Understanding Investing

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Asset classes

It is important to understand the main asset classes and how they can affect the returns and risk of your portfolio. The types of asset classes include:

Cash

Cash generally refers to investments in bank bills and similar securities which have a short investment timetable. They provide a stable, low risk income in the form of regular interest payments.

Risk and potential return:

Fixed interest

Most government bonds, corporate bonds, mortgages and hybrid securities generally operate in the same way as loans. The income return is usually in the form of regular interest payments for an agreed period of time.

Risk and potential return:

Property & Infrastructure

Property is shares in property investments. Sectors include commercial, retail, hotel and industrial property. Returns are made from rental income and increases in property market value. Infrastructure assets are those that deliver services necessary for daily life and economic activity such as airports, toll roads and pipelines. Returns are made from fees, patronage, rental income and the revaluation of assets.

Risk and potential return:

Australian shares

A share represents part ownership of a company. Shares are generally bought and sold on the stock exchange. Returns usually include capital growth (or loss) and income through dividends which may be franked (i.e. the company has already paid tax on the earnings).

International shares

International shares generally work the same as Australian shares. The additional benefit is the increased opportunity to invest in a much wider range of countries (e.g. Europe, Asia) and a broader selection of companies outside Australia. However, currency valuations may affect performance.

Growth Alternatives

Growth alternatives are investments that provide an alternative source of return and growth opportunity to that derived from "traditional" growth assets such as shares, property and infrastructure. This is typically achieved by implementing alternative investment approaches using mainstream assets classes. Their performance is generally unrelated to other asset classes i.e.

		they don't follow market trends and they may have varying investment time frames.
Risk and potential return:	**Risk and potential return:**	**Risk and potential return:**
		

There may be asset types within each asset class. For example, within shares, there is a choice of Australian and international shares and within international shares, there is choice of specific regions or countries like China or emerging market shares.

Asset Allocation
The term "asset allocation" refers to the process of determining the proportions of money to invest in the various asset classes i.e. Cash, Fixed Interest, Property and Infrastructure, Australian Shares, International Shares and Growth Alternatives.

You should be aware that shares together with fixed interest and property can be volatile assets i.e. the value can go up and down. The reward for taking on greater volatility is the likelihood of higher returns over the long term.

Investment Risks
Risk is the chance that you will not achieve your goals. Successful investing is largely about managing risk and taking advantage of opportunities for higher returns. Any investment decision that you make means you must take a risk of some sort. The decision whether or not to accept risk is a personal one and may be affected by a number of factors such as your age, investment experience, financial position and investment time frame.

Some risks can be reduced through professional portfolio management and strategic diversification. However, any time you invest, there will always be some element of risk which cannot be avoided.

It is important to understand the relationship between risk and return. Generally, the higher the level of short - term risk you are prepared to accept when investing, the higher the potential for loss. This is called the risk / return trade off.

Before investing you need to decide how comfortable you are with investment risk and how much risk you are prepared to take to achieve the returns you want. We refer to this as ‘Risk Profile’.

Any investment decision you make means that you must take a risk of some sort. The decision will directly relate to the amount of money you invest, your circumstances at the time and your needs for the future. If you have a better understanding of risk, you can make a more informed investment decision by accepting some risks and rejecting others. It is important point that you understand the effects of risk, particularly over your investment time frame.

The decision to accept or reject certain risks is a very personal one. Only you can make that decision. Our role is to help you by providing some guidance on how to consider and assess risk. Following is a summary of some of the risks that can affect investors.

Risk	Explanation
Asset liquidity	An asset cannot be sold due to lack of liquidity in the market for example unlisted property trusts
Credit Risk	This applies to debt type investments such as term deposits and fixed interest. The institution you have invested with may not be able to make the required interest payments or repay your capital.
Currency	For overseas investment there is the risk the value of other currencies may change in relation to the Australian dollar and reduce the value of the investment.
Inflation Risk	The real purchasing power of your money may not keep pace with inflation. Inflation is an important consideration for all investors. If the after tax return on your investments is less than the rate of inflation, then the real value of your money will decline.
Interest Rate Risk	For investors relying on fixed rate investments, maturing money may have to be reinvested at a significantly lower rate.
Legislative Risk	Your investment strategy could be affected by changes in the current laws and regulations.
Liquidity Risk	You may not be able to access your money quickly, or without cost, when it is required.
Manager Performance	The risk that individual investment managers underperform.
Market Risk	Movements in the market mean the value of your investment can go down as well as up, sometimes suddenly. Different types of investments experience different levels of volatility (i.e. ups and downs). Volatility becomes a problem if you do not have the time frame to withstand the rough patches. It is important to remember that markets go through regular ups and downs and that capital losses can occur if investments are redeemed when markets are down. While it is tempting to sell out of an investment after its value has fallen, history has taught us that investors who stick with their strategy generally go on to recover and prosper.
Market Timing Risk	Anticipating market rises and falls can be extremely difficult because no two economic cycles are the same. Market timing is not a good long term approach that tends to result in an overall poor return and high transaction costs. A sensibly diversified portfolio will generally outperform a continually changing portfolio.
Mismatch Risk	The investment you choose may not be suitable for your needs and circumstances. A perfectly sound investment choice for you now may not be best for you at another time.
Risk of not Diversifying	All your capital will be affected if your single investment does badly. Diversification means spreading your money across different investments to reduce risk. The right asset allocation is an important driver for the long-term returns of your portfolio.

