

When patience is a virtue

As an investor it has been a rough 12 months in the sharemarket. Returns delivered over this year to 30 October 2008 were a disappointing -38.3 per cent, as measured by the S&P/ASX 300 Accumulation Index. These results remind us just how volatile markets can be in the short term.

The current market volatility is nothing unusual, when compared to historical data. Since 1987, the fluctuations in annual financial year returns for the Australian sharemarket (S&P/ASX All Ordinaries Index) have ranged from 54 per cent in 1987 to -12.1 per cent in 2008.

Bear markets in Australian shares since 1960

If history is anything to go by the sharemarket will turn around and exceed past highs. As the table below shows, on average, bear markets in Australia took 15 months to low, with the market falling an average of 34 per cent. The table also shows it takes on average 41 months to make a new high after a low, with the percentage gain in the first 12 months after the low being (on average) 32 per cent. If this is anything to go by then hopefully this means that the worst is nearly over.

Share bear markets in Australian shares	Months to low	% fall	Months after low to make new high	% gain in first 12 months after low
Sep 60 – Nov 60	2	-23.2	33	+12
Feb 64 – Jun 65	16	-20.4	25	+9
Jan 70 – Nov 71	22	-39.0	94	+52
Jan 73 – Sep 74	20	-59.3	59	+51
Nov 80 – Jul 82	20	-40.6	17	+39
Sep 87 – Nov 87	2	-50.1	75	+35
Aug 89 – Jan 91	15	-32.4	30	+39
Feb 94 – Feb 95	12	-21.7	20	+25
Mar 02 – Mar 03	12	-22.3	15	+27
Average	15	-34	41	+32
Nov 07 - ?	13	-49.5*	?	?

Source: AMP Capital Investors

*All Ordinaries Index: 1/11/2007 - 6853.6 (all time high), 4/12/2008 - 3468.1. Source: Stock Doctor® and www.asx.com.au.

Prior to the financial crises, the Australian sharemarket enjoyed a period of low volatility and above average returns – delivering four consecutive years of 20 per cent plus returns (2004 to 2007 financial years).

But with all of these statistics and volatility – it is important to remember that overall the sharemarket continues to climb in an upward trend. Since 1900, Australian shares have delivered a total return (capital growth plus dividends) of 12.4 per cent a year on average¹.

So with this information at hand some of you may be asking what do I do next?

Stay vigilant and committed to your long term strategy.

