



INDEPENDENT FINANCIAL ADVISERS



Investments  
&  
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## Investment Review: February 2008

~ STRAIGHTFORWARD ADVICE..... IN BLACK AND WHITE ~

## *About Hurst Financial Consultancy*

Hurst Financial Consultancy was founded in 1997 by the Managing Director, Michael Hurst. The company has operated successfully in Salisbury from inception serving clients locally, nationally and internationally.

The company focus has always been on excellence.

We have also developed a strong focus on state of the art information technology being aware of its significant value in not only collating data, but managing the performance of investments. We have our own in-house IT department and use its services constantly to develop the service that we give to our clients to ensure it is always “leading edge”.

As Independent Financial Advisers we have access to the full range of products and services available in the UK as opposed to a Tied Agent or Company Representative who may only advise and offer products from the company they represent. This means that we are able to give you impartial advice and recommend the most appropriate products for you, so that you will enjoy choice, value for money and our high-quality service.

Investment markets this year have been turbulent with the major Stock Market Indices falling since the beginning of January. Unusually for investments a wide spread of asset classes have been adversely affected during this period; i.e. shares, corporate bonds and property [commercial & residential]. However shares have taken the brunt of the downfall.

We know the major reasons for the falls in the markets and they are as follows:

1. US Sub Prime Mortgage crisis – this has been a problem since summer last year and it undermines market confidence because of the possibility of banks losing a significant amount of money from repossessions and the US consumer not spending and therefore leading to a potential contraction of their economy. As the US is the global force in trade any problems for them can effect the rest of the global economy and therefore stock markets.
2. Global Credit Crunch – this is linked to the above issue as it has made banks reluctant to lend and they are hoarding funds. This creates a problem as mortgages become harder to refinance and therefore people pay more in their mortgage payments and do not spend in the wider economy. This could lead to a contraction of economic growth and again this could affect stock markets adversely. This reluctance to lend could affect property prices as people may not be able to get financing to purchase residential or commercial property.
3. Societe Generale – this bank offloaded a very large amount of shares in a very short amount of time and it has been suggested that caused the rout in late January when the market fell 5% in one day. This sort of day understandably creates panic and makes investors nervous; it creates a desire to sell and therefore a potential snowball effect.
4. Monoline Bond Insurers – these companies underwrite corporate bonds and their financial strength can determine the credit rating of the bond and bonds with their credit ratings lowered could be sold causing them to lose significant value. The issue for these companies is that it is thought that they are underwriting bonds with an exposure to sub prime mortgage debt. This is not necessarily a problem but the fact that they did not know the level of the exposure is. Corporate bonds make up a very large part of the financial world and this has been one of the major issues in the stock markets for the last few weeks.
5. Rising energy & food prices – Oil is very expensive at over \$100 a barrel and this extra cost affects nearly everything that requires fuel to transport or manufacture. This is inflationary and reduces the amount of disposable income in the economy. The same is true of food as cereal prices are high due to poor weather and the rise in production of bio fuels.

Going forwards these issues will have varying effect on the economy as some of them may have peaked and some may create future problems.

The sub prime crisis has not gone away but much of the bad news is now in the open and is factored into market prices. Also the interest rate reductions in the US will go some way to alleviating repossessions going forward.

The credit crunch will not go away as quickly as hoped and all we can do with this is keep a watching brief and hope that the banks will become comfortable with lending. Banks want to lend as it is how they make money so they are incentivised to resolve this issue ASAP.

Societe Generale seems to have thankfully been a blip and the initial panic it created abated quite quickly.

Monoline bond insurers have had good news this week as there have been suggestions that rescue packages are in place and that various measures taken by the companies have shored up their financial strength. This is what has led to the market rally since Friday 22<sup>nd</sup> Feb.

Oil, gas, electric and food prices are inflationary and the Central Banks are conscious of this and the rise in prices will reduce the chances of major interest rate cuts which would obviously help the economy and therefore the markets; however low inflation is important for medium to long term issues so a fine balancing act is required.

