

## SPECIAL EDITION

We trust our Clients will find this Special Edition informative and interesting.

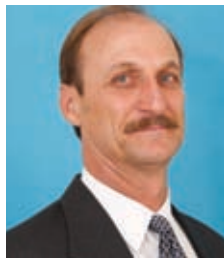
The current turbulence in international markets underlines the need for investors to seek out quality financial advice. Clients who stick to a well designed robust strategy, rather than overreacting to market events, are far more likely to achieve their long term financial goals.

History shows the folly of investors trying to time their movement in and out of the market.

I encourage you to speak to your Fiducian Financial Adviser should you have any questions about this Special Edition.

**Alan Hinde**  
Head of Financial Planning

## AN INTERVIEW WITH FIDUCIAN'S INVESTMENT MANAGER



**Conrad Burge**  
Investment Manager, Fiducian Portfolio Services

We asked Conrad Burge to share his musings on what has been a difficult year for investors in this Special Edition. In addition, Conrad's in-depth analysis in the Fiducian Quarterly Investment Strategy Report is available through your Adviser.

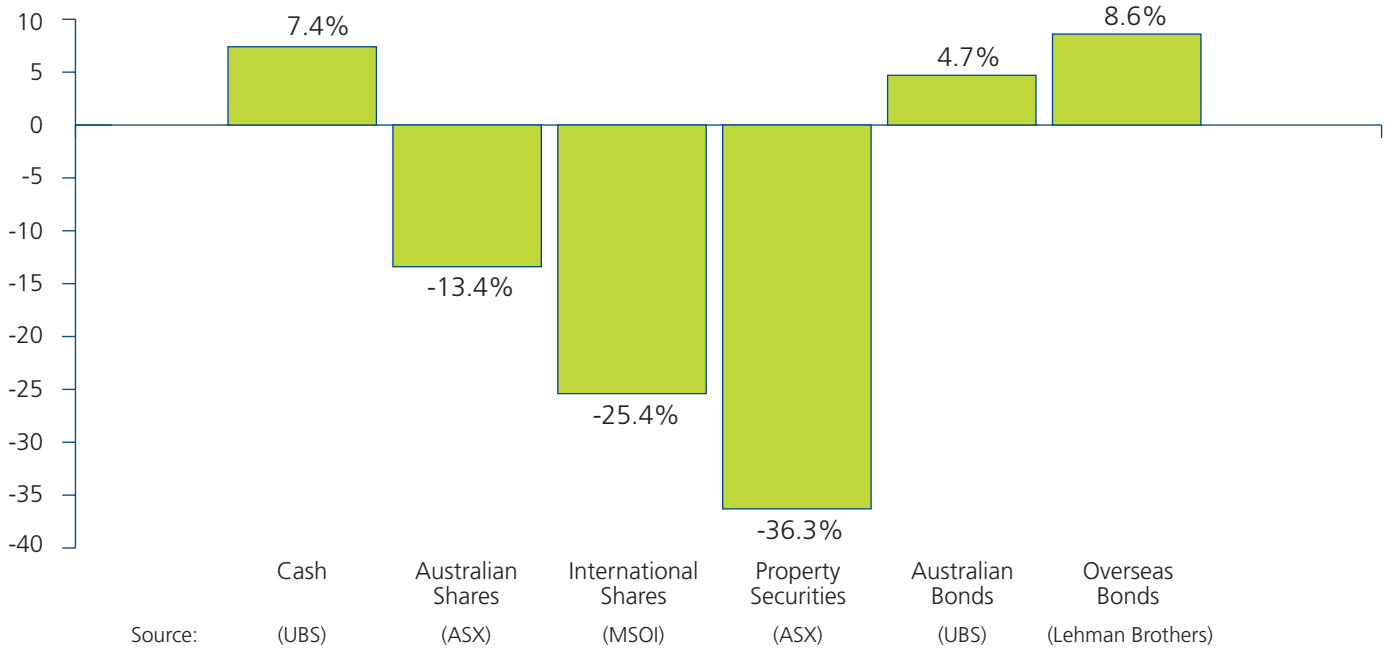
### **Q: Why are Balanced Funds showing negative returns this year?**

### **A: Share and Listed Property Markets have been weak.**

From time to time balanced funds do not perform well. In fact, our Investment Strategy Planner indicates that investors should expect balanced funds to give negative returns in 1 out of every 7 years. Even capital stable funds, which have a relatively low exposure to growth assets, can provide negative returns at times. This is because diversified funds have exposure to shares and other so-called 'growth' assets, including listed property securities. For balanced funds, exposure to growth assets is usually reasonably high (around 70%). Shares and other growth assets tend to have higher volatility than more 'defensive' assets,

in that they can have strong moves either up or down at various times. Over the 2007-08 financial year just passed, the Australian share market index fell by over 13%, while international markets fell even more heavily and the listed property index fell the most, sliding by around 36% over the year. Positive returns by defensive sectors, including bonds (fixed interest) and cash were not enough to offset the declines in the equity markets. The following graph shows the index performance over the financial year of various asset sectors, all of which are usually included in balanced funds:

