

Welcome to the 2011 Winter Edition of the Strategy First Financial Planning newsletter.

While 30 June brings the end of the financial year, it's also a key date where fund managers, super funds etc. release their investment performance numbers for the past twelve months and longer.

Strategy First invests your money based on its Investment Philosophy. The philosophy has remained consistent since the business began back in September 2005 and has operated throughout significant upheaval in financial markets.

At this time each year, we formally evaluate the results of our Investment Process to determine if it has actually added value. This is the focus of this newsletter.

Furthermore, over the course of the next four newsletters, we will be expanding on the four main parts of our Investment Process:

- Spring 2011:** Your Risk Profile and how this affects your allocation to Growth and Defensive assets.
- Summer 2011:** Growth Assets and our approach to Equities
- Autumn 2012:** Defensive Assets and our approach to Fixed Interest.
- Winter 2012:** Active vs. Passive Management.

As usual, you will also find all our regular features such as the current 10-year forecast returns for each asset class and some information on what has been happening in the world of Strategy First.

### Strategy First Performance

Since inception, Strategy First has applied our Investment Philosophy to all client portfolios. Some client portfolios differ at the margin, but only because of individual circumstances.

The Investment Process is reliable, robust and is backed by widely tested, peer reviewed, academic research.

We meet formally as an Investment Committee each quarter to review forecast returns and market valuations for each asset class, being shares, property, fixed interest and cash.

Asset Allocation is the decision of how a portfolio is allocated to these different asset classes, taking into account current valuations, forecast returns and associated risks.

We firmly believe the most efficient and effective way to implement our asset allocation decisions is to invest via low cost managed funds that maximise diversification and after tax returns.

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## Evaluation Process

To test this at a practical level, we have a fully invested portfolio [the SF Portfolio] that is invested 100% in line with our Investment Philosophy. We then look at this on two levels:

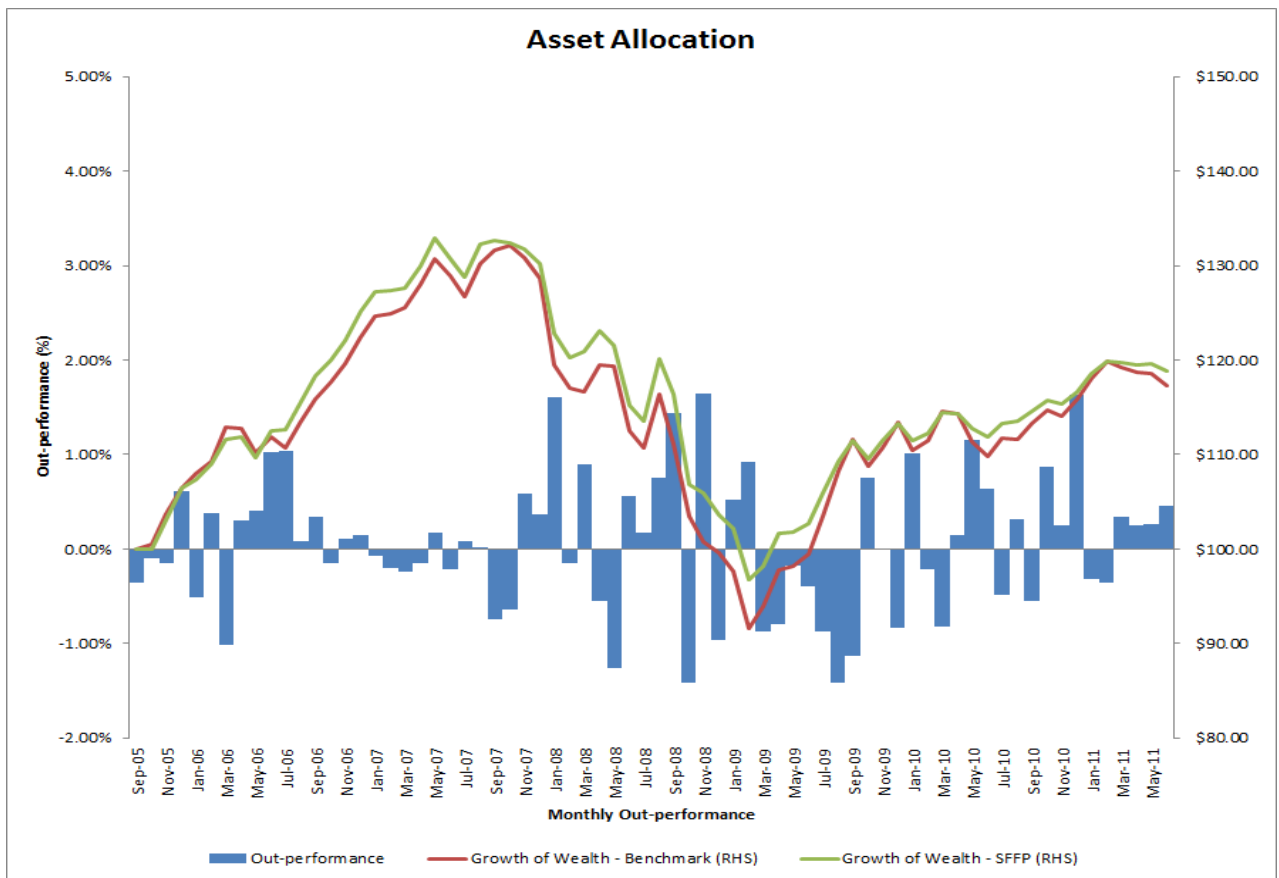
- The return derived from Asset Allocation – i.e. the return from being invested in the given asset class and how our decisions to change the asset allocation over time add or detract from returns; and
- The return achieved from Security Selection – i.e. the after fee return from the specific managed funds we use to implement the agreed Asset Allocation.

