Why diversity is king

Past performance of any one asset class is no guarantee of future success, writes ***Anthony Keane***

TRYING to pick the next big investment winner can feel like having a go at lucky dip – with good reason.

A new analysis of nine major asset classes over the past 10 years shows that all but one – cash – has claimed the title of the year's best investment at least once.

Vanguard Australia's 2016 Index Chart shows that since 2007 Aussie shares have topped the table only once, a 30 per cent jump in 2007 just before the global financial crisis, while US shares and international bonds have been winners twice. Last financial year, Australian property trusts did the best with a 24.6 per cent gain.

Vanguard Australia head of market strategy Robin Bowerman says the numbers highlight the value of diversification.

"It shows how hard it is to time markets to pick next year's winning asset class," he says.

"It's difficult for people to accept that there isn't some secret formula that lets you invest in things before they go up.

"If you accept the fact that you can't predict markets, that's why you diversify, placing a lot of bets across the whole market."

FINANCIAL YEAR TOTAL RETURNS each year's best performers green and the worst red

YEAR	Aussie shares	International Shares	International Shares (hedged)	US Shares	Aussie bonds	International Bonds (hedged)	Cash	Aussie listed property	International listed property
2007	30.3%	7.8%	21.4%	5.6%	4.0%	5.2%	6.4%	25.9%	3.0%
2008	-12.1%	-21.3%	-15.7%	-23.4%	4.4%	8.6%	7.4%	-36.3%	-28.6%
2009	-22.1%	-16.3%	-26.6%	-12.5%	10.8%	11.5%	5.5%	-42.3%	-31.2%
2010	13.8%	5.2%	11.5%	8.9%	7.9%	9.3%	3.9%	20.4%	31.3%
2011	12.2%	2.7%	22.3%	3.7%	5.5%	5.7%	5.0%	5.8%	9.2%
2012	-7.0%	-0.5%	-2.1%	11.1%	12.4%	11.9%	4.7%	11.0%	7.5%
2013	20.7%	33.1%	21.3%	32.5%	2.8%	4.4%	3.3%	24.2%	24.3%
2014	17.6%	20.4%	21.9%	22.7%	6.1%	7.20%	2.7%	11.1%	11.8%
2015	5.7%	25.2%	8.5%	31.8%	5.6%	6.3%	2.6%	20.3%	23.1%
2016	2.0%	0.4%	-2.7%	7.5%	7.0%	10.8%	2.2%	24.6%	20.4%

Source: Vanguard

The Vanguard data shows that cash has been the worst investment class for three of the past 10 years, and in the past three years its annual investment returns have failed to rise above 2.8 per cent.

However, cash remains popular among Aussie investors because it's the only asset that comes with the safety of a Federal Government guarantee on bank deposits.

"We also have had pretty volatile markets, which feeds into people saying 'I'm not sure, so I will keep my money parked in cash'," Bowerman says.

Despite low official interest rates in Australia and overseas over the past decade, buying bonds has been the best move for three of 10 years. In 2008 and 2009 it was international bonds and in 2012 Australian bonds chimed in with a 12.4 per cent gain.

"In Australia we don't appreciate the value of fixed income," Bowerman says.

He says the rise of exchange traded funds in recent years gives investors better access to bonds – both government and higher-yielding corporate bonds.

Financial strategist Theo Marinis says the key message for any investor is "Diversify, diversify, diversify".

"Nobody's got a crystal ball and you can't predict what asset class is going to perform best next," he says.

Marinis says quite often, one year's best investment performer drops off the next year "to rebalance the scales", highlighting the benefit of diversification.

"You won't shoot the lights out but you won't blow up your portfolio either," he says.

Vanguard's analysis tracks asset class performance over 30 years. It found that a $10,000 investment in 1986 in Australian shares has grown to $154,405, while the same amount in cash would be worth $75,023 — inflated by 15 per cent-plus interest rates paid on deposits in the late 1980s.

"Diversifying across multiple asset classes allows investors to take advantage of growth on several fronts, while providing some safe harbours against unexpected risks and market corrections," Bowerman says.