Enduring investment principles

A long-term perspective combined with a watchful eye on how market risk can impact your personal investment objectives are two of the key messages that can be taken from Vanguard's 2010 Index Chart that tracks the performance history of financial markets over the past 30 years.

Past performance is not a reliable indicator of future returns however this long-term view of market returns does provide a useful context for investors and highlights the value of taking a truly long-term approach.

As well as outlining the investment performance of major asset classes, the 2010 Index Chart signposts key economic, social, political and demographic changes. Looking at investment markets over a 30 year period offers insight into key investing principles – namely the value of diversification, understanding risk and taking a long-term view.

These key principles have stood the test of time – and numerous market tests - including the global financial crisis.

1. Take a long-term approach

Allowing emotions to drive investment decisions - be it overconfidence in rising markets or fear in falling markets – rarely serves investors well. Successful investors ignore the short-term emotions of markets and take a long-term approach to investing. History shows that long-term investors have been rewarded for being patient and disciplined around rebalancing portfolios back to target asset allocation settings.

2. Understand market risk

Vanguard's Index Chart shows that over the past 30 years positive returns have outweighed negative returns across all major asset classes. For example, since 1980 Australian shares have delivered positive returns in 24 out of 30 financial years, returning an average annual return of 11.1 per cent to June 2010. That provides a comforting historical context without any guarantee it will be repeated in the future. For investors long-term objectives are arguably a more critical driver in determining how much market risk the portfolio is exposed to.

For example, being 100 per cent invested in Australian shares over that time carries 100 per cent market risk and there have been periods – most recently in 2008 - of extreme volatility when the market value plunged 51.4 per cent, dramatically exposing that risk. It is one of the key reasons Vanguard advocates diversification across (as well as within) asset classes.

Some investors find the notion of trying to time markets alluring. However, getting the timing right is extremely difficult and having money on the side lines and trying to anticipate when markets will rebound can often mean missing out on the strong return periods as we saw in 2009.

For instance, if an investor missed the best 10 Australian share market trading days between 1980 and 2010 (that's 10 trading days out of 7,588) they would have earned returns of 9.1 per cent p.a. compared with 11.1 per cent p.a. for those who stayed fully invested, thereby reducing the final value of their investment by $100,164 or 42.4 per cent.

3. Maintain portfolio diversification

Investing across asset classes provides exposure to market growth opportunities while reducing portfolio risk. Having a portfolio which holds a broad range of asset classes, sectors and securities ensures that you are well positioned to capture market growth while helping to moderate return volatility over time. Ultimately no one can predict the future, which is why investing based on short-term performance can be a dangerous strategy compared to taking a diversified long-term approach.

It is also why Vanguard believes that the asset allocation decision is one of the most important decisions that investors (and their advisers) make.

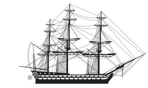
History of market recoveries

The table below shows the extent to which the Australian share market has recovered from a significant event or crisis. On average, the Australian share market has fallen around -25.5 per cent after a crisis event, but invariably recovered in the proceeding 12 month period. This highlights the volatile nature of share market investing and how periods of negative returns occur, but typically recover over time.

Event	Event start date	Duration	Post-event market low	Following 12 month performance
Stock Market Crash	19 October 1987 (Black Monday)	23 days	-46.0%	41.0%
First Gulf War in Iraq	2 August 1990	167 days	-21.8%	44.7%
Asian Financial Crisis	1 July 1997	119 days	-14.7%	15.2%
U.S. Terrorist Attacks	11 September 2001	13 days	-9.7%	8.0%
Lehman Brothers Collapse	15 September 2008	172 days	-35.4%	59.6%
Average fall				**-25.5%**
Average duration				**99 days**
Average 12 month recovery				**33.7%**

Taking a long-term perspective

Market returns - 1 July 1980 to 30 June 2010



Vanguard INVESTMENTS®

PM - Australia: Fraser | Hawke | Keating | Howard | Rudd | Gillard

Pres. - U.S.A.: Carter | Reagan | Bush | Clinton | Bush | Obama

Labor · Liberal · Democrat · Republican

80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 00 01 02 03 04 05 06 07 08 09 10