### Asset Class Performance 2007-2008



### Q: What sectors were winners and losers during the year?

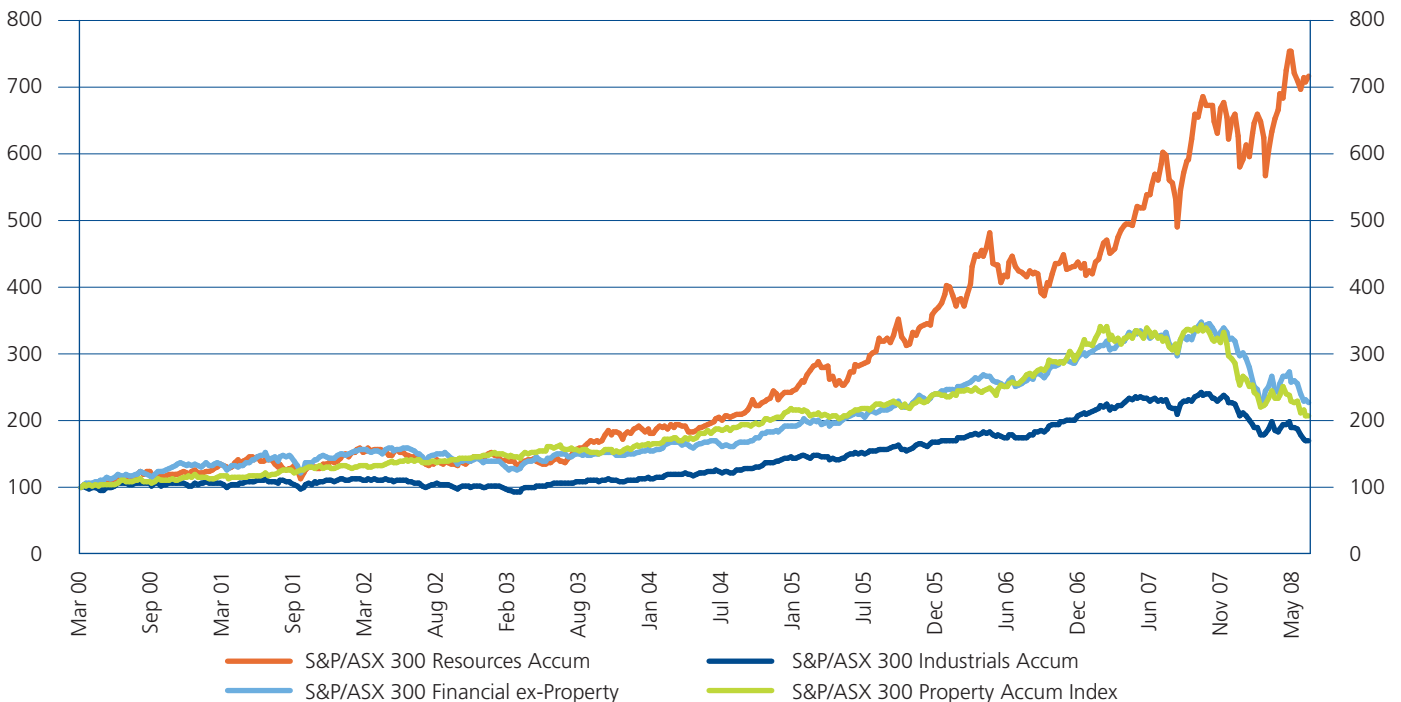
### A: Resources have done well, while listed property has fallen heavily.

While the share market as a whole has been performing poorly lately, there has been one sector that has been doing extremely well, namely the resources sector. The graph below highlights the

out-performance of the resources sector over the past 8 years, compared with the financials sector (banks, insurance companies and other 'financially' related stocks), the industrials sector and the

listed property sector. Fiducian's Australian Shares Fund is well represented in the resources sector through the stock selections of its underlying managers.

