TOWN CLOSE
Financial Planning

Investment expectations

future proofing your finances

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WHAT TO EXPECT WHEN IT COMES TO INVESTMENTS

This is one of a series of short papers covering various aspects of investing. The others are "Diversification, "Risk" and "Strategy".

Everything you don't need in the next three years or as an emergency fund should be invested to beat inflation. Inflation at 3% pa means the value of your money halves every 20 years.

We must beat inflation if we are to provide you with the money you need to do the things you want. If we don't, you will be poorer tomorrow than you are today. That's a terrible result.

Therefore we arrive at a portfolio investment, typically, 20% in bonds and 80% in equities (please see "Investment Strategy" for more detail).

However, your investments will suffer temporary setbacks!

Over some periods of time, you could be worth less than you were previously and this may persist for quite a few months. In our view, these temporary declines are much more acceptable compared to the permanent loss that inflation will inflict.

We will never know when a correction will begin. We won't know when it will end. But we do know that, however deep or shallow the correction is, it will be temporary.

This level of uncertainty is not a risk (if you stick to your plan) when you have a 30+ year investment horizon. And, when it is over, the permanent uptrend will reassert itself.

Here's a rough idea of what you should expect to happen:

- An average annual drop of around 10-15%, ie., values will drop by 10-15%, then recover.
- We will not flinch; to profit from this perfectly normal occurrence we would have to pick both the top and bottom of the market.
- That means we would have to be right twice. We won't be.
- Nobody will be, not consistently. So, by far the best thing to do is sit on your hands.
- Furthermore, the chance of any decline over the next 12 months is about 25%.

- There's about a 13% chance it'll be 10% - and a 6% chance it's 20%.
- All of which means that, 75% of the time, values fall and then recover in full during the same 12-month period.
- The other 25% of the time, they recover not long after.
- All declines to date have proven to be temporary.
- In return for this, you can expect inflation-beating returns over the years.