## Have Our Asset Allocation Decisions Added Value?

The bar chart below shows the relative outperformance/underperformance of the SF portfolio, on a monthly basis since inception 6 years ago. The benchmark we have used it to is a standard “Growth” portfolio, with an unchanging asset allocation.

Overlaying this, are line charts that show how \$100 invested in each portfolio would have grown over the last six years.

We have assumed index returns for both portfolios.



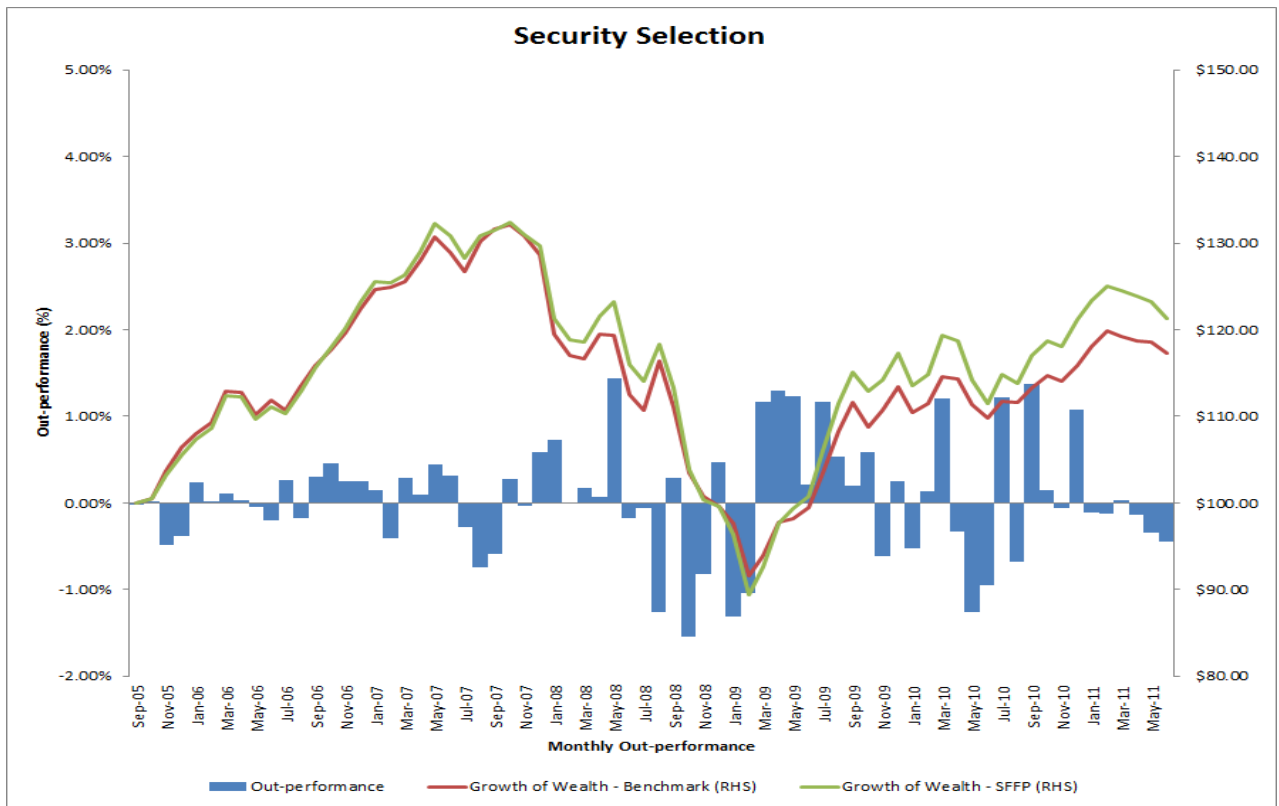
As you can see, there have been periods where the SF portfolio has outperformed and underperformed the benchmark portfolio, which is what would be expected in the short-term.