### Resources, Industrials and Financials Relative Stock Performance March 2000 – June 2008



## Q: Is there any good news?

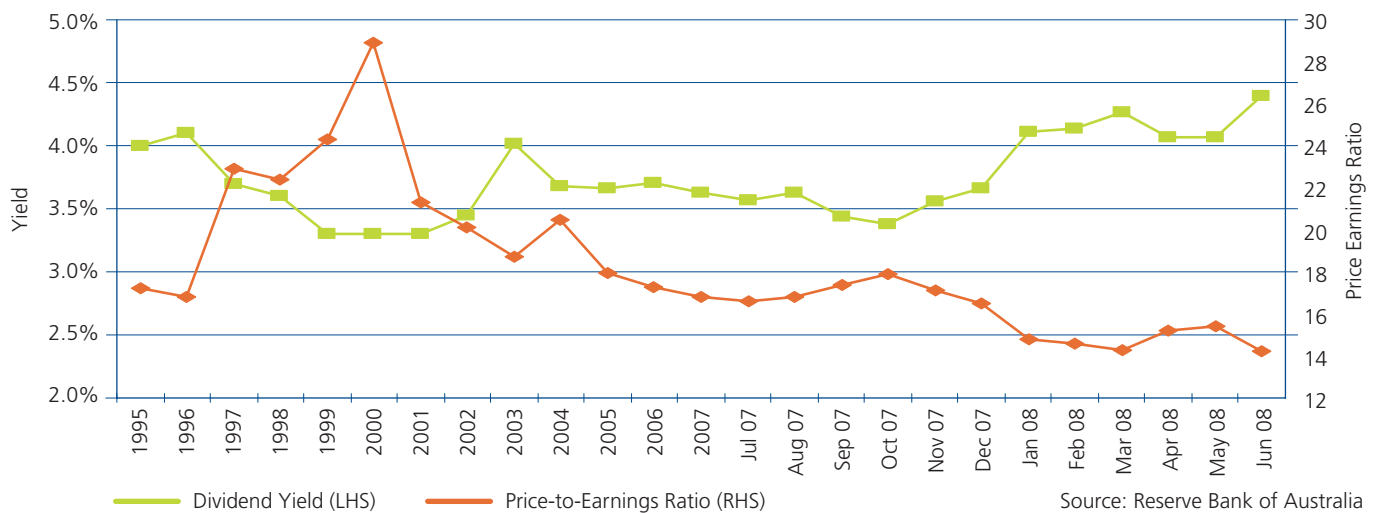
### A: Share and Listed Property Markets now appear to be fair value.

Following their contraction over the past year, equity and listed property markets now appear to be fairly priced. Some valuation parameters, such as the price-to-earnings ratio (PER) illustrate this. For example, at end-June, the Australian share market's PER was around 14.3 (Reserve Bank data for trailing earnings). This ratio is well below its long-run average and below any ratio for the market in at least

the last decade. Similarly, the market's average dividend yield was around 4.4% for June, the highest since the market's last trough in early 2003. Valuation parameters for the listed property securities sector also appear attractive, with an average forward dividend yield for the large cap listed property sector (as at 30 June 2008) of nearly 10% (Phoenix Portfolios data) and even higher for the small cap sector.

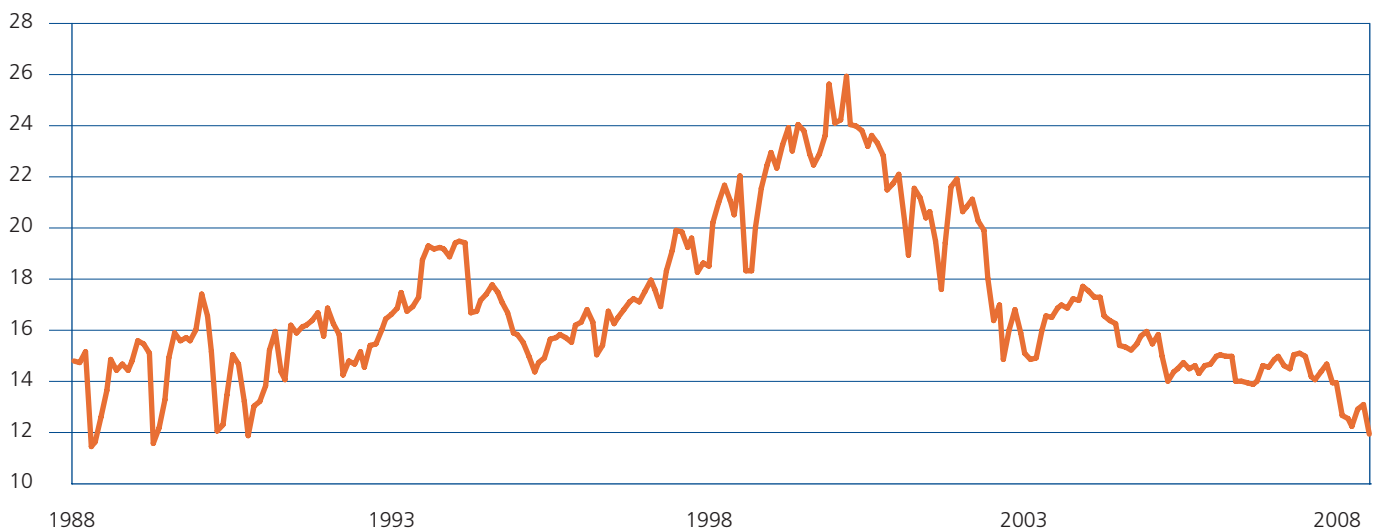
These securities are also mostly trading at an (average discount of around 38%, Phoenix Portfolios data) to net tangible assets which is well below the perceived value of the underlying properties. The following graph illustrates the movement in both the PER and the dividend yield for the Australian share market since 1995, emphasising the relatively good value now evident in the domestic market:

**Australian Share Market Price-to-Earnings Ratio and Dividend Yield (1995 to 30 June 2008)**



The graph below shows that the average PER for the global share market is also currently at historical lows since the 1980's:

