Perpetual

The real value of investing in shares

2011

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Contents

A quality sharemarket investment can lead to both capital growth and income over time.

What are shares?

What are shares?

A share is part ownership in a company. Shares can be for a private or public company. Publicly listed companies are more liquid (ie there are people looking to buy your investment should you wish to sell) as they trade on an exchange. This allows you to invest in many companies, in many industries.

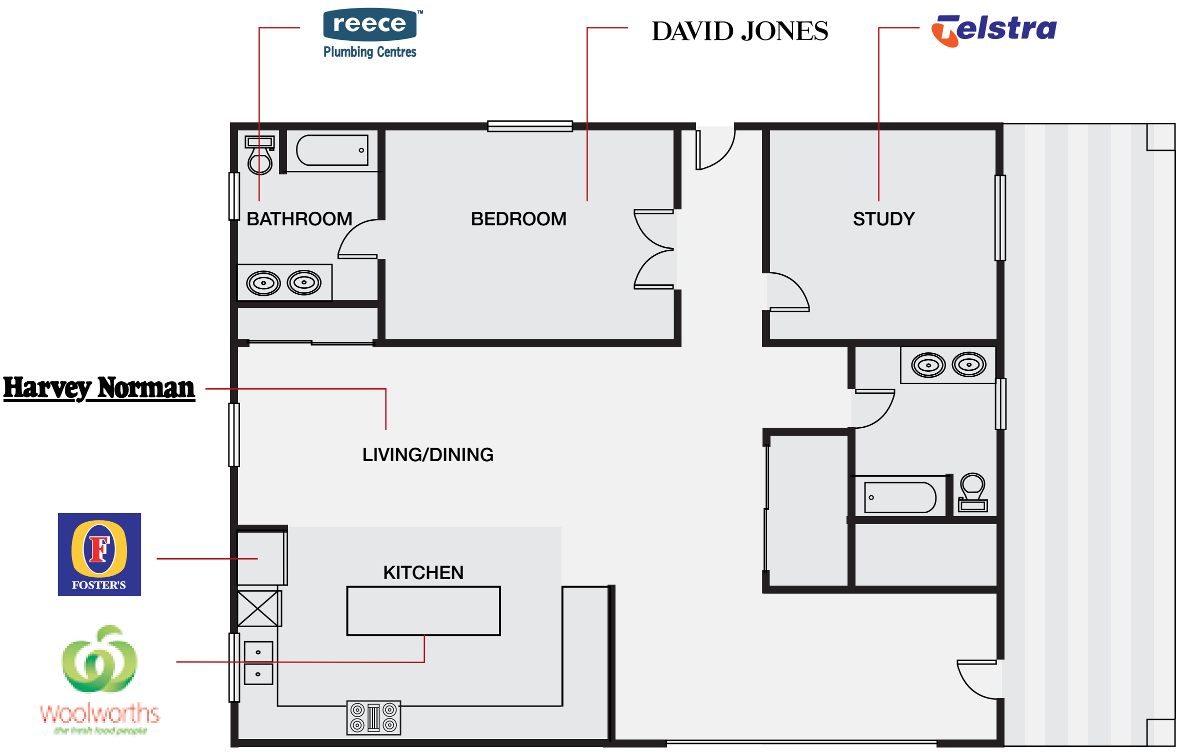
You can buy shares directly on the sharemarket or via a managed fund. A quality sharemarket investment can lead to both capital growth and income over time.

You can invest in household brands

Next time you walk in your front door, take a look at the brand names around your home. Do you have a lounge from Harvey Norman or a Telstra phone line? Are there groceries from Woolworths in your kitchen? These are all the products of companies that are listed on the Australian Securities Exchange (ASX).

You could share in the future profitability of these and other companies by investing in shares.

Figure 1 – Common brands around the home



Key point

The sharemarket

The sharemarket is a market in which buyers and sellers come together to buy and sell shares. In Australia, the leading market for shares is the Australian Securities Exchange. It is made up of close to 2,000 companies. It is the eighth largest sharemarket in the world, and the second largest in the Asia-Pacific region behind Japan (as per MSCI World weightings, 31 December 2010).

Investing in shares for capital growth

Shares can provide capital growth

If you plan to invest for the medium to long term (five to seven years), you might be looking for an investment that increases in value over time. This is called capital growth. Shares can provide capital growth through increases in their market price. Under normal conditions, the movement in a company's share price reflects changing expectations of its profits. That is, earnings per share directly influence a company's price per share.

When a company makes a profit, it must decide how to distribute it. For example, it might pay a portion of the profit to shareholders in dividends, or reinvest 100% back into the company to finance expansion, new technology or equipment.

The ability to reinvest in the company to promote greater growth and future profit (and dividends) can result in higher share prices — the benefit of which is passed on to shareholders. And as a company's profits improve over time, demand for the company's shares increases, pushing up share prices and providing more capital growth (Figure 2).

Shares have different characteristics – some shares may provide more income, while others may provide more capital growth.

For instance, if you had invested $10,000 in the sharemarket at the end of December 1995, the value of your money would have quadrupled over the 15 years to December 2010 – see Figure 3.

Figure 2 – A company must decide how to distribute profits

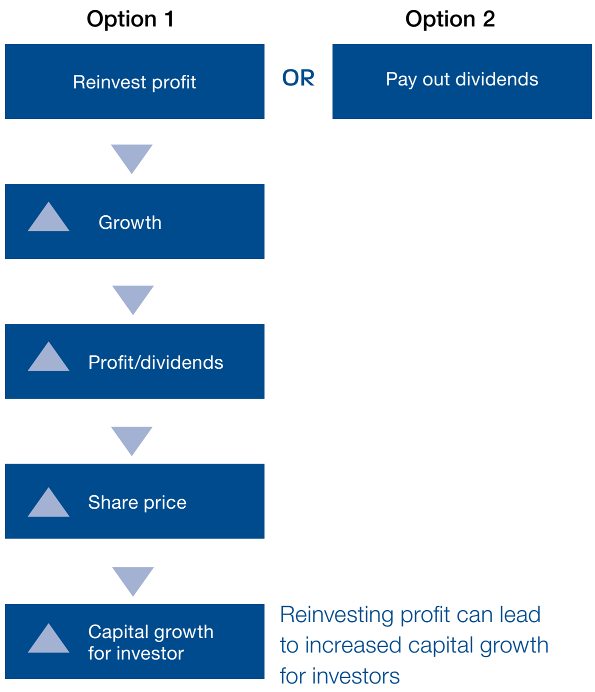
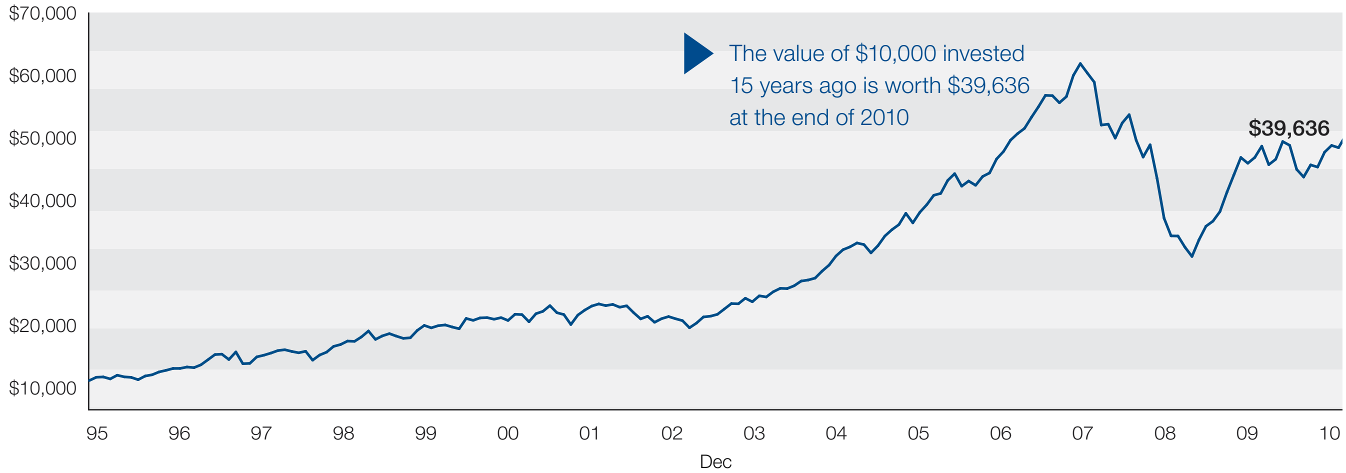


Figure 3 – Shares can provide capital growth
Growth of the Australian sharemarket (dividends reinvested)



Source: Datastream. As at 31 December 2010. As measured by the Blended All Ordinaries Accumulation Index. Post 31/3/2000 S&P/ASX All Ordinaries Accumulation Index. Prior to 31/3/2000 ASX All Ordinaries Accumulation Index. Past performance is not indicative of future performance.