Specifically, if you had invested \$100 in each portfolio in September 2005, the SF portfolio would now be worth \$118.87 and the benchmark portfolio worth \$117.27. This equates to an additional 1.6% of value added to the portfolio due to Strategy First's asset allocation decisions.

### Do the Managed Funds We Use Add Value?

In similar fashion, we have also analysed the impact of SF's security selection decisions on portfolio returns. In this scenario, we have compared a portfolio comprised of index funds (before fees), to a portfolio that reflects SF's preferred funds (after fees).

We have assumed both portfolios have the same static asset allocation.



As with our asset allocation analysis, there have been short-term periods where the SF portfolio underperformed the benchmark portfolio. However, the cumulative performance for the period clearly shows the SF portfolio outperforming the benchmark over the total period. In this case, providing an additional return of 4.0%, after the management fees associated with the selected Investment Funds, over the period.

## 10 Year Forecast Returns

The table below outlines our 10-year forecast returns this time last year, compared with expectations for the next 10 years, based on July 2011 valuations. The forecast returns are used to make an assessment on whether we see an asset class as cheap, fair value, fully valued or expensive.

Asset Class	Forecast Return June 2010 (% p.a.)	Forecast Return July 2011 (% p.a.)	Status July 2011
Cash	5.1	5.0	n/a
Fixed Interest	6.7	6.5	Fair Value
A-REITs	6.9	7.6	Fully Priced
Shares – Australian	9.9	10.6	Fair Value
Shares – International	7.6	6.9	Fully Priced

Over the last 18 months, both global and domestic markets have continued to remain volatile.

Based on current valuations, Australian shares are at the high end of our Fair Value range and International shares are on the border of our fully valued and overvalued ranges.

A-REITs (Listed Property Trusts) are at the high end of our Fully Priced range and we remain concerned about the high concentration in the sector and the strong correlation with price movements in equity markets. Therefore, we continue to recommend no exposure to this asset class.

Long dated Fixed Interest is fair value and we are only investing in high-quality Fixed Interest.

## Information Overload!

Over the past few years, there has been a massive increase in the volume of financial and economic information that is readily available to investors. In theory, this should lead to more informed and rational investment decisions, but is this really the case? Chief Economist and Head of Investment Strategy at AMP Capital Investors, Dr Shane Oliver, offers his opinion in his article 'Is too much information making us worse investors?' We have reproduced an excerpt from this article below:

*"It's self-evident there is a long worry list for investors right now. There are fears Greece will bring down the European economy. The US economy has slowed, ending the second round of quantitative easing and politicians are squabbling about increasing the US Government's debt ceiling. In China and emerging markets, there are worries policies to slow inflation will cause a hard landing. Australia has its own overlay of worries around further interest rate hikes, the strong Australian dollar and uncertainty around government policy, notably the carbon tax. Natural disasters, such as floods, earthquakes, tornados and volcanic eruptions have only added to the sense of unease.*

*All these worries are real and this has me wondering whether 24 hour news cycles, combined with the information avalanche we are now being smothered with, are actually improving the information flow to investors or has it just made investors more fearful, short sighted and jittery? Has it led investors to a short-term focus which is not in their long-term financial interest?*

*There is no doubt the global financial crisis has left the world with a hangover but has the world really changed? The global economy has been through difficult phases in the past and we got through it. The last century has been full of disasters and catastrophes. And yet, despite this, since the 1900s Australian shares have returned 11.8% per annum (or 7.7% pa after inflation), which is double both the 5.9% pa return from bonds over the same period and 5.3% pa returned on cash since 1926.*