**MSCI World Forward Price-to-Earnings Ratio (31 January 1988 – 30 June 2008)**

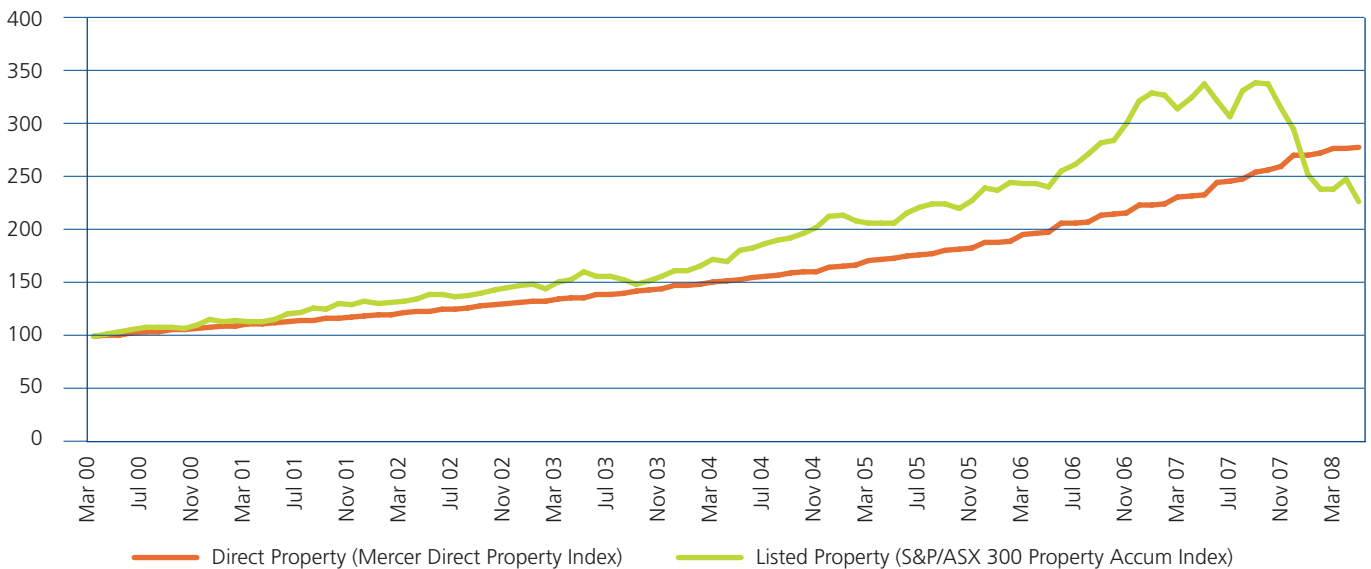


The graph below illustrates how the listed property sector has fallen compared with the unlisted property sector (also known as direct property). Direct property has not fallen much this year yet because it is only occasionally revalued (sometimes only once per year or even once every three

years). Fiducian has always avoided investing in direct or unlisted property assets because, as noted, valuation can be a murky business in this sector, while liquidity is also a major concern (it may be impossible to withdraw investments when desired). These drawbacks also apply to

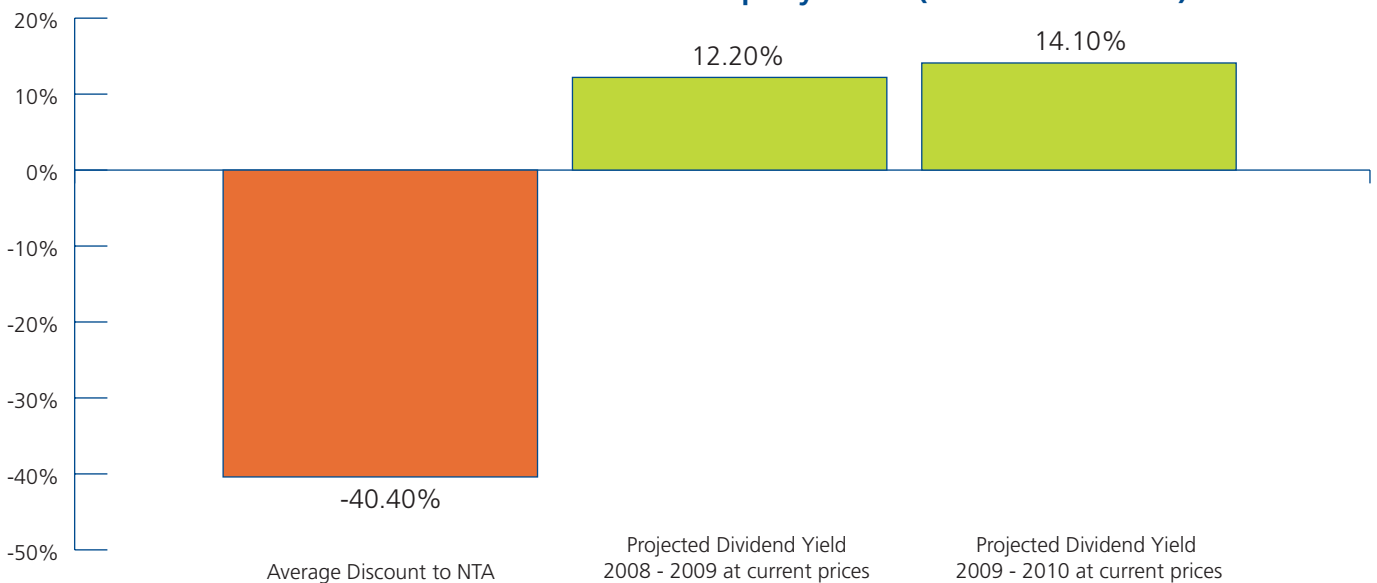
'private equity' (unlisted shares). Currently, listed property appears better value than direct property and appears under-valued compared with historical norms.