It is important to note how inflation erodes your purchasing power




	Milk	Bread	Beer	Car
1970	$0.25	$0.21	$0.22	$2,967
2010	$3.73	$3.79	$3.31	$39,990

Source: ABS Data cube 6403.0.55.001, www.holden.com.au. As at 31 December 2010.

Capital growth can protect against inflation

Inflation erodes your purchasing power, and can also diminish your investment returns. But investments that provide capital growth help protect your money against inflation.

Figure 4 shows the relative performance of an Australian managed share fund, the Perpetual Industrial Share Fund, compared to cash. You can see that over the long term the managed share fund's investment return has been significantly higher than inflation, unlike the cash return. This is due to the share fund's combination of capital growth and income. However, there are some periods where returns in cash are greater than shares. These do not typically last too long and usually occur in periods of declining share prices.

It's very important to protect your savings with an investment strategy that places some of your money in growth assets, such as shares. The longer your investment timeframe, the more important growth assets become.

Example

The effect of inflation

Peter has invested $10,000 in cash and receives a one year return of 5%. The inflation rate is 3%. Peter's 'real' return after inflation is 2%.

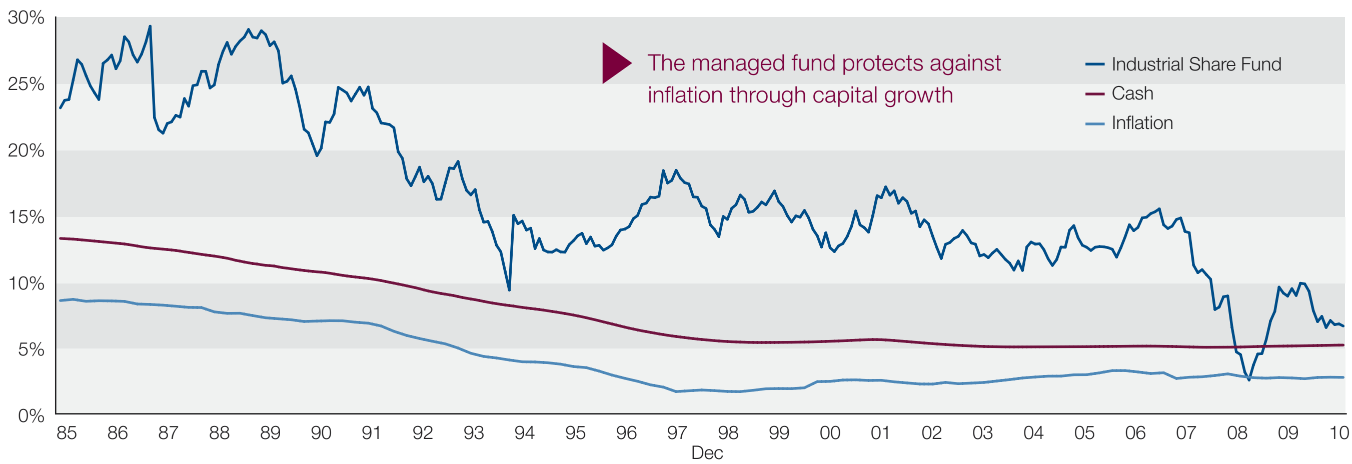
5% interest – 3% inflation = 2% real return

Paul has also invested $10,000, but in shares. At the end of year one, he receives dividend income of 5% plus capital growth of 5%. Before inflation, his total return is 10%. His 'real' return after inflation is 7%.

5% income + 5% growth = 10% return – 3% inflation = 7% real return

This example demonstrates how, even if inflation has eaten into your investment income, capital growth can provide some protection.

Figure 4 – Capital growth can protect against inflation
Perpetual's Industrial Share Fund vs cash (7 year rolling annualised returns)



Source: Reserve Bank of Australia (RBA) and Perpetual. As at 31 December 2010. Cash is calculated using the RBA target cash rate since January 1990. Prior to this the 90-day Bank Bill is used as a proxy for the cash rate. Total return shown for the Perpetual Industrial Share Fund has been calculated using exit prices after taking into account all of Perpetual's ongoing fees and assuming reinvestment of distributions. No allowance has been made for taxation. Past performance is not indicative of future performance.

Investing in shares for income

Shares can provide income

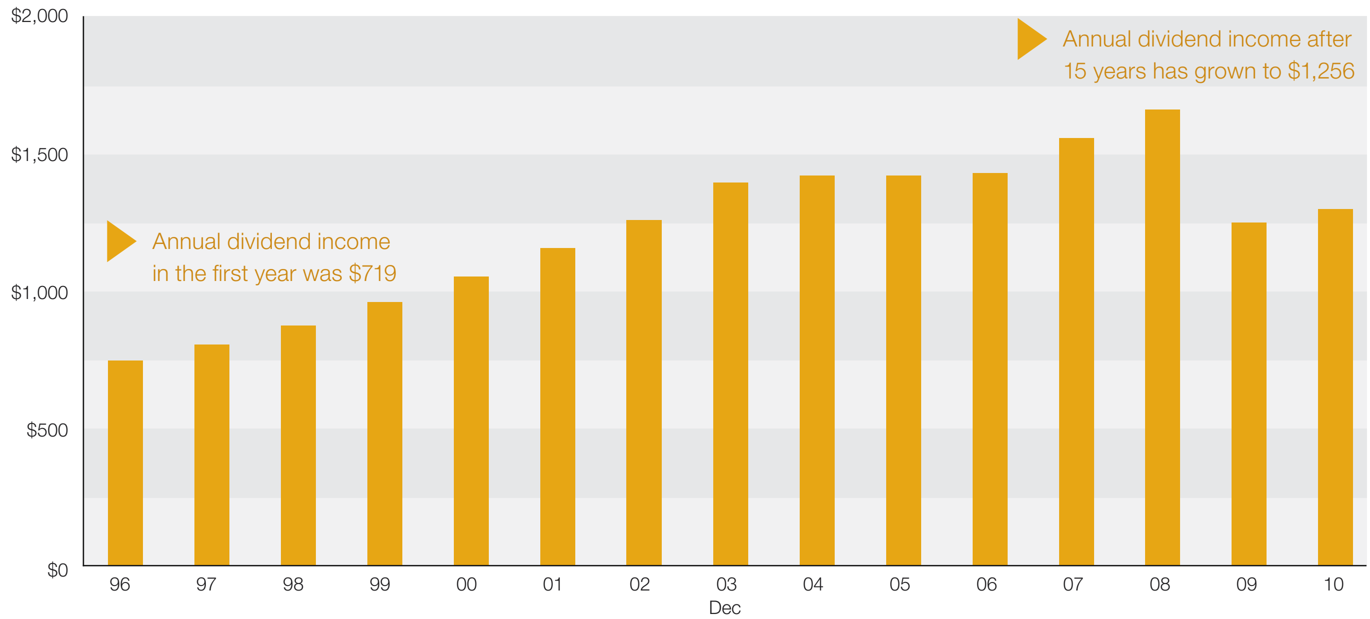
Shares can provide capital growth, but did you know that they can also provide you with a strong and steady income over the long term? They may also be tax-effective.

How you earn income from shares

The income you receive from shares is in the form of dividends. Dividends can grow over time as the capital value of your investment also grows.

For example, if you invested $10,000 in the National Australia Bank (NAB) fifteen years ago, the income (or dividend) that you received in the first year was $719. Over time, the share price of NAB has risen, and so too has your dividend income. At the end of 2010, your annual dividend income had grown to $1,256 (Figure 5). Over the fifteen years you would have received a total of $17,653 in dividend income.

Figure 5 – Shares can provide a steadily growing income stream
$10,000 invested in NAB – growth in dividends



Adjusted for bonus issues.

Source: RBS Equities. As at 31 December 2010.

