

Current Financial Turmoil

The current turmoil in financial markets is unprecedented in modern economic history and is clearly unsettling for all investors. However, for longer term investors the crisis has seen the prices of a great many assets, particularly in the share market, knocked down to levels that appear to us to represent outstanding value.

We do not know where prices may go in the short-term; they certainly could fall further. But, in our view, this is a once in a decade opportunity to buy good quality assets at very low prices. Accordingly, while we were selling down some of the Fund's share investments one and two years ago, we are not doing any selling now; rather we are seeking to selectively add to our investments.

We certainly appreciate that these circumstances are unsettling for members and that many of us wish that we had switched into cash a year ago. Our experience is that it is extraordinarily difficult to time markets and all too easy to miss out when markets recover. In this regard it is worth noting that market prices are subject to two major factors: sentiment and expectations of the future. Sentiment can range from outrageously optimistic, as was the case before the 1987 share market crash, to absolutely pessimistic, which is where we are now. One very successful long-term investment strategy has been to sell at high prices to the excessively optimistic and to buy at low prices from the grossly pessimistic.

While it is understandable that short-term risk may encourage some members to consider selling growth oriented investments now at very low prices, in a long-term sense all this does is lock in losses and expose the investor to a very large risk of missing out when prices rise.

This is where the expectations factor comes in – today's financial markets are pricing in nothing less than a major depression but while we believe that a number of major economies will experience mild recessions, the worse has already been priced into the market. More importantly, as is nearly always the case, the financial markets will start to price in economic recovery well in

advance of it actually happening. That is, by the time that we know that the time of maximum economic danger has passed, markets will almost certainly have recovered strongly and it will be too late to buy back in.

So, to sell now is to lock in past losses and to substantially reduce the probability of enjoying compensating gains when markets do start to recover.

Tim Hughes
Chief Investment Officer

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