### Performance of the Listed Property sector compared to the Direct Property sector



The following graph illustrates the value now apparent in the listed property sector:

### Valuation Parameters for the Listed Property Sector (as at 30 June 2008)



Source: Phoenix Portfolios

With an average dividend yield of over 12% projected for the 2008-09 financial year (and a weighted average yield of over 9%) and with an average discount to net

tangible assets (NTA) of around 40%, the sector would appear to offer reasonably attractive valuations for investors.

## Q: Should we invest in Share Markets at all?

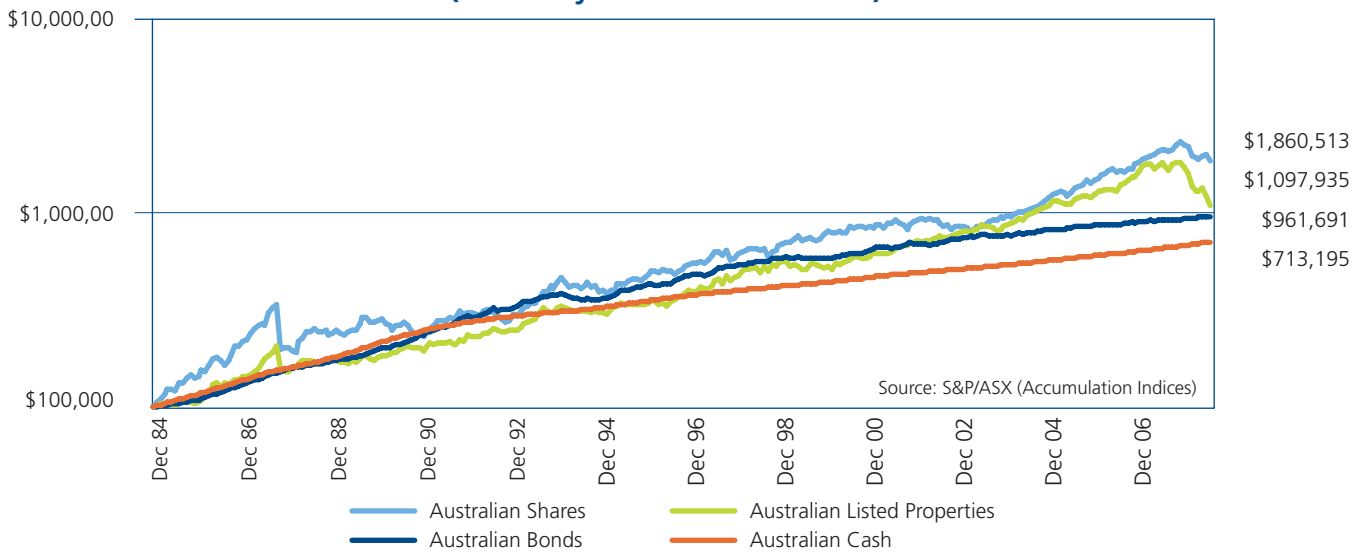
### A: Yes we should – share markets offer the best long-term returns.

Over the longer-term, financial theory tells us that share markets should out-perform defensive markets, such as bond markets or cash investments. This is because investors require a premium to compensate them for taking the extra risk of investing in volatile markets such as

shares. Interestingly, long-term market data confirms these theoretical assumptions and shows us that we can expect higher returns from shares, given a longer-term time frame. The following graph looks at what an initial investment of \$100,000 in various Australian asset