A growing income stream

When it comes to an investment that pays regular income, you may think first of a term deposit. Although a term deposit can provide regular income, it's important to remember that it doesn't offer any capital growth, so the income doesn't grow over time as it does for shares.

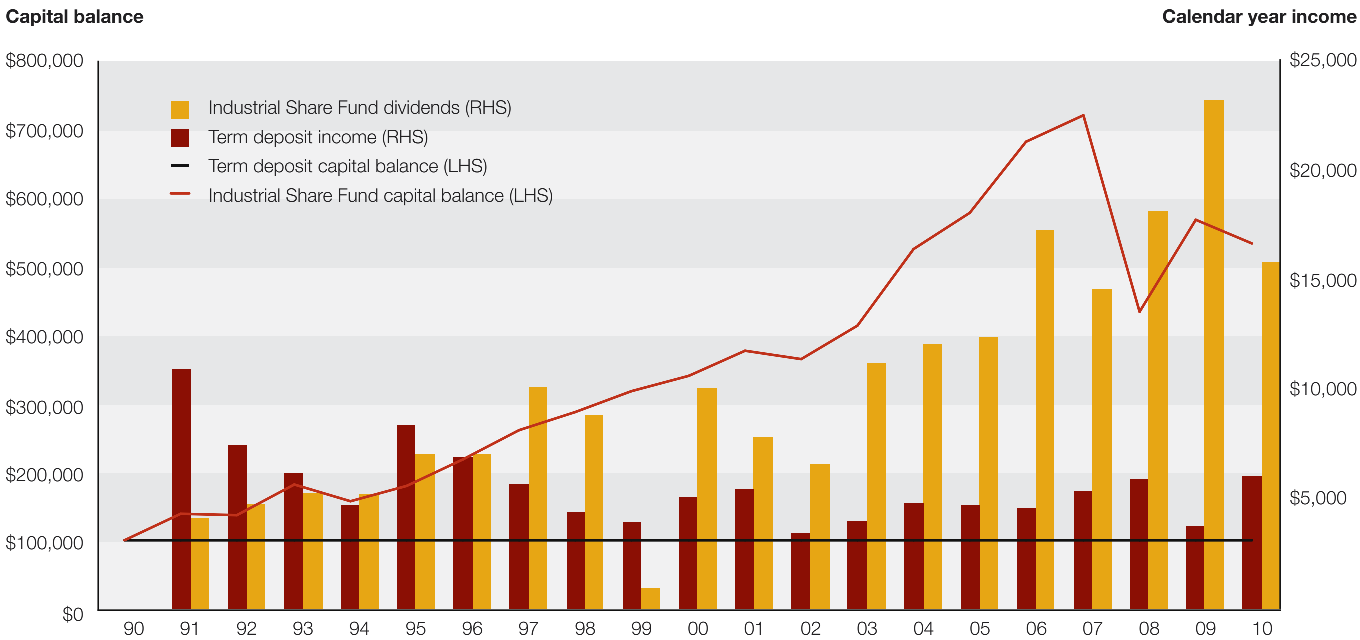
Figure 6 shows the growth in the dividend component of distributions and the growth in the capital value of the Perpetual Industrial Share Fund, compared to the interest and capital value of term deposits over the past 20 years.

If you had invested $100,000 in the Fund at the end of December 1990, you would have earned over $200,000 from tax-effective dividends by the end of December 2010, while the value of your investment would have increased around 5 times. However, if you had invested in term deposits they would have earned around $111,000 in interest and the value of your investment would have stayed the same.

The best of both worlds

Clearly, the total income and capital gain earned from the Perpetual Industrial Share Fund over the period far exceeds the total income and capital gain earned from term deposits, even though the initial investment was the same.

Figure 6: The Perpetual Industrial Share Fund has been a source of income and capital growth
$100,000 invested in the Perpetual Industrial Share Fund and term deposits (31 December 1990 to 2010)



Source: Perpetual and Reserve Bank of Australia. Methodology: Years to the end of December. Income drawn down annually. To calculate dividends, the net realised capital gains portion of WealthFocus Industrial Share Fund distributions, excluding capital gains tax, have been reinvested. These reinvestments have been made at the application price, taking into account buy spreads. Dividends (and the benefits of imputation credits) have not been reinvested and are expressed as an annual payment of the same timing as the term deposit. Results are net of fees. Past performance is not indicative of future performance.

Share income can be tax-effective

The income you receive from shares can also be very tax-effective. This is because Australian share income is taxed favourably through 'dividend imputation' (see box). Income assets like cash and term deposits do not receive the same favourable tax treatment.

Key point

Dividend imputation

Dividend imputation allows a shareholder to receive a tax credit for their dividends if the company has already paid full company tax of 30%. This is called an 'imputation credit'. Any dividends that carry these tax credits are known as 'franked dividends' (Figure 8).

If you have a marginal tax rate (MTR) of more than 30%, you pay tax on your investment at your MTR minus 30% (the tax already paid by the company).

For example, since Bob's MTR is 46.5% pa (including medicare levy), he pays tax on his investment at a rate of 16.5% pa. If his MTR was under 30% pa, he would receive a tax credit which he could use to reduce the amount of tax he pays on other income.

The same rules apply if you invest in shares through a managed fund.

Example

Benefits of dividend imputation

Bob and Bill each invest $10,000. Bob invests his money in shares, while Bill chooses to invest in a term deposit. The shares and term deposit both generate income of $500 (a return of 5% on the investment amount). Bill and Bob pay tax at 46.5% (including Medicare levy). Figure 7 shows the after-tax result.

While Bob and Bill are both paying tax at the same rate, their tax outcomes are quite different. Overall, Bob has paid $115 less tax than Bill. This is because Bob received an imputation credit on the dividend income from his shares, while Bill did not receive any credit for his investment income. The net result is that Bob's after tax income is significantly higher ($382) than Bill's ($267).

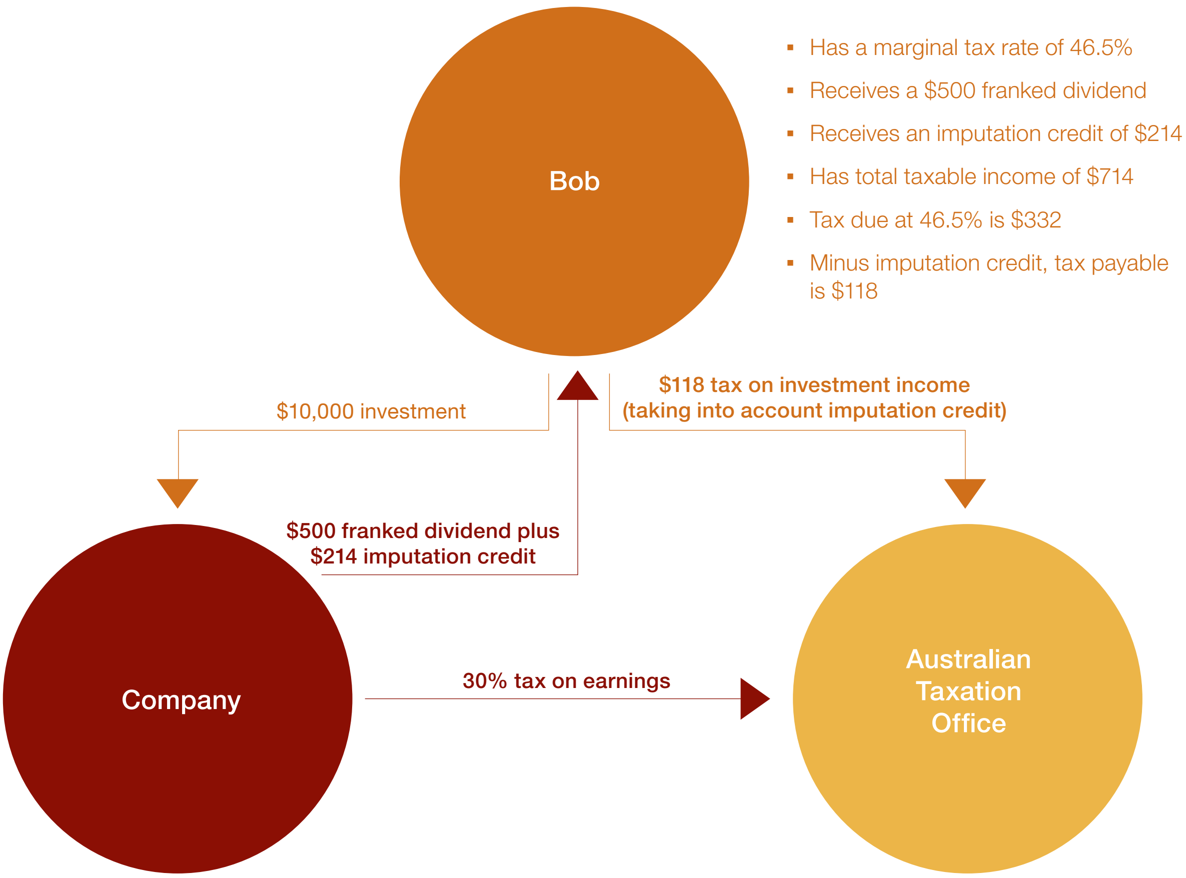
Figure 7 – the benefits of dividend imputation