The short term outlook for the markets and therefore your investments is not clear; however the medium term outlook is I believe favourable. The markets have fallen very rapidly and have seemingly factored in some very bad news that may or may not happen. On this assumption any more bad news may not affect the markets too badly and if there is no bad news then markets could lift quite quickly.

With regard to your investment I am comfortable with the investment mix that we have. The funds we are in are diversified across assets and regions; they are managed by large companies with proven records and I believe that we should wait until financial news becomes clearer before we make any changes.

I have been looking at past market behaviour using various pieces of information from investment companies and they show some interesting trends. The following table, published by New Star Investments, shows the effect of investing £1000 in the three detailed asset classes from 1971.

FTSE ALL SHARE INDEX			UK COMMERCIAL PROPERTY			BARCLAYS GILT INDEX		
% Return	Year	Return on £1,000	% Return	Year	Return on £1,000	% Return	Year	Return on £1,000
47.4	1971	£ 1,474.00	16.1	1971	£ 1,161.00	27.3	1971	£ 1,273.00
16.4	1972	£ 1,715.74	29.3	1972	£ 1,501.17	-3.8	1972	£ 1,224.63
-28.7	1973	£ 1,223.32	28.4	1973	£ 1,927.51	-8.9	1973	£ 1,115.63
-51.8	1974	£ 589.64	-15.9	1974	£ 1,621.03	-15.2	1974	£ 946.06
152.1	1975	£ 1,486.48	11.4	1975	£ 1,805.83	36.8	1975	£ 1,294.21
2.2	1976	£ 1,519.19	9.4	1976	£ 1,975.58	13.7	1976	£ 1,471.51
49.2	1977	£ 2,266.62	26.4	1977	£ 2,497.13	44.8	1977	£ 2,130.75
8.5	1978	£ 2,459.29	25.6	1978	£ 3,136.40	-1.8	1978	£ 2,092.40
10.5	1979	£ 2,717.51	22.8	1979	£ 3,851.50	4.1	1979	£ 2,178.19
35.4	1980	£ 3,679.51	17.5	1980	£ 4,525.51	20.9	1980	£ 2,633.43
13.8	1981	£ 4,187.29	15	1981	£ 5,204.33	1.8	1981	£ 2,680.83
29.2	1982	£ 5,409.97	7.5	1982	£ 5,594.66	51.3	1982	£ 4,056.09
29.2	1983	£ 6,989.68	7.6	1983	£ 6,019.85	15.9	1983	£ 4,701.01
32	1984	£ 9,226.38	8.8	1984	£ 6,549.60	6.8	1984	£ 5,020.68
20.1	1985	£ 11,080.89	8.3	1985	£ 7,093.22	11	1985	£ 5,572.96
27.5	1986	£ 14,128.13	11.3	1986	£ 7,894.75	11	1986	£ 6,185.98
8	1987	£ 15,258.38	26	1987	£ 9,947.38	16.3	1987	£ 7,194.30
11.5	1988	£ 17,013.09	29.5	1988	£ 12,881.86	9.4	1988	£ 7,870.56
36.1	1989	£ 23,154.82	15.4	1989	£ 14,865.67	5.9	1989	£ 8,334.92
-9.7	1990	£ 20,908.80	-8.4	1990	£ 13,616.95	5.6	1990	£ 8,801.68
20.7	1991	£ 25,236.93	-3.1	1991	£ 13,194.83	18.9	1991	£ 10,465.20
20.5	1992	£ 30,410.50	-1.6	1992	£ 12,983.71	18.4	1992	£ 12,390.79
28.4	1993	£ 39,047.08	20.2	1993	£ 15,606.42	28.8	1993	£ 15,959.34
-5.9	1994	£ 36,743.30	11.9	1994	£ 17,463.58	-11.3	1994	£ 14,155.94
23.8	1995	£ 45,488.20	3.6	1995	£ 18,092.27	19	1995	£ 16,845.57
16.7	1996	£ 53,084.73	10	1996	£ 19,901.50	7.7	1996	£ 18,142.67
23.6	1997	£ 65,612.73	16.8	1997	£ 23,244.95	19.4	1997	£ 21,662.35
13.8	1998	£ 74,667.29	11.8	1998	£ 25,987.85	25	1998	£ 27,077.94
24.2	1999	£ 92,736.77	14.5	1999	£ 29,756.09	-3.5	1999	£ 26,130.21
-5.9	2000	£ 87,265.30	10.5	2000	£ 32,880.48	9.2	2000	£ 28,534.19
-13.3	2001	£ 75,659.02	6.8	2001	£ 35,116.36	1.3	2001	£ 28,905.14
-22.7	2002	£ 58,484.42	9.6	2002	£ 38,487.53	9.8	2002	£ 31,737.84
20.9	2003	£ 70,707.67	10.9	2003	£ 42,682.67	1.6	2003	£ 32,245.65
12.8	2004	£ 79,758.25	18.3	2004	£ 50,493.59	7.2	2004	£ 34,567.33
22	2005	£ 97,305.06	19.1	2005	£ 60,137.87	8.4	2005	£ 37,470.99
16.7	2006	£ 113,555.01	18.1	2006	£ 71,022.83	-0.01	2006	£ 37,467.24