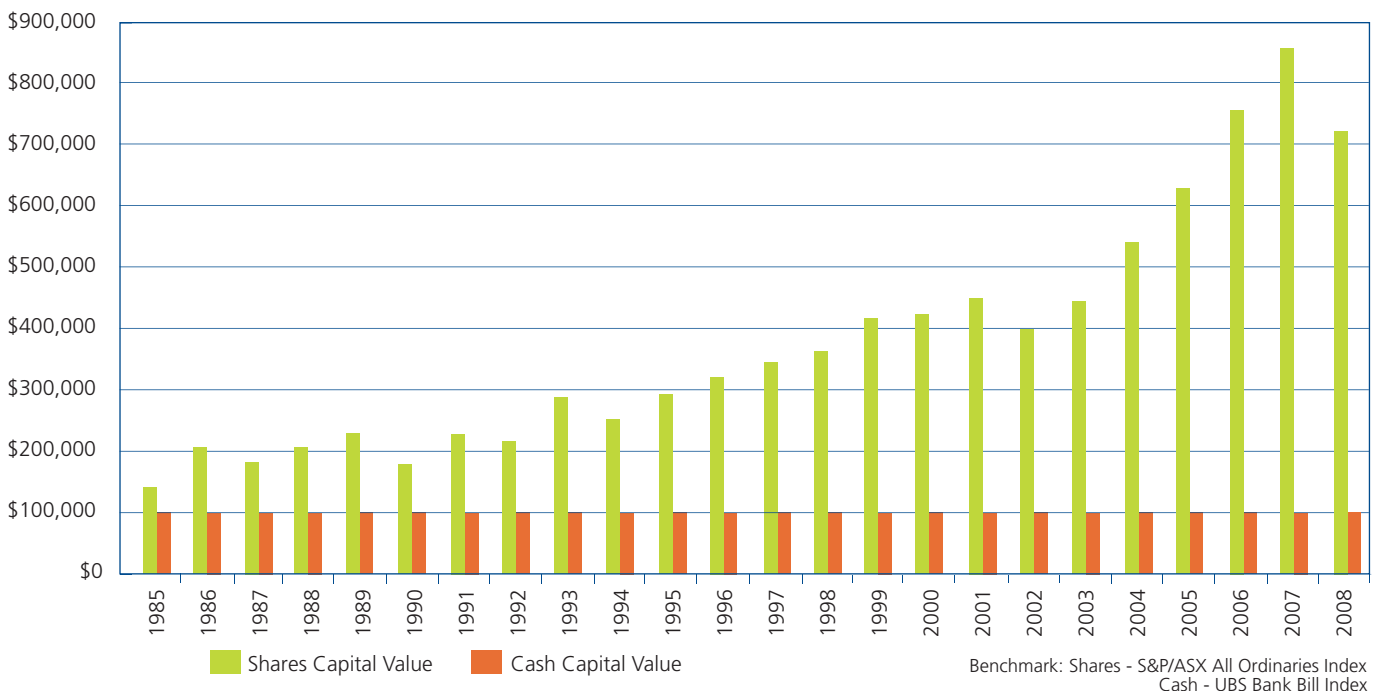
sectors on 1 January 1985 would have become by end-June 2008, a period of over 23 years. Despite the recent market corrections, shares and property have significantly out-performed other sectors:

**Value of \$100,000 Invested in Australian Markets (1 January 1985 – 30 June 2008)**



The graph below compares \$100,000 invested in the Australian Sharemarket and in cash/money market securities in 1985. Both provide a level of income, but share markets increase the value of your investment over the longer-term, whereas investments in cash funds bring no capital growth at all.

**Annual Capital Growth of Australian Shares compared to Cash (1 January 1985 to 30 June 2008)**



## Q: What about Emerging Markets?

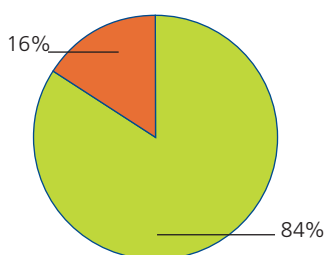
### A: Emerging Markets still appear to represent very good value.

Emerging markets have performed well in recent years, all because of very strong growth in many of these economies, particularly in the Asian region. This out-performance of developing economies compared with the advanced economies

is likely to continue into the future, with the International Monetary Fund forecasting that the Asian region (ex-Japan), for example, could grow by around 8% in real (inflation-adjusted) terms for at least the next five years, while

the advanced economies are likely to limp along at much slower growth rates. The following graph shows how the developing economies have been taking an increasing share of the global economic pie in recent years.