Marginal tax rate 46.5% pa

	Bob (Shares)	Bill (Term deposit)
Initial investment	$10,000	$10,000
Dividend income from shares	$500	–
Interest return from term deposit	–	$500
Imputation credit	$214	–
Taxable income	**$714**	**$500**
Tax due at 46.5%	$332	$233
Minus imputation credit	-$214	–
Tax payable	$118	$233
After tax income	**$382**	**$267**

Source: Perpetual.

Figure 8 – How dividend imputation works
Bob's $10,000 investment



Source: Perpetual.

Shares can be volatile – don’t panic

The Australian sharemarket is volatile

The Australian sharemarket fluctuates every day, because every day thousands of buyers and sellers of shares trade them. Sometimes, specific events will cause the value of certain shares to rise or fall. You may remember some positive events that caused the sharemarket to rise (eg tech boom, resources boom). You might also remember some negative events that caused it to fall (Asian financial crisis, ‘Tech Wreck’ and global financial crisis).

But overall, the value of the Australian sharemarket has risen substantially over time.

In fact, the value of $50,000 invested at the end of 1995 is worth $176,888 at the end of 2010, 15 years later (Figure 9). This is an average return of 8.8% pa (assuming dividends are reinvested).

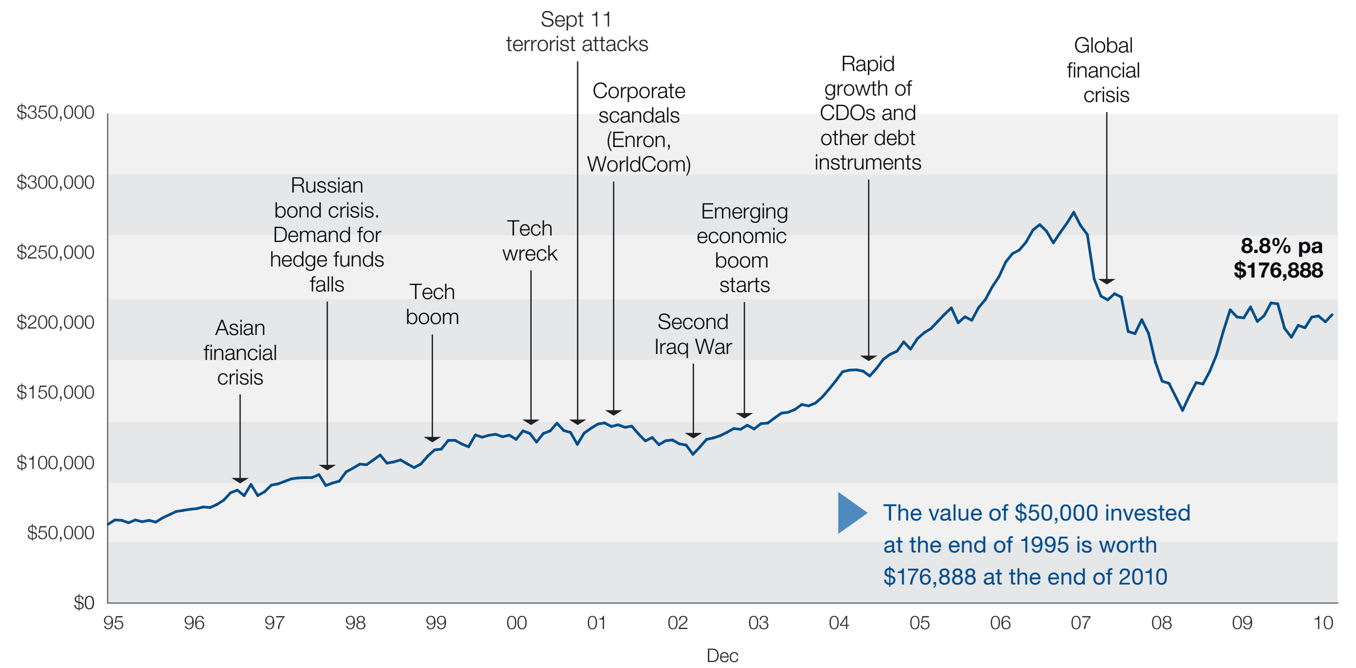
Historically, markets have always recovered

The Australian sharemarket began trading in 1875. It has delivered positive annual returns in 97 out of 135 years. This is 72% of the years. Of these positive returns, most were between 0% and 20% pa (Figure 10).

There are, of course, years when the sharemarket has delivered extraordinary positives (over 40%) or negatives (under -40%). But it’s important to remember that these results are rare.

While the swings in the market might look extreme over one year, they are less pronounced over the long term. Traditionally sharemarkets have recovered from short-term setbacks with significantly higher gains.

Figure 9 – Growth of the Australian sharemarket
S&P/ASX 300 Industrial Accumulation Index



Source: Perpetual. As at 31 December 2010. No allowance has been made for taxation. Past performance is not indicative of future performance.

Volatility is not necessarily a bad thing

Figure 10 shows just how volatile shares can be. For instance in the 1930s:

1. Shares fell by more than 30% in 1930.
2. But for much of the decade returns were very strong, ranging between 10% and 20%.
3. They even rose as high as 21% in 1933.

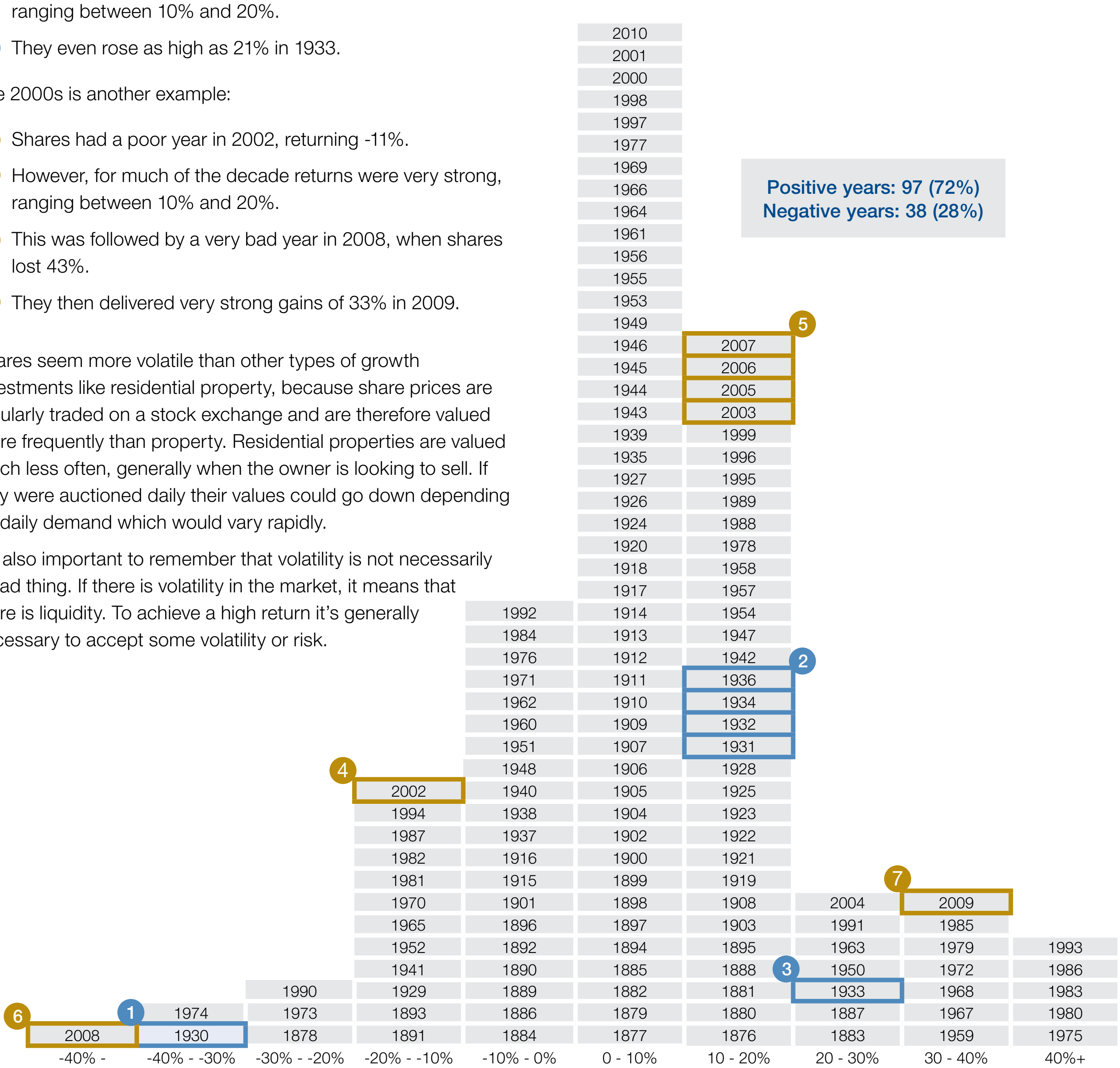
The 2000s is another example:

