Principles for successful long-term investing
Using Market Insights to achieve better client outcomes
2Q 2016
MARKET INSIGHTS WAS FOUNDED IN 2004 IN THE WAKE OF THE FALLOUT FROM THE TECH BUBBLE. AT A TIME WHEN INVESTORS NEEDED IT MOST, THE FIRST GUIDE TO THE MARKETS PROVIDED CLARITY AND PERSPECTIVE, AND HELPED TO REINFORCE KEY HABITS OF SUCCESSFUL LONG-TERM INVESTORS. TODAY, MORE THAN A DECADE LATER, IT IS IN THAT SAME SPIRIT THAT WE ARE PLEASED TO OFFER, “PRINCIPLES FOR SUCCESSFUL LONG-TERM INVESTING”. WE BELIEVE THAT A COMBINATION OF THESE PRINCIPLES, SOUND FINANCIAL ADVICE AND DEEPER INSIGHTS CAN HELP MAKE EVERY INVESTOR BETTER OFF.
PRINCIPLES FOR SUCCESSFUL LONG-TERM INVESTING

1. PLAN ON LIVING A LONG TIME
2. CASH ISN’T ALWAYS KING
3. AVOID EMOTIONAL BIASES BY STICKING TO A PLAN
4. VOLATILITY IS NORMAL; DON’T LET IT DERAIL YOU
5. STAYING INVESTED MATTERS
6. DIVERSIFICATION WORKS
**1 – PLAN ON LIVING A LONG TIME**

**LEFT:**

**We are living longer**

Thanks to advances in medicine and healthier lifestyles, people are having longer lives. This chart shows the probability of reaching the ages of 80 or 90 for someone who is aged 65 today. A 65-year-old couple may be surprised to learn that there is a 50% probability that at least one of them will live another 25 years, reaching the age of 90!

**RIGHT:**

**Many of us have not saved enough**

Many studies, including the one referenced here, reveal that individuals do not feel adequately prepared for retirement. There is a significant shortfall between the number of years a person expects their savings to last and the number of years a person typically spends in retirement. Investors should start early by saving more, investing with discipline and having a plan for their future.
Cash pays less

Investors often think of cash as a safe haven during volatile times, or even a source of income. But banks no longer need to tap retail investors for funds – the rate of interest earned on term deposits is falling and the gap above the official policy rate narrowing. With interest rates expected to stay lower for longer, investors should be sure that an allocation to cash doesn't undermine their long-term investment objectives.

There's a lot of it

More than $500 billion of cash still sits on the “sidelines” earning an increasing lower rate of interest, and will have missed out on the strong equity market performance following the global financial crisis.
**Home-country bias**

The Australian economy represents only a fraction of the global economy and accounts for only 2.6% of the world's equity markets. Yet for most Australian investors, a large portion of their investment is focused on this small portion of global capital markets.

**Familiarity bias and concentrated positions**

The major Australian equity index, the ASX 200 Index, is not representative of global equity markets and has an out-sized weighting towards the financial and materials sectors which includes banks and resource companies. Because of “home bias” and investors' preference for the domestic equity market, investors may find themselves having larger position in these sectors than a global investor.

It is important that investors are aware of these biases and employ a disciplined investment plan that can help minimise their influence.
Seeing through the noise

Every year has its rough patches. The red dots on this chart represent the maximum intra-year decline in each calendar year for the ASX 200 Index going back to 1994. While it is impossible to predict those pull-backs, investors should learn to expect them; after all, markets suffered double digit pull-backs in 18 of the last 22 years.

But investors should also have a plan for when the going gets tough, instead of reacting emotionally. The grey bars represent the full year market returns from 1 January to 31 December. Despite the pull-backs, the equity market managed to deliver positive returns in roughly 75% of the calendar years since 1994.
Good things come to those who wait

While markets can always have a bad day, week, month and even year, history suggests investors are less likely to suffer losses over longer periods.

This chart illustrates this concept. While one-year equity returns have varied widely since 1950 (+61% to -43%) a blend of equities and bonds has not suffered a negative return over any ten-year rolling period within the past 65 years.
Diversification has served its purpose

The last 15 years have been a volatile and tumultuous ride for investors, with multiple natural disasters, numerous geopolitical conflicts and major market downturns. While volatility might be a normal part of investing, investors can help minimise some of these risks through diversification.

Despite the difficulties, the worst performing asset class of those shown was cash. Meanwhile a well-diversified portfolio including equities, bonds and some uncorrelated assets returned 7.5% per year over this period.
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