#### Source

Investment Property Databank November 2007  
New Star Fund Managers

What is evident from this table is that over a period of time each asset class has risen and that when there has been a downturn it has not lasted beyond the short to medium term and that after the down period there has been a significant upturn. Also the following information sheet from JP Morgan shows this trend on a micro scale in that the days following significant falls significant gains can happen. This evidences to me the need to not overreact to falling markets, as a loss would only be realised should a withdrawal be made. **This is not to say that investments are guaranteed to go up as they can and do go down in value**, but in my view the percentage decision is to stay invested and await a recovery.



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# TIME, not TIMING: the key to successful investing

When the market climate is uncertain, investors often become nervous and lose sight of their long-term investment goals. They are often tempted to postpone new investment, and even to sell their current holdings with the aim of reinvesting when the stock market stabilises.

However, if investors are able to take a long-term view, it is often best to hold onto investments through periods of volatility.

### The pitfalls of market timing

Of course, all investors would like to be able to predict the movements of the market, buying at the bottom and selling at the top. This is called market timing.

Unfortunately, it is very difficult to time movements in and out of the market, particularly in periods of extreme volatility. And getting it wrong can significantly affect the performance of investments.

Selling at the first sign of a downturn can prove particularly bad. Sharp falls in markets are often followed by sharp gains. While it may be tempting for investors fearing further losses to sell their investments, they risk locking in losses and missing out on gains.

### In for the long haul

The long-term performance of equities demonstrates that there is no need to time the markets; it's enough just to be in the markets. Research shows that investments made when the market has already begun to recover, and those made when it is still falling, have still paid dividends.

In contrast, waiting for a better time to invest can cost investors dearly. As the graph below illustrates, investors who remained fully invested in the UK market over the last five years would have received returns in excess of 60%. In contrast, investors who missed out on the ten best days would have seen their returns cut to just 40%, while those who missed the best 40 days would have made just 4%.

Many of the stock market's best days have come immediately after sharp falls.

### FTSE All-Share performance over the past five years



Source: Bloomberg/JPM

And this doesn't only apply to the UK market. The below table takes the example of other major markets, and shows the pitfalls of trying to time the markets and getting it wrong.

### Returns over five years - effect of missing best days

Market	Index	Fully invested	Missing best 10 days	Missing best 40 days
UK	FTSE All Share	63.4	40.0	3.9
US	S&P 500	56.4	11.6	-39.2
Global	MSCI World	63.7	21.6	-26.2

Source: Bloomberg/Datastream. Returns from 01/09/02 to 28/08/07.

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