4. Shares had a poor year in 2002, returning -11%.
5. However, for much of the decade returns were very strong, ranging between 10% and 20%.
6. This was followed by a very bad year in 2008, when shares lost 43%.
7. They then delivered very strong gains of 33% in 2009.

Shares seem more volatile than other types of growth investments like residential property, because share prices are regularly traded on a stock exchange and are therefore valued more frequently than property. Residential properties are valued much less often, generally when the owner is looking to sell. If they were auctioned daily their values could go down depending on daily demand which would vary rapidly.

It's also important to remember that volatility is not necessarily a bad thing. If there is volatility in the market, it means that there is liquidity. To achieve a high return it's generally necessary to accept some volatility or risk.

Figure 10 – Markets have always recovered
Annual performance of the Blended All Ordinaries Price Index (1876-2010)



Source: Goldman Sachs JB Were and Australian Securities Exchange as at 31 December 2010. As measured by the Blended All Ordinaries Price Index (1875 to 1936 the Commercial and Industrials Price Index, 1936 to 1979 the ASX All Ordinaries Price Index and from 1979 the S&P/ASX All Ordinaries Price Index).

The key to successful investing is time, not timing

Many investors try to 'time' their investments into the strongest performing asset class of any given period to capture the best returns. However, the key to successful investing is time, not timing.

The perils of market timing

While you might be able to pick the future performance of a sports team based on last year's performance, this is often because you know the team, you know the competition and the environment doesn't change much (and even then it is often hard). However, with investment markets, it's more difficult. Factors such as interest rates, exchange rates, commodity prices and consumer spending all come into play at a global and local level to influence performance. As a result, last year's winner can easily become 'today's loser'.

Some investors can get it right some of the time. But more often than not, 'market timers' sell when a market is low and are out of the market when the inevitable rally occurs. In this way, market timing exposes you to the very risks you are trying to avoid.

Example

From best performing asset class to worst, within a year

Australian shares

- Best asset class in 1991 (34%) ▶ Worst in 1992 (-2%)
- Best asset class in 1993 (45%) ▶ Worst in 1994 (-9%)

International shares

- Best asset class in 1995 (27%) ▶ Worst in 1996 (7%)
- Best asset class in 1999 (17%) ▶ Worst in 2000 (3%)

Listed property

- Best asset class in 2006 (34%) ▶ Worst in 2007 (-8%)

Cash

- Best asset class in 1994 (5%) ▶ Worst in 1995 (8%)

Source: Datastream. Best and worst selected from Australian shares, International shares, Australian listed property, Australian fixed income and cash.

Key point

Asset classes

Shares are one type of 'asset class'. Other types include property, fixed income and cash. Each of these asset classes have different risk/return profiles. Generally income assets (like fixed income and cash) can be less risky than growth assets (such as shares and property).

The benefits of dollar cost averaging

Instead of trying to 'time' the market, you may be better off dollar cost averaging. Dollar cost averaging is an investment approach where you invest the same amount of money on a regular basis, usually monthly, into a share investment. It takes advantage of the only certainty of the sharemarket – that prices will continue to rise and fall.

Dollar cost averaging is a convenient and flexible way for investors to gain additional exposure to investments over time. The benefit of this strategy is that it reduces the risk of investing a large amount of money in a single investment at the wrong time.

By investing a fixed amount at set intervals, you are smoothing the ups and downs of the sharemarket. Your fixed amount will buy more units when the prices are low and fewer units when the prices are high. This means the average price paid can be lower than the average market price (Figure 11).

Adopt a regular savings plan

A savings plan is a disciplined method of investing and also an excellent way to benefit from dollar cost averaging. With a savings plan, a set amount of money is automatically debited from your bank account each fortnight or month.

You could use a savings plan to save for your children's education, a holiday, a new car, or for your retirement.

Discipline is the key – not large sums

You do not need a large amount of money to be a successful sharemarket investor. What is important is making a commitment to a regular savings plan.

Example

Dollar cost averaging

Jim establishes a dollar cost averaging plan. He invests $200 per month in XYZ, a listed Australian company, for 10 months (Column A).

Jim's regular investment is made at the same time each month. Each month, the market price of XYZ shares has varied (Column B).

This affects the number of shares that Jim receives for his $200 investment each month (Column C).

Figure 11 – The average price you pay per share can be lower

A	B	C
Regular monthly investment	Market price of XYZ shares each month	No. of XYZ shares received each month
$200	$10	20
$200	$9	22
$200	$7	29
$200	$6	33
$200	$6	33
$200	$6	33
$200	$6	33
$200	$7	29
$200	$9	22
$200	$10	20
Total $2,000	Average $7.60	Total 274

Source: Perpetual. Does not include transaction costs eg brokerage.

Outcome:

Jim has purchased 274 shares for $2,000 over ten months. The average price of XYZ shares Jim purchased is **$7.29** (equal to $2,000 divided by 274). This is less than the average market price of XYZ shares, which is **$7.60** (average of Column B).

By making smaller, regular, investments Jim has purchased more shares overall for a lower price.

Diversification can smooth the ride

Good returns offset poor returns

A much better strategy than attempting to time the market is to diversify your money across a range of asset classes. By placing your money in a number of asset classes, good returns received from one investment can offset the bad performance of another over particular periods.

Figure 12 shows the three-year returns of different asset classes since 1995, and the difference between the best and worst performing asset classes.

It shows that even when the returns of most asset classes are negative, the difference between the best and worst is still substantial.

