

A Balanced Approach to Investing – Michael Lannon

People today are generally more aware and better informed about personal finance and investment than they were in past decades. A plethora of books, magazines and TV shows discuss everything from reduced-fee bank accounts to the ups and downs of international sharemarkets. Ironically, this abundance of information can make it difficult for investors to stay focused on their own investment needs. However the emergence of Internet financial service providers has helped in consolidating a lot of information in one place.

What do I need to consider before investing?

When looking to invest, it's important to have clear investment objectives. For individuals, these could range from needing an income stream to wanting to invest for the future, from getting the most out of your retirement funds to investing for a child's education. Most people have short term as well as long term goals. Different goals require you to consider the different asset classes and their characteristics.

What is the difference between income and growth investments?

Income assets such as term deposits and savings accounts are typically low-risk investments and tend to provide low returns. While they may be an appropriate investment choice for money you will need in the short term (eg for a holiday), they typically do not provide enough growth to adequately counter the effects of tax, fees and inflation in the longer term.

Growth assets such as Australian and international shares have historically offered relatively high total returns, with a higher degree of risk. Though this risk means growth assets can fluctuate in value in the short term, these fluctuations have tended to average out in the longer term, resulting in more consistent returns. Growth assets can therefore be a wise investment in the long term (over five years).

If, like most people, you have both short and long term goals, then you may want to consider including both income and growth assets in your investments.

How do I pick the best asset class to invest in each year?

Each asset class performs well at different times. In a perfect world, people would be able to predict which asset class would provide the best returns over the year and invest accordingly. In reality, you can take a big step towards being in the best performing asset class every year by diversifying your investments across all four asset classes.

Another advantage of diversifying across asset classes is that it smooths your returns, offsetting any fluctuations in one asset class against the performance of the others.

How can I achieve diversification?

While the rigorous research and analysis needed to successfully diversify investments within and across the full range of asset classes can be unfeasible for most people, there are fortunately more effective ways to achieve a diversified portfolio. By investing in a managed fund, your money is pooled with other investors and managed by a team of dedicated professionals. You stand to benefit from their skills and resources as well as the advantages of scale.

Diversified managed funds invest in the full range of asset classes, combining the advantages of professional management within the share, property, bond and currency portions of the portfolio with active asset allocation across the asset classes to manage the mix according to the prevailing market conditions.

Moreover, managed funds come in a variety of types for different investor needs. For example, some have higher weighting to growth assets and so have benefited from their historically higher returns in the longer term. Others have higher weighting to income producing assets and provide investors with a lower-risk investment with some exposure to growth. Balanced funds aim for a balance between growth and income producing assets.

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