$500,000 · $100,000 · $10,000

Australia's population 14,807,400
Gold peaks US$850
First CMT established
IBM PC introduced
Ash Wednesday bushfires
Australia II wins Americas Cup
Medicare introduced
Banking industry deregulated
A$ floated on int'l market
Capital Gains Tax introduced
EFTPOS introduced
"Banana Republic"
Fringe Benefits tax introduced
Stock Market Crash
Berlin Wall torn down
Bond Corp collapse
Iraq invades Kuwait
Commonwealth Bank float
Mabo
Superannuation Guarantee introduced
Woolworths float
Netscape Navigator launched
QANTAS float
Asian currency crisis
Telstra float
AMP float
ASX float
Republic referendum
GST introduced
Terrorist attacks in US
Bali bombing
Second Iraq War
Boxing Day tsunami
US subprime crisis
Australia's population 22,384,600
Lehman Brothers collapse

$284,304 *11.8% p.a.*
$234,319 *11.1% p.a.*
$184,681 *10.2% p.a.*
$183,518 *10.2% p.a.*
$178,614 *10.1% p.a.*
$145,040 *9.3% p.a.*
$36,617 *4.4% p.a.*

Growth of $10,000
with no acquisition costs or taxes, & all income reinvested

Percentage Returns at 30 June 2010[1]

	1 Year	5 Year	10 Year	20 Year	30 Year
Australian Shares[2]	12.8%	4.5%	7.0%	9.7%	11.1%
International Shares[3]	5.2%	-2.2%	-4.6%	4.9%	10.1%
US Shares[4]	8.9%	-2.9%	-5.0%	7.3%	11.8%
Australian Bonds[5]	7.6%	6.0%	6.3%	8.8%	10.2%
Listed Property[6]	20.4%	-8.0%	3.0%	7.1%	10.2%
Cash[7]	3.9%	5.8%	5.5%	6.3%	9.3%
CPI[8]	3.1%	3.0%	3.2%	2.6%	4.4%

Australian Recessions[9]

Interest Rate[10]

20% · 15% · 10% · 5% · 0%

Compound Annual Rate of Inflation by Decade: 8.3% · 2.3% · 3.2%

Inflation[11]

15% · 10% · 5% · 0%

Avg Weekly Earnings $208 · Avg Weekly Earnings $462 · Avg Weekly Earnings $622 · Avg Weekly Earnings $938

A$/US$ Exchange Rate

US$1.25 · US$1.00 · US$0.75 · US$0.50

Sources: Australian Bureau of Statistics, ASX Limited, Melbourne Institute of Applied Economic & Social Research, Commonwealth Bank of Australia, MSCI Barra, Reserve Bank of Australia, Standard & Poors, Thompson Reuters, UBS AG Australia Branch. **Notes:** 1. One-year returns are total returns from 1 July 2009 to 30 June 2010. Five, ten, twenty and fifty-year returns are average annual compound returns to 30 June 2010. 2. S&P/ASX All Ordinaries Accumulation Index. 3. MSCI World ex-Australia Net Total Return Index. 4. S&P500 Total Return Index. 5. Prior to December 1989 the index is the Commonwealth Bank All Series Greater Than 10 years Bond Accumulation Index. From September 1989 the index is the UBS Composite Bond Accumulation Index. 6. S&P/ASX Listed Property Trust Accumulation Index. 7. Data prior to March 1987 supplied by Reserve Bank of Australia. From March 1987 the index is the UBS Bank Bill Accumulation Index. 8. ABS Consumer Price Index. 9. Recessions as defined by the Melbourne Institute of Applied Economic and Social Research. 10. Interest Rate prior to July 1981 is a short-term Government Bond rate. From July 1981 the interest rate is the Reserve Bank of Australia's Official Cash Rate. 11. Annualised Rate of Inflation. All figures are in Australian dollars.

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Balancing risk and return

Diversifying across asset classes helps to reduce volatility and smooth out returns over time. While this strategy cannot protect you against negative returns, it can reduce the impact of poorly performing asset classes.

Asset classes perform at different times and can have inverse relationships. Holding a diversified portfolio reduces market volatility as returns from better performing investments help offset underperforming ones.

While investment market returns can be volatile over shorter time periods, long-term average returns have remained strong. This reinforces the importance of staying the course and sticking to your strategy despite short-term setbacks.