Risks can be mitigated by ensuring an investment strategy is setup that meets your personal needs and objectives and can be managed by diversifying your investments, ensuring thorough research on the products and that you understand your goals and how much risk you are willing to accept.

Investment timeframe

One of the primary issues to consider is the timeframe of investing, that is, the length of time to hold an asset to obtain the benefit of investing. Investment timeframes are generally described as short term (1-3 years), medium term (3-5 years), and long term (5-7 + years).

Diversification

Diversification is an important investment strategy used to manage investment risk and volatility (i.e. the ups and downs of your investment) within a portfolio whilst still providing an appropriate level of return.

The key to diversification is to invest in assets that have different characteristics and perform differently in varying market conditions.

You can diversify your portfolio in different ways. Examples of diversification include investing:

- across a range of asset classes including growth assets like shares and property and defensive assets like fixed interest and cash
- across different countries and regions such as Australian and international assets, Asia and emerging markets
- across different securities that provide you access to a range of companies and sectors.

History shows that no one asset class has consistently out-performed year after year. This is illustrated in the following Vanguard Index Chart 2024 which shows the one year return from the various asset classes from over the last 20 years.

Financial year total returns (%) for the major asset classes

YEAR	AUST. SHARES	INT'L SHARES	INT'L SHARES (HEDGED)[1]	U.S. SHARES	AUST. BONDS	INT'L BONDS (HEDGED)[2]	CASH	AUST. LISTED PROPERTY	INT'L LISTED PROPERTY[3]
1995	6.4	14.2	**3.7**	**29.9**	11.9	13.1	7.1	7.9	7.5
1996	14.3	6.7	**27.7**	13.5	9.5	11.2	7.8	3.6	**2.4**
1997	26.8	28.6	26.0	**41.5**	16.8	12.1	**6.8**	28.5	35.7
1998	**1.0**	42.2	22.1	**57.5**	10.9	11.0	5.1	10.0	25.0
1999	14.1	8.2	**15.9**	14.9	3.3	5.5	5.0	4.3	**-6.8**
2000	16.8	**23.8**	12.6	18.2	6.2	**5.0**	5.6	12.1	14.1
2001	8.8	-6.0	**-16.0**	0.6	7.4	9.0	6.1	14.1	**38.2**
2002	-4.5	-23.5	-19.3	**-25.8**	6.2	8.0	4.7	**15.5**	7.5
2003	-1.1	**-18.5**	-6.2	-16.1	9.8	**12.2**	5.0	12.1	-5.2
2004	22.4	19.4	20.2	14.7	**2.3**	3.5	5.3	17.2	**28.7**
2005	**24.7**	0.1	9.8	**-2.8**	7.8	12.3	5.6	18.1	21.2
2006	24.2	19.9	15.0	11.5	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	-23.2	4.4	**8.7**	7.3	**-36.3**	-28.6
2009	-22.1	-16.2	-26.6	-12.4	10.8	**11.5**	5.5	**-42.3**	-31.2
2010	13.8	5.2	11.5	9.5	7.9	9.3	**3.9**	20.4	**31.3**
2011	12.2	**2.7**	**22.3**	3.1	5.5	5.7	5.0	5.8	9.2
2012	**-7.0**	-0.5	-2.1	10.1	**12.4**	11.9	4.7	11.0	7.5
2013	20.7	33.1	21.3	**35.0**	**2.8**	4.4	3.3	24.2	24.3
2014	17.6	20.4	**21.9**	20.8	6.1	7.2	**2.7**	11.1	11.8
2015	5.7	25.2	8.5	**31.9**	5.6	6.3	**2.6**	20.3	23.1
2016	2.0	0.4	**-2.7**	7.3	7.0	10.8	2.2	**24.6**	20.4
2017	13.1	14.7	**18.9**	14.4	0.2	-1.0	1.8	**-6.3**	-4.8
2018	13.7	15.4	10.8	**18.7**	3.1	2.5	**1.8**	13.0	9.0
2019	11.0	11.9	6.6	16.3	9.6	7.0	**2.0**	**19.3**	13.5
2020	-7.2	5.2	3.6	**9.6**	4.2	5.3	0.8	**-21.3**	-13.4
2021	30.2	27.5	**37.1**	29.1	-0.8	**-1.4**	0.1	33.2	23.3
2022	-7.4	-6.5	-11.3	-2.4	-10.5	-8.2	**0.1**	**-12.3**	-5.5
2023	14.8	22.6	18.3	**23.5**	1.2	-1.5	2.9	8.1	**-1.5**
2024	12.5	19.9	21.5	24.1	3.7	1.9	4.4	**24.6**	3.9
Ave.	**9.9%**	**9.4%**	**9.2%**	**12.6%**	**5.8%**	**6.3%**	**4.2%**	**9.5%**	**9.6%**
Best	**30.3% (2)**	**42.2% (1)**	**37.1% (6)**	**57.5% (8)**	**16.8% (1)**	**13.1% (3)**	**7.8% (1)**	**33.2% (4)**	**38.2% (4)**
Worst	**-22.1% (2)**	**-23.5% (2)**	**-26.6% (3)**	**-25.8% (2)**	**-10.5% (2)**	**-8.2% (4)**	**0.1% (6)**	**-42.3% (5)**	**-31.2% (4)**

(X) denotes the number of times each asset class was the best/worst performer during a financial year ending between 1995 and 2024.

Source: Andex Charts Pty Ltd, June 2024.

2024 Vanguard Index Chart