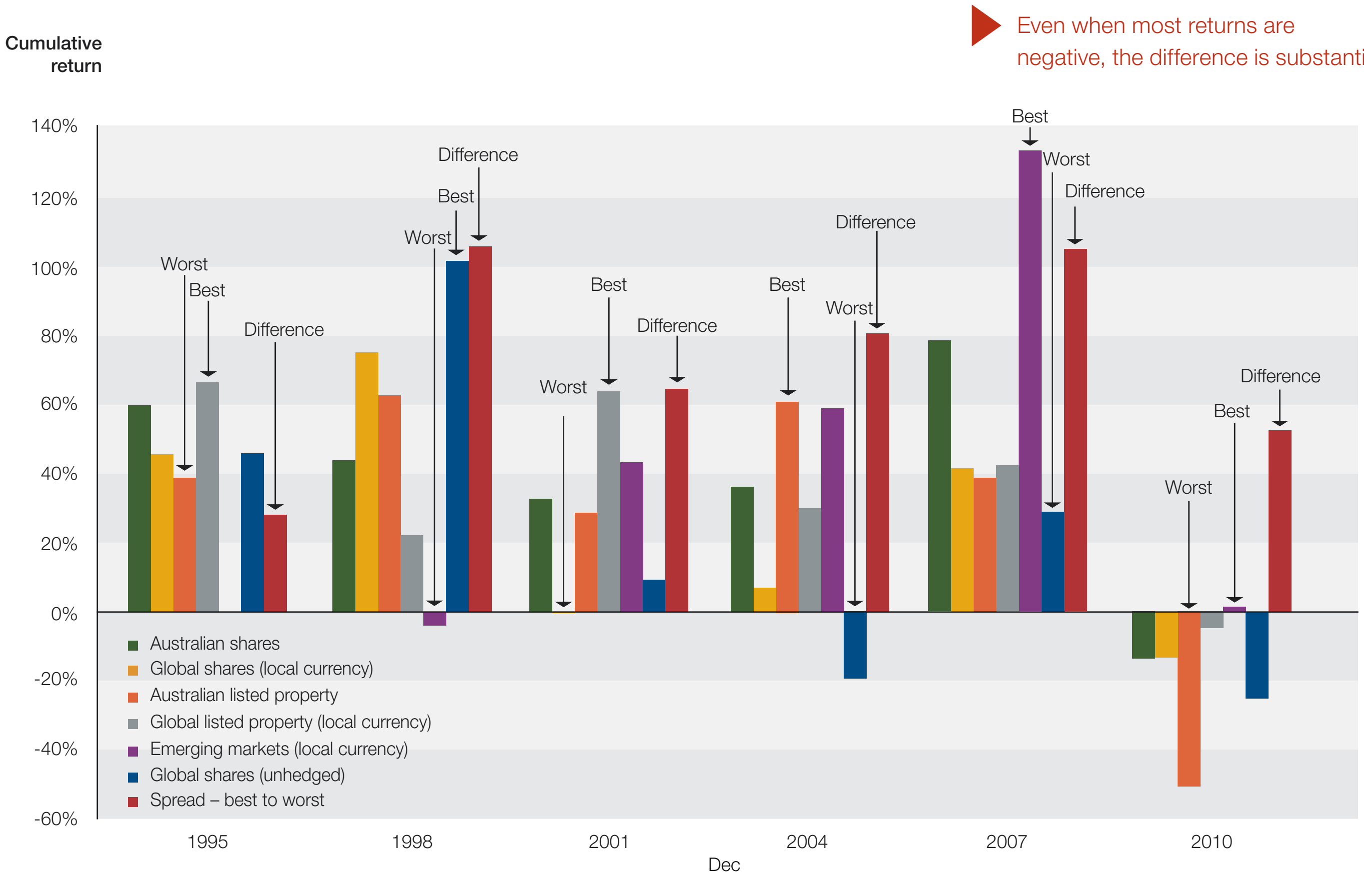
Key point

Diversification

Diversification is like having a balanced diet. You wouldn't eat steak every day for breakfast, lunch and dinner because you would be missing out on the benefits of other food groups. See our guide to 'Why diversification is important' for more on the benefits of diversification.

Figure 12 – The benefits of diversification are clear
Cumulative 3-year return of each growth asset class since 1995

Even when most returns are negative, the difference is substantial



Source: Datastream, Mercer, IRESS. As at 31 December 2010. Emerging markets (local currency) cumulative 3-year return to 1995 not available.

Example

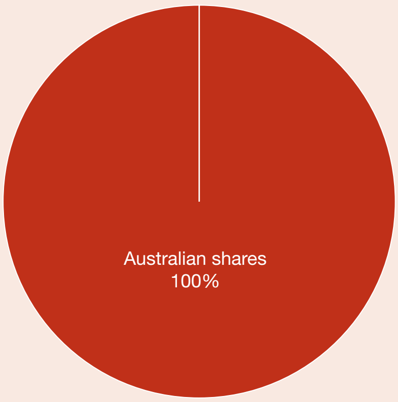
The benefit of a balanced portfolio

Andrew and Richard set up investment portfolios in December 1985. Andrew's portfolio is made up of 100% Australian shares. Richard's portfolio is made up of 70% growth assets (40% Australian shares, 25% international shares, 5% property) and 30% income assets (20% fixed interest, 10% cash).

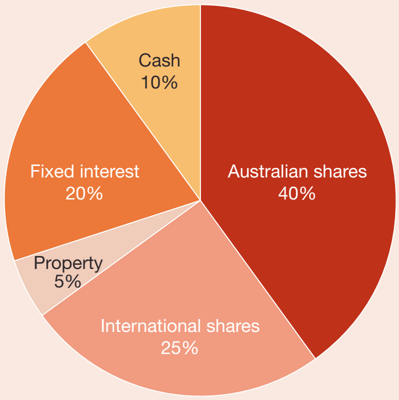
While their returns at the end of December 2010 are very similar, Richard's portfolio was significantly less volatile because it was diversified across asset classes.

Figure 13 – The benefit of a balanced portfolio

Andrew's portfolio



Richard's portfolio



	Andrew (100% Australian shares)
Return % pa	10.9
Risk (volatility) % pa	16.7
Worst one year return (%)	-41.8
Worst cumulative three year return (%)	-28.0

	Richard (Balanced, 70% growth)
Return % pa	9.8
Risk (volatility) % pa	9.5
Worst one year return (%)	-24.0
Worst cumulative three year return (%)	-15.4

Source: Datastream. Buy/sell spreads for rebalancing assumed to be 0.30% each way on Australian shares, international shares and property and 0.1% each way on Australian fixed interest.

Reweighting to reduce volatility and improve performance

When you establish a diversified portfolio, it is tempting to leave your money in the asset classes which are performing well and to ignore the asset classes which are not performing as strongly.

However, to successfully maintain a diversified portfolio, you need to regularly review and reweight your investment. This can be done with the assistance of your financial adviser.

Reweighting a balanced portfolio can reduce volatility and improve performance.

Your financial adviser will be able to help you select an individual asset allocation that is appropriate for your risk profile, investment timeframe and income requirements.

Example

Reweighting a portfolio

In the previous example, Richard invested $100,000 in December 1985 in a portfolio made up of:

- 40% Australian shares (measured by the Blended All Ordinaries Index)
- 25% international shares (measured by the MSCI World ex Australia Accumulation Index $A)
- 5% listed property trusts (measured by the Blended Property Trusts Accumulation Index)
- 20% fixed interest (measured by UBSA Composite Bond Index)
- 10% cash (measured by UBSA Bank Bill Index)

Richard's financial adviser reweighted his portfolio every month – in other words, the proportion invested in each asset class was maintained regardless of changes in valuation. Over the 25-year investment period, Richard's initial investment of $100,000 has increased in value to $1,034,386 (to 31 December 2010).

Source: Datastream. Perpetual.

Key point

Reweighting

Reweighting means taking your investment portfolio back to its original proportional distribution across each asset class. The benefit of reweighting is that it reduces the volatility of your returns. It also reduces the temptation to chase each year's best performing asset class, which often means you're buying and selling at precisely the wrong times.

Diversification is important for income

Many retirees rely on investment returns to provide them with an income to meet their living expenses. Many invest in short-term 'income' assets for this reason, as they perceive them to be the safest form of investment.

Short-term 'income' assets like cash and term deposits generate a return based on interest rates. If interest rates increase, the returns on these income assets also increase. And if interest rates fall, the returns on these income assets also fall.

Different investors can be affected differently by interest rate movements, eg income investors versus those who have borrowed to invest (geared) for growth (Figure 14). This is why diversification is important across asset classes.

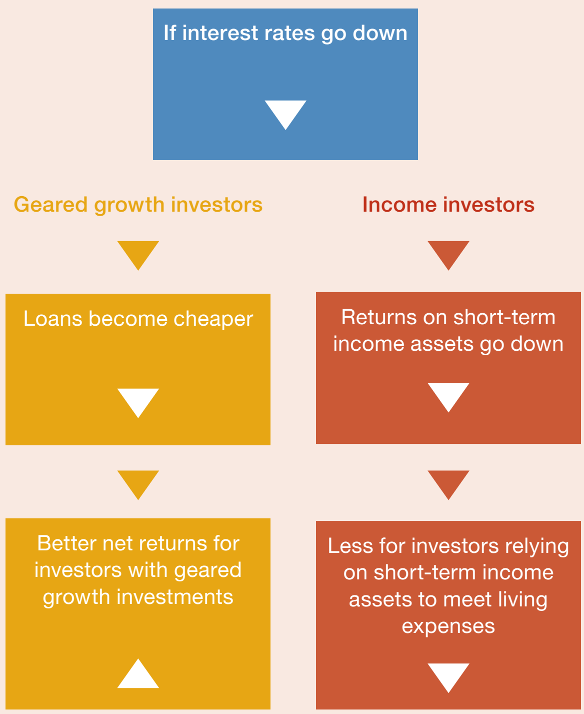
Example

The effect of interest rates on an income investor

Joe, a retiree, has living costs of around $25,000 pa. He invested his retirement savings of $200,000 in an interest-bearing term deposit in early 1990 at a rate of 18% pa. This met his retirement income needs.