Financial Year Total Returns for the Major Asset Classes

Best Worst

	Australian Shares	International Shares	International Shares (Hedged)	US Shares	Australian Bonds	International Bonds (Hedged)	Cash	Australian Listed Property	International Listed Property
1981	15.8%	13.0%	20.4%	21.6%	2.3%		14.1%	24.6%	
1982	-29.0%	-4.0%	-10.4%	-0.6%	-5.1%		18.1%	3.6%	
1983	34.7%	72.7%	49.6%	88.4%	25.6%		15.5%	23.7%	
1984	13.5%	2.3%	2.0%	-3.2%	21.4%		12.6%	35.3%	
1985	36.5%	61.6%	29.9%	69.5%	17.0%		14.0%	11.8%	
1986	42.5%	55.2%	34.5%	33.5%	20.5%	29.2%	18.3%	23.8%	
1987	54.0%	32.6%	33.2%	17.7%	12.1%	17.6%	17.3%	41.3%	
1988	-8.6%	-10.0%	-5.3%	-15.5%	19.4%	12.5%	12.5%	-2.8%	
1989	3.5%	18.1%	18.3%	26.7%	3.0%	16.3%	15.7%	-1.1%	
1990	4.1%	1.9%	5.3%	11.5%	17.8%	13.1%	18.5%	15.2%	
1991	5.9%	-2.0%	-5.8%	10.3%	22.4%	15.3%	13.5%	7.7%	-15.9%
1992	13.3%	7.1%	-3.0%	16.3%	22.0%	15.8%	9.0%	14.7%	6.9%
1993	9.9%	31.8%	17.3%	26.6%	13.9%	14.7%	5.9%	17.1%	28.3%
1994	18.5%	0.0%	6.7%	-6.5%	-1.1%	2.1%	4.9%	9.8%	8.4%
1995	5.7%	14.2%	3.7%	30.0%	11.9%	13.1%	7.1%	7.9%	7.5%
1996	15.8%	6.7%	27.7%	12.9%	9.5%	11.2%	7.8%	3.6%	2.4%
1997	26.6%	28.6%	26.0%	42.6%	16.8%	12.1%	6.8%	28.5%	35.7%
1998	1.6%	42.2%	22.1%	58.2%	10.9%	11.0%	5.1%	10.0%	25.0%
1999	15.3%	8.2%	15.9%	14.2%	3.3%	5.5%	5.0%	4.3%	-6.8%
2000	13.7%	23.8%	12.6%	18.2%	6.2%	5.0%	5.6%	12.1%	14.1%
2001	8.8%	-6.0%	-16.0%	0.5%	7.4%	9.0%	6.1%	14.1%	38.2%
2002	-4.5%	-23.5%	-19.3%	-26.3%	6.2%	8.0%	4.7%	15.5%	7.5%
2003	-1.1%	-18.5%	-6.2%	-15.2%	9.8%	12.2%	5.0%	12.1%	-5.2%
2004	22.4%	19.4%	20.2%	15.4%	2.3%	3.5%	5.3%	17.2%	28.7%
2005	24.7%	0.1%	9.8%	-4.1%	7.8%	12.3%	5.6%	18.1%	21.2%
2006	24.2%	19.9%	15.0%	11.6%	3.4%	1.2%	5.8%	18.0%	24.2%
2007	30.3%	7.8%	21.4%	5.6%	4.0%	5.2%	6.4%	25.9%	3.0%
2008	-12.1%	-21.3%	-15.7%	-23.4%	4.4%	8.7%	7.4%	-36.3%	-28.6%
2009	-22.1%	-16.3%	-26.6%	-12.5%	10.8%	11.5%	5.5%	-42.3%	-31.2%
2010	13.8%	5.2%	11.5%	8.9%	7.6%	9.3%	3.9%	20.4%	31.3%
Best	**54.0%** (4)	**72.7%** (3)	**49.6%** (2)	**88.4%**(6)	**25.6%** (3)	**29.2%** (3)	**18.5%** (2)	**41.3%** (3)	**38.2%** (4)
Worst	**-29.0%** (2)	**-23.5%** (2)	**-26.6%** (3)	**-26.3%** (5)	**-5.1%** (3)	**1.2%** (2)	**3.9%** (5)	**-42.3%** (4)	**-31.2%** (4)

(X) denotes the number of times each asset class was the best/worst performer during a financial year between 1981 and 2010.
Note: For the sources used in the table above, please refer to source notes on previous pages. Assumes 100% reinvestment of distributions. Returns shown are before fees and taxes.