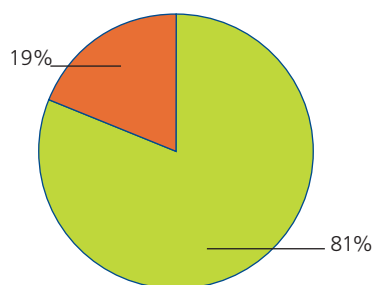
1992 Share of the World GDP



\$US 24 trillion

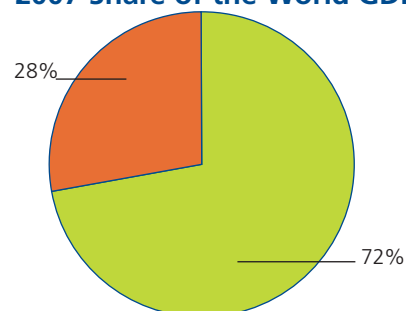
Developing Advanced

1999 Share of the World GDP



\$US 31 trillion

2007 Share of the World GDP



\$US 54 trillion

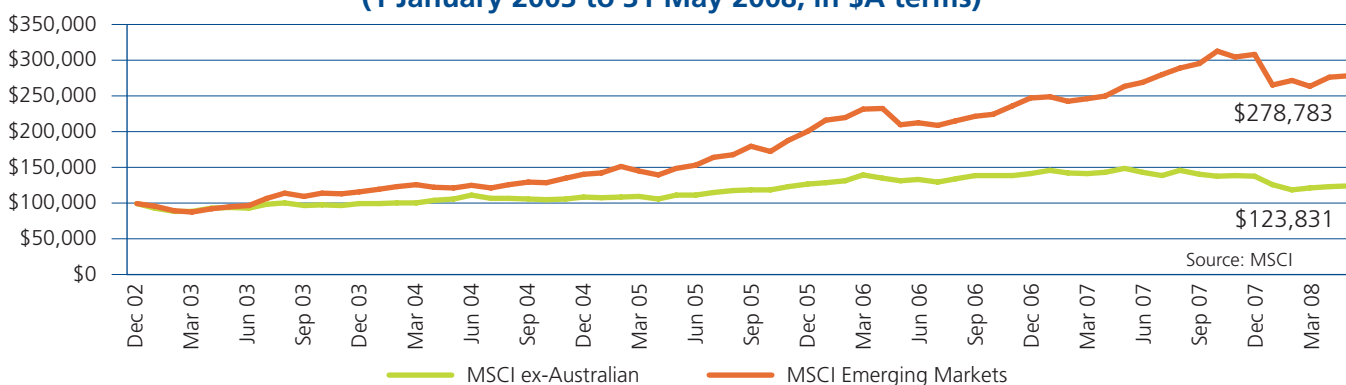
Source; International Monetary Fund, 2008 (Data at current market exchange rates)

As a result of this out-performance in economic growth, emerging share markets have also been doing well relative to the major markets and still appear to be reasonably valued compared with

other investment opportunities. The following graph looks at the performance of emerging markets compared with the share markets of the major economies over recent years. Although emerging

markets have out-performed by a considerable margin, they still remain cheaper than the major markets, according to various value measures.

Performance of Emerging Markets compared with the Major Markets  
(1 January 2003 to 31 May 2008, in \$A terms)



Source: MSCI

## Q: What about Fiducian's Manage the Manager Investment Style?

### A: Fiducian's Investment Process has inbuilt flexibility.

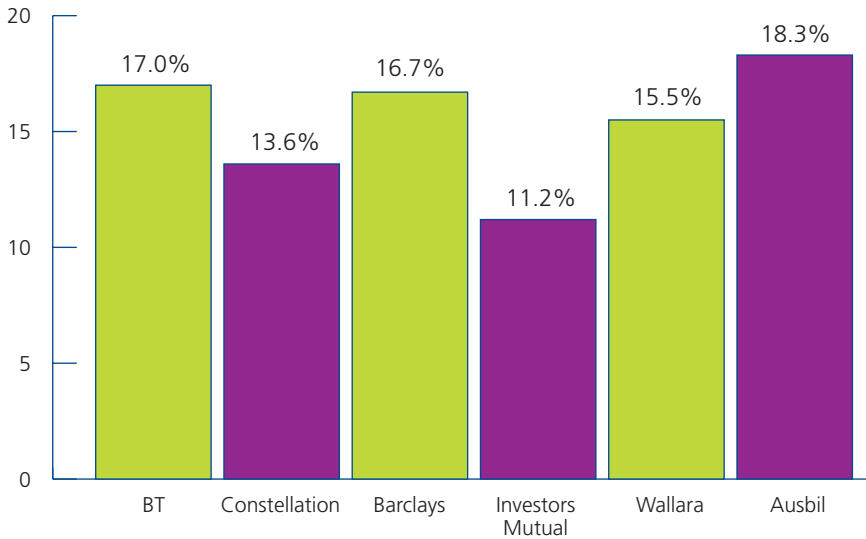
Fiducian has its own investment style, termed the Manage the Manager process, in which underlying portfolios are blended to reduce potential volatility within asset sectors. Fiducian also uses its own system of tilting towards different managers

within this process. We can also replace managers who do not perform to our requirements. This process has delivered gains to investors over time. For example the graph over the page illustrates how the system has added value

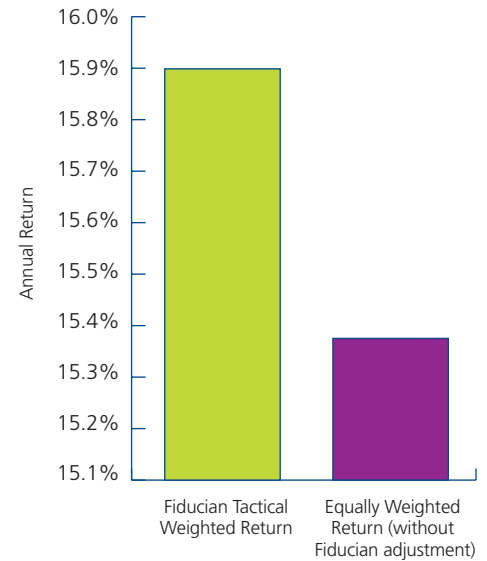
for the Fiducian Australian Shares Fund over the three years to end June 2008. By tilting, or over-weighting some managers and under-weighting others, Fiducian was able to add value for its investors over the three-years to end-May 2008:

### Fiducian's Tilting Process

Fiducian selected Australian shares managers annual returns over the 3 years to end May 2008.