However, by late 2009 interest rates had fallen dramatically. He could no longer meet his income needs with the interest from his short-term income investments alone.

Figure 14 – The effect of falling interest rates



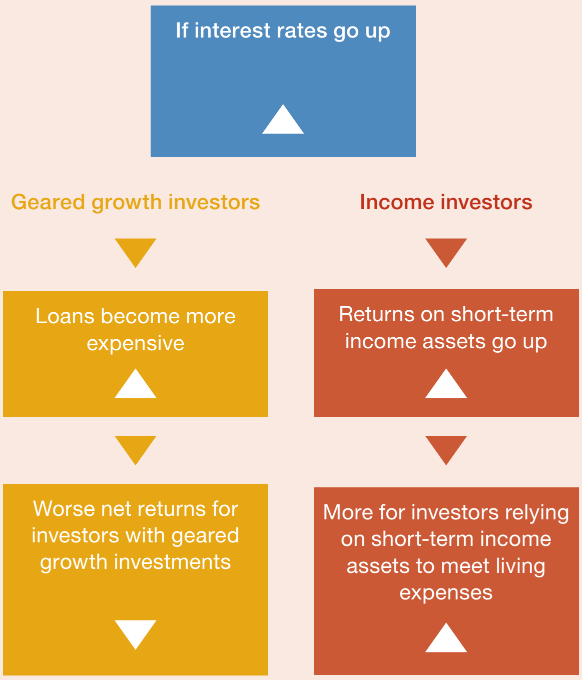
Example

The effect of interest rates on a geared portfolio

Rita borrowed $100,000 five years ago to purchase a portfolio of Australian shares. Her borrowing cost at the time was 10% pa, or $10,000.

Five years later, due to interest rate movements, Rita's cost of borrowing had risen to 15% pa, or $15,000. Rita was negatively affected by the rise in interest rates, as it meant the cost of financing her investment was more expensive and the net return of her investment was less.

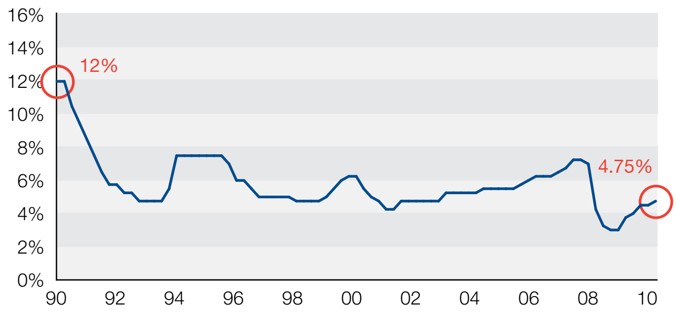
Figure 15 – The effect of rising interest rates



The cash rollercoaster

Figure 16 shows the movement of interest rates since the end of December 1990. Over this period they have ranged from a high of 12% to a low of 3% at the end of December 2010. If you were relying on interest rates only to provide you with a 'salary' to meet your cost of living, you wouldn't want to see your salary drop so steeply. This is why it's important to have some of your portfolio allocated to investments that can provide capital growth and a growing income stream over time – like shares.

Figure 16 – The cash rollercoaster
Interest rates have moved dramatically over the past 20 years



Source: Reserve Bank of Australia.
Data from 31 December 1990 to 31 December 2010.

Understanding risk

Australian and international shares form a very important part of a well-diversified portfolio. The percentage of your portfolio that you invest in shares will depend on your investment timeframe and your tolerance to the volatility of the sharemarket.

Shares have historically demonstrated greater volatility and can be considered to have higher investment risk than other asset classes such as mortgages, fixed interest securities or cash.

As such, shares are ideally suited to investors with a minimum investment timeframe of five years. For such investors, short-term volatility isn't important. What is important is that:

- shares tend to regain any short-term lost performance and generally outperform all other asset classes over the long term
- shares can provide long-term capital growth
- shares can provide a strong and growing income stream.

By not investing in growth assets such as shares, you face the greater risk of earning less than inflation or not effectively diversifying your assets.

Key point

Risk profile

Your risk profile is determined by your investment time horizon, your expectations for returns and how much risk (volatility) you can tolerate. Once you identify your risk profile, you can select the type of investments that suit you.

Which type of share ownership is right for me?

Share ownership can be divided into two categories:

- Direct ownership – where you buy shares directly, usually through a stockbroker (Figure 18)
- Indirect ownership – where you buy units in a managed fund which invests in shares on your behalf (Figure 19).

What are managed funds?

A managed fund pools your money with money from other investors to form an investment fund. Specialist investment managers then invest the money in the fund on your behalf.

So instead of having $2,000 or even $20,000 to invest, your money has access to the buying power of millions of dollars. This buying power means you can benefit from opportunities normally only available to large corporations or those with extensive knowledge.

Managed funds come in many shapes and sizes. Some funds invest in just one type of investment such as Australian shares, while others known as diversified funds invest across a range of asset classes including Australian shares, international shares, fixed income, property securities and cash.

How are managed funds structured?

Most managed funds are structured as unit trusts. When you invest, your money buys 'units' in a fund. The number of units you receive depends on the amount you invest and the current unit price. Put simply, if a unit in a fund was worth $1 and you invested $2,000, you would receive 2,000 units (less the value of an entry fee and transaction costs, if charged).

The unit price reflects the value of the fund's investments. If the value of the investments rises, the unit price rises. Likewise, if the value of the investments falls, the unit price falls. In many funds, the unit price can go up and down each day depending on the changing value of the underlying investments. To determine the value of your investment, simply multiply the current unit price by the number of units you hold. Companies that offer managed funds can provide you the latest exit unit price over the phone or on their website.

Which investment is right for me?

When deciding whether to invest in shares directly or through a managed fund, you need to weigh up the benefits and drawbacks of each method of investing (Figure 17).

Figure 17 – Direct shares versus managed funds

	Direct ownership	Managed funds
Research	Selecting the right shares takes careful research and knowledge. You could do your own research and select the shares yourself. You could also pay a stockbroker for their expertise.	By investing in a managed fund, you are outsourcing the stock selection to the fund managers – trained investment specialists who constantly research and monitor the investment markets.
Time management	The administration that comes with holding shares directly can be time consuming, especially if you have several stocks in your portfolio.	When you invest in a managed fund, your fund manager will handle all the paperwork and administration, provide you with regular information on the fund's performance and provide annual tax statements and tax guides.
Diversification	A truly diversified portfolio of shares, property, fixed interest and cash can be very difficult for an individual investor to achieve. You need to invest in several shares to gain diversification benefits.	One of the greatest benefits of managed funds is that they allow you to diversify your investments. Managed funds can offer diversification benefits across asset classes, within asset classes, or around the world.
Cost	A truly diversified share portfolio can be expensive.	Managed funds are a low cost way to access professional investment expertise.

