenue. The benefit will also give the business funding to find and train a suitable replacement without it losing financially from the loss of a key person.

To begin the process, the business should identify its key personnel. It is then important to estimate each key person's net worth to the business by considering how much the effect of losing each person would cost the business financially.

The owner should then take out life, disability and/or trauma insurance to protect the business from the impact of losing key personnel. The sum insured will be determined by the estimation of each key person's net worth to the business.

Premiums are paid by the business and if a claim is accepted on your plan for the event that you have insured, your business will be paid a benefit in accordance with the sum insured.

Issued by Aviva (Aviva Australia Holdings Ltd ABN 38 095 045 784 and its related companies and entities)

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Source: Aviva

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