### Fiducian Adds Value Through Tilting



## Q: How has the Fiducian Investment process performed?

### A: Fiducian's record remains a good one.

Fiducian has performed very well over the longer-term as is clear from the graph below. Over the past year, however, our diversified funds have not performed as well as previously. One of the key reasons for this is that recently listed property has under-performed other sectors by a significant margin over the past year. Although Fiducian has been underweight this sector relative to its own benchmarks, it has nevertheless tended to have a greater weighting than many of its competitors. One reason for this is that Fiducian has always avoided investing in unlisted securities, including both 'private

equity' and so-called direct property. Direct property has had a very good year, greatly out-performing listed property, although historical data suggests that over the longer-run, listed property tends to out-perform, due to a greater concentration of high quality property in the listed sector. Furthermore, whereas listed property is valued by the market on a continuous basis, direct property is only occasionally valued (sometimes only every year or even three years). The following graph illustrates the relative performance of our three diversified funds, including the Fiducian Balanced

Fund, since early 2001. Fiducian's Manage The Manager process blends a range of investment styles to average their returns. In other words its funds are not designed to top the performance charts over short periods. However its process of steady, consistent average to above average short term returns, dampen the volatility and risk that any single fund manager may deliver. As a consequence, its longer term performance steadily stands out, while other funds frequently move up and down the rankings or even close their funds.

## Superior Long Term Performance

### Fiducian Funds Performance – May 2008

Fiducian Funds	1 year		3 years		5 years		7 years	
	Return	Rank	Return	Rank	Return	Rank	Return	Rank
Fiducian Capital Stable	-1.3%	18/95	6.3%	14/86	7.3%	14/63	6.1%	11/41
Fiducian Balanced	-8.7%	101/177	8.3%	51/154	10.3%	29/107	6.8%	6/67
Fiducian Growth	-10.9%	148/177	8.8%	33/154	11.1%	12/107	7.0%	5/67

Note: Returns are after fees and before taxes.

Source: Morningstar published performance data for Australian managed funds.

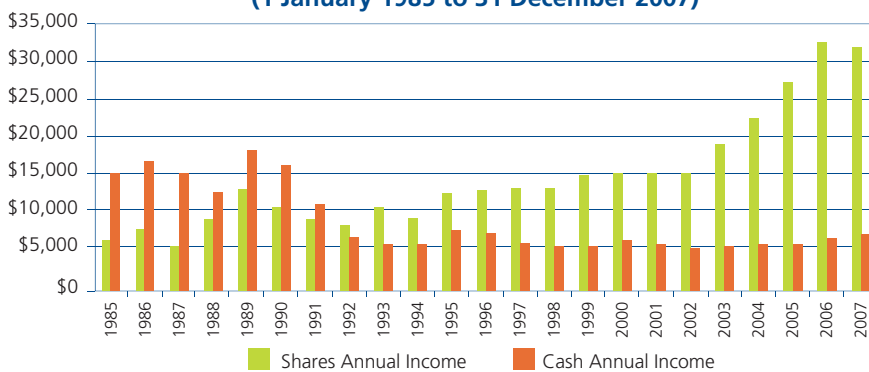
## Q: What are some good options for very defensive investors?

### A: Bank Deposits are not the only defensive strategy.

A good defensive approach in the current market would be to invest in a mix of relatively high yielding products. These could include exposure to the **Fiducian Structured Income Fund**, which includes well-diversified investment in private loans, as well as first mortgages. This fund returned around 10.4% for the 2007-08 financial year and has not had any suggestion of likely default of any of its over 40 underlying private loans. This fund is expected to continue to provide solidly positive returns for investors. Investment in this fund could be coupled with well-diversified listed property exposure through the **Fiducian Property Securities Fund**, which following the listed property falls of the past year, is now providing a high yield for investors (expected to be around 9% for the current financial year, based on capital values at the end of June). Another defensive option is the **Fiducian Capital**

**Stable Fund**. This fund typically has only around 30% in growth assets. Because of this exposure, this fund would be expected to out-perform cash funds over the longer-term. This fund has performed very well over time, ranking 14th out of 86 similar funds over the three years to end-June, according to Morningstar data (as set out in the graph above). Yet another investment option, assuming that income is a priority, would be to include exposure to the **Fiducian Imputation Portfolio**, which at end-June 2008 was offering a grossed-up dividend yield to investors of well over 8.0%. We should also keep in mind the fact that over time the income from share market dividends tends to grow in line with the increasing capital value of shares, so that over the longer-term, investments in share markets usually provide greater annual income than cash investments, as shown in the following graph for the Australian share market:

Annual Income of Australian Shares compared to Cash  
(1 January 1985 to 31 December 2007)



## Q: Is there a final word?

### A: Yes, beware the risk of missing a market rebound.

A defensive approach to investing will not be suitable for everyone and given the very fair valuations for most share and listed property markets at present, including emerging share markets, prudent investors who can withstand the current market turmoil would be well advised to maintain appropriate levels of exposure (in accordance with their agreed risk profiles) to growth sectors. The real risk of a defensive strategy is

that the opportunity to reap the rewards of any market rebound would be lost to those with their investments embedded in bank deposits or other low-risk asset sectors. It is important to note that no one can foretell the best time to re-enter share markets once investors have moved to other sectors. As Warren Buffet once said, 'the share market is a wonderfully efficient mechanism for transferring wealth – from the impatient to the patient'.



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