

UNDERSTANDING PERFORMANCE

Performance affected by credit crisis – in ways you may not expect

Global financial markets have been volatile since July 2007 when the subprime crisis emerged in the US. The ensuing global credit crisis has caused great financial stress and uncertainty for borrowers – corporations and homeowners with mortgages alike.

In September 2008, the sense of panic deepened with the collapse of Lehman Brothers, a large US investment banking firm. We are now facing a crisis of confidence that has resulted in redemptions from funds, forced selling of quality investments to meet redemptions, and the fear of investing even though attractive opportunities have emerged.

With all of this turmoil, the ongoing declines in superannuation performance in recent months may be disappointing, but perhaps not surprising for those following the news.

However, it may be surprising to learn of the issues faced by index managers and that they have sometimes struggled in the face of extreme chaos to remain close to the index. Index managers also have to cope with technical changes in the indices they track.

On top of this, extreme intra-day volatility coupled with large cashflows can distort daily unit prices at the investment option level. Also, short-term comparisons with index performance may be misleading if the comparison dates vary by only one day in a volatile market environment. In October 2008, these distortions resulted in a few of the Aon Master Trust's sector index options showing performance better than the index and the underlying manager (State Street Global Advisors) and this is visible in the three-month returns.

Our performance figures based on the unit prices are correct; the apparent strength of our index options relative to the index is a technical outcome of the unit pricing calculations. Please note that our unit prices are calculated by BNP Paribas, a third-party leader in the field. BNP follows the trustee's unit pricing policy and is subject to comprehensive governance of their procedures.

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