Figure 18 – Investing in shares directly

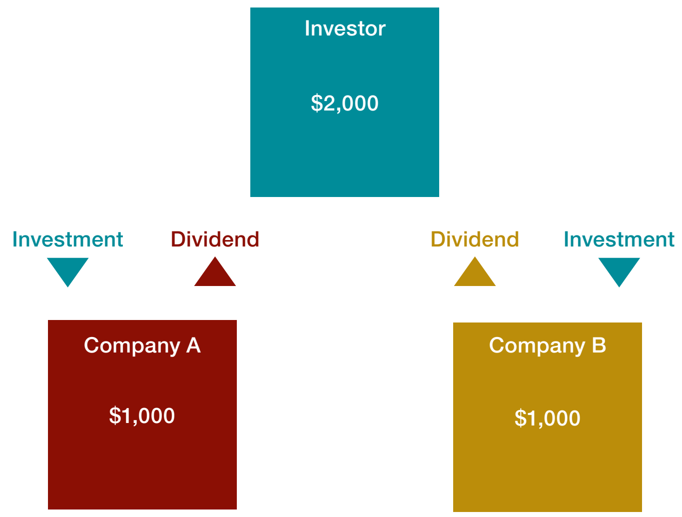
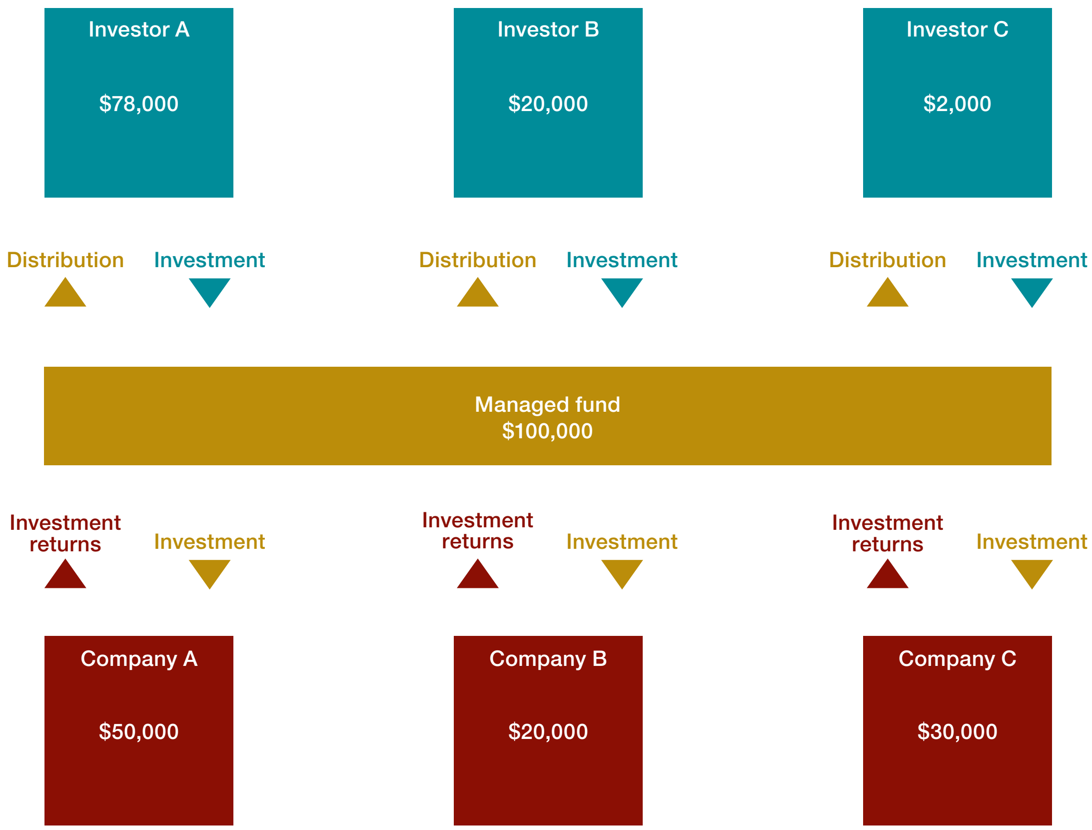


Figure 19 – Investing in shares through a managed fund



Fund managers use an index as a 'benchmark' or performance standard.

Monitoring the performance

Monitoring the performance

If you follow movements in the sharemarket, or you own a share investment, you've probably heard of the S&P/ASX 300 Index. You may also have read about fund managers outperforming their various 'benchmark indices'.

What is an index?

An index measures the change in value of a particular group of investments over time. For example, the S&P/ASX All Ordinaries Price Index, the headline index accounting for approximately 95% of the Australian sharemarket, is a measure of the price of the shares of the major companies listed on the ASX.

The other popular Australian index is the S&P/ASX All Ordinaries Accumulation Index. This index measures the total return of the share price movements and dividends (assuming these dividends were reinvested to buy more shares). As dividends are an important feature of a sharemarket investment, the Accumulation Index is a much better gauge of medium- to long-term total performance.

The price and accumulation indices measure the performance of the same companies and record this performance in 'points'.

Benchmark indices

Over time, the S&P/ASX indices have been used as a key tool for the Australian investment community. The All Ordinaries Index is an umbrella index, with six ASX Benchmarking Indices beneath it. The S&P/ASX All Ordinaries Index comprises the largest 500 stocks by average market capitalisation. Its main purpose is to measure the performance of the market.

Fund managers will choose an index for their fund based on how closely the index matches their own stock selection. They will then use this index as a 'benchmark' or performance standard. Some examples of Perpetual's benchmark indices are listed in Figure 20.

Figure 20 – Perpetual's benchmark indices

Perpetual fund	Benchmark
Perpetual Australian Share Fund	S&P/ASX 300 Accumulation Index
Perpetual Industrial Share Fund	S&P/ASX 300 Industrials Accumulation Index
Perpetual Smaller Companies Fund	S&P/ASX Small Ordinaries Accumulation Index
Perpetual Concentrated Equity Fund	S&P/ASX 300 Accumulation Index
Perpetual Geared Australian Fund	S&P/ASX 300 Accumulation Index
Perpetual SHARE-PLUS Long-Short Fund	S&P/ASX 300 Accumulation Index
Perpetual Ethical SRI Fund	S&P/ASX 300 Accumulation Index

About Perpetual

Investing for generations

Perpetual is one of Australia's most experienced investment and trustee groups, with an enduring passion for protecting and growing our clients' wealth.

Founded in Sydney in 1886 as Perpetual Trustees, we have managed and invested our clients' money with integrity and expertise for 125 years.

Today we are one of the Top 100 companies listed on the Australian Securities Exchange, manage investment funds exceeding $27 billion, administer client funds of over $209 billion, and advise clients on over $8 billion of investments (as at 31 December 2010).

We provide quality investment products, financial advice and corporate services to individuals, families, financial advisers and corporates.

More about our investment business

- **Investment products.** We offer a broad range of investment, superannuation and retirement income products. Our choice of investment funds includes all major asset classes, managed by Perpetual or other leading fund managers, as well as diversified and multi-manager funds.
- **Investment management.** We invest in all major asset classes including shares, fixed interest and property. We make active investment decisions based on our intensive analysis of an investment's intrinsic quality, value and risk. Our investment team is one of the most stable and experienced in the industry and has been recognised through many industry awards.

Investing with Perpetual to reach your goals

About Perpetual's Australian share funds

If you're looking for an Australian share investment that can offer long-term capital growth and income, Perpetual's Australian share funds may suit you.

Our Australian shares investment philosophy is to invest in quality companies at attractive prices. We focus our attention on those companies that exhibit characteristics including:

- a track record of earnings and cashflow
- a strong balance sheet and sound capital structure with a conservative level of debt
- quality business
- a sound management team with a strong shareholder focus.

We believe that our disciplined process gives our investors the best chance of achieving consistent returns and dividends over the long term, and peace of mind that these companies will survive even in the most difficult of times.

Our flagship Australian share funds are:

- **Perpetual Industrial Share Fund.** One of Australia's longest running managed funds, investing in quality Australian industrial shares to provide investors with capital growth and consistent and regular income.
- **Perpetual Australian Share Fund.** Also one of Australia's longest running managed funds, investing in quality industrial and resource stocks to provide investors with capital growth and income.
- **Perpetual Concentrated Equity Fund.** A portfolio of fewer stocks, but selected with higher conviction than our flagship Australian share funds. This concentration may lead to short-term volatility.

We also offer specialist Australian share funds, including:

- **Perpetual Geared Australian Fund.** Like Perpetual's Australian Share Fund, but with potential to maximise returns through internal gearing of up to 60%.
- **Perpetual SHARE-PLUS Long-Short Fund.** A portfolio of quality industrial and resource shares that can take short positions in selected Australian shares to enhance returns.
- **Perpetual Ethical SRI Fund.** A portfolio that may match investor's social and ethical beliefs or preferences, without compromising returns over the long term.
- **Perpetual Smaller Companies Fund.** A portfolio of quality companies which, when first acquired, do not rank in the S&P/ASX 50 Index.

For current returns, visit www.perpetual.com.au

To learn more about Perpetual's Australian share funds, please contact your financial adviser or phone Perpetual Investor Services on **1800 022 033**.

Learn more

We have a range of educational tools to help you understand various investment concepts and to give you an overview of our products.

- The real value of investing internationally
- Guide to investing flyers
- Fund profiles
- Sharemarket charts
- Glossary of investment terms

You can find them and additional educational material at **www.perpetual.com.au**

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