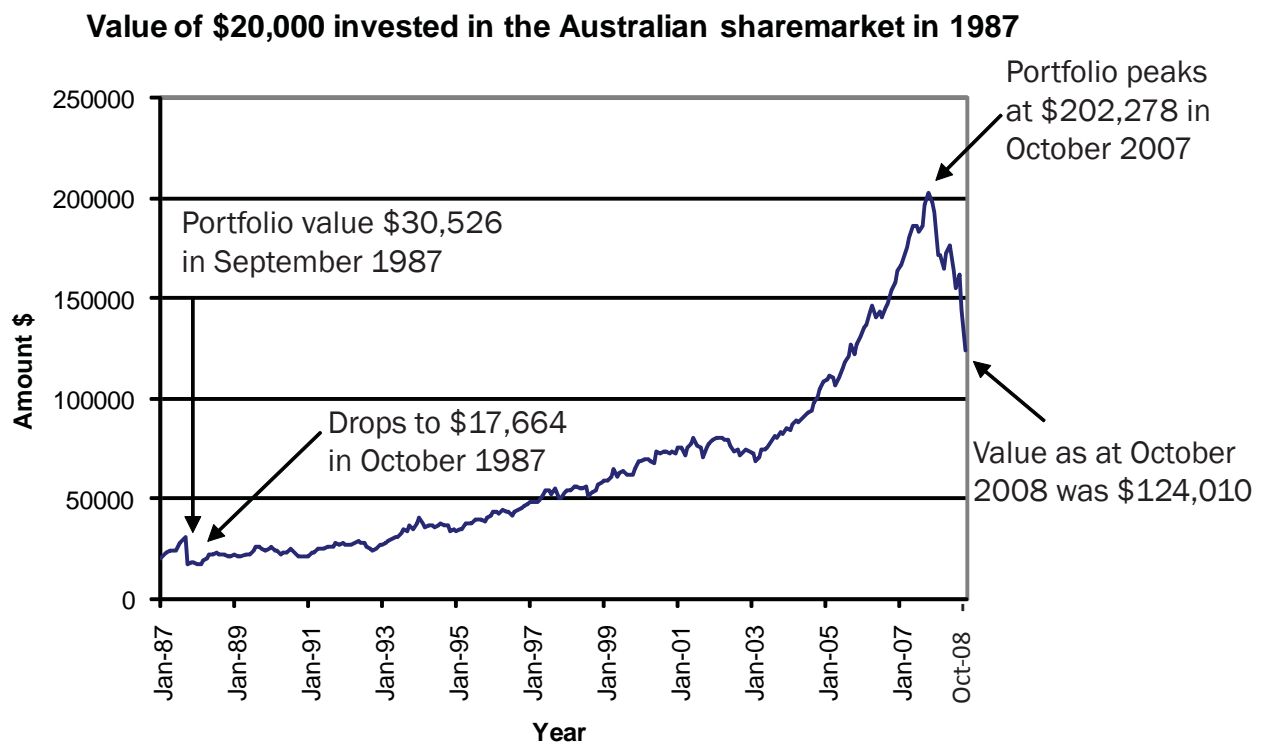
Long-term investors reap the rewards

While it can be challenging to stay focused on your investment strategy when markets are fluctuating, abandoning it can be costly. Selling shares in a falling market not only cements losses, but increases your risk of being out of the market when it rebounds.

In October 1987, the ASX All Ordinaries Index dropped by 42 per cent over a month. Many investors panicked and decided to flee the market. Investors who stayed the course during the 1987 stock market crash and rode out the market volatility fared much better over the longer term than those who retreated.

The graph below shows the value of a \$20,000 investment portfolio since January 1987. After enjoying eight months of exceptional returns this investor's portfolio value fell from \$30,526 to \$17,664 in October 1987.

However this investor had a long term strategy and even though it took more than five years for their portfolio to recover to its pre-October 1987 level, the strategy has paid off. After reaching a peak of \$202,278 in October 2007, the portfolio as at October 2008 was worth \$124,010, representing a compounded annual year growth rate (CAGR) of 8.71 per cent p.a. since inception.



Example based on All Ords returns

Quality not quantity

Often investing in a select portfolio of high quality, financially healthy stocks can prove superior to following the herd, and investing in stocks just because everyone else is.

This Lincoln Australian Share Fund² (the 'Fund') doesn't include stocks in the portfolio just because they form part of the index – only companies judged financially healthy earn a place in the portfolio.

At the core of the Fund's stock selection process is Lincoln's unique Financial Health analysis methodology. Developed in 1982 by Dr. Merv Lincoln, the Financial Health model has proven itself over the last 20 plus years. By combining financial health assessment, key accounting ratios and other quantitative and qualitative measures, our methodology aims to identify companies with the best long-term growth prospects.

Esteemed economist associate Professor Neville Norman says: "It's in the nature of equity investments that there will be fraud and there will be recent events that no model or combination of data will ever capture. But the two outstanding characteristics of the Lincoln health score model are first of all, that it is based on research, not just feelings and inclinations, and secondly, that research is wrapped up into a model".

Professor Norman believes this results in a numerically consistent and objective basis for stock selection decisions.

Onwards and upwards

Some of the recent volatility is based on irrationality and fear rather than fundamentals, but fundamentals are what really drives markets over the long term. There are some very financially sound, high quality companies out there at valuations lower than their fundamentals suggest.

Now is the time to stay vigilant and as history shows, having a long term investment strategy in high quality, financially healthy stocks can be rewarding.

Like to know more?

To find out more about the Lincoln Australian Share Fund and our long-term approach to investing please call Ben McGrath, Managed Investments Team on **1300 676 332**.

1 The Australian, 'Climbing back: checking for signs of a market recovery', James Dunn, 15 October 2008

2 The underlying investment portfolio for the Lincoln Wholesale and Retail Australian Share Funds

Important information: This information is issued by Lincoln Indicators Pty Ltd.

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