*Maybe the world has become more problematic, but I doubt it. When I think of what my parents went through, such as the Great Depression, loss of infant siblings, numerous wars and post war recessions, I find it very hard to agree that life is harder today than it was when they were growing up.*

*While not to deny the current list of worries, one wonders whether the communication revolution is making the list seem worse than it really is. Thanks to increased access to information, we are now bombarded by news on a continuous basis. Whether it's on the television via regular updates on numerous news and finance channels, or through websites, blogs and twitter on smart phones, it's hard to escape.*

*The trouble is, much of this is background noise and random movements in economic data, due more to statistical aberrations than fundamental swings in the economy. And of course bad news sells better than good, which is why, for example, we hear so much about Greece, which accounts for less than 2% of the European economy, compared to Germany, which is doing fantastically well and accounts for 20%.*

*In theory, the improved flow of, and access to, economic and financial information should be making for better, more efficient investment markets. However, it is doubtful this is the case.*

*Academic economists focus on two types of market efficiencies. The first is the speed with which new information is reflected in the price of shares and currencies and the second is whether it is done so in a rational way. On the first point, it's likely we have made great strides as the democratisation of information has seen financial prices reflect new information quickly. But there is little evidence that all the extra information is resulting in more rational pricing in shares and currencies. Asset bubbles and busts are as common as ever.*

*In fact, at the individual investor level, it's likely the increased flow of information might be adversely affecting investors. The constant information bombardment is likely making investors excessively cautious, boosting short-term speculation relative to medium-and longer-term investment. This in turn is likely to be negative for the economy.*

*Against this backdrop, there are two things investors should do. Firstly, turn the volume down on the news front, consume less of it. Secondly, adopt a long-term strategy and stick to it."*

## Rhys Phillips – The Hero In Our Midst!

When we're not working hard to secure your financial future, the staff of Strategy First engage in various sports, volunteer work and other activities. Today, we are putting the spotlight on one of our paraplanners, Rhys Phillips, who is a member of Queenscliff Surf Life Saving Club.

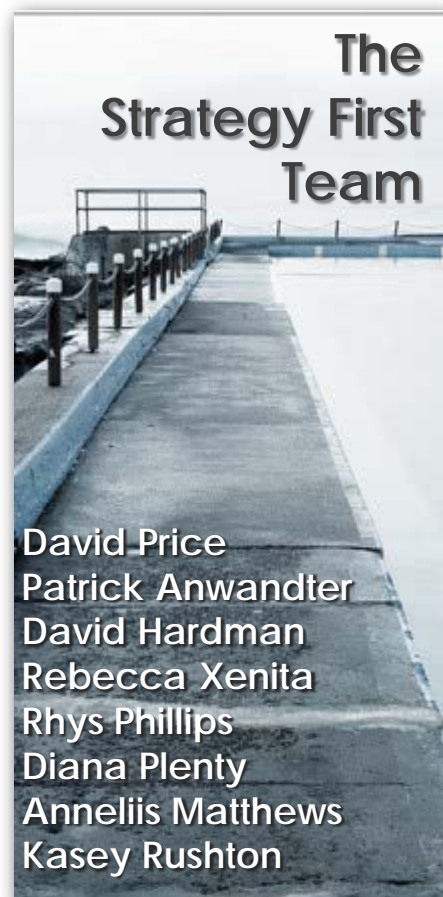
In addition to his ordinary patrolling duties, Rhys is a member of the Club's Inflatable Rescue Boat (IRB) team. IRBs are a vital tool for Life Savers on all of Australia's beaches, providing rapid access to distressed swimmers, even in the most challenging conditions.

Each year, Surf Life Saving NSW holds a multi-round premiership competition, where the best IRB crews from around the state compete and hone their skills. This competition culminates with the NSW State Championships, which, this year, were held on 11 and 12 June at Woolgoolga, in the state's north.

After two hard days of racing and battling a violent shore-break, Rhys managed to claim two championship medals: a gold in the Novice Rescue event (for first-time racers) and; a bronze in the Under-23 Teams event.

This was a fantastic result and we are very proud of Rhys' effort.

The Queenscliff team brought home a total of seven medals from the event and will be attending the Australian Championships in Glenelg, SA, later this year. We wish Rhys and his teammates all the best!



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