



Market update May 2008

(Prepared by Mark Sainsbury, Chief Investment Officer, FSS Trustee Corporation)

Since mid-March or thereabouts, investment markets have shown more settled behaviour and this has allowed both share markets and fixed income markets to recover some lost ground.

Despite the more stable conditions, we cannot allow ourselves to relax just yet. There is still a reasonable level of volatility in markets caused by a combination of:

- the release of good or bad news
- the actions of central banks in raising or lowering interest rates
- fluctuations in commodity prices such as oil and gold.

Investment markets generally are struggling to find any real direction and this, in turn, is making it very difficult for investors to have confidence in their decision-making.

In our last update, we noted that the main challenge for investment managers in this sort of environment is to predict when market uncertainty will give way to asset values that reflect the true level of activity in the real economy. This statement is still very relevant. While most commentators agree that the US is in or near recession, it is still not clear what effect this will have on other economies, and whether the recent fall in financial markets has fully captured these conditions.

First State Super's asset allocation has been reasonably defensive for some time, which has protected our members from some of the impact of the recent share market decline. Although investment portfolios will never be totally immune from market falls, the Trustee has responded to the current market conditions in a timely manner, which has allowed the Fund's portfolios to perform reasonably well compared to other schemes' average returns. We anticipate this will continue during any extended period of market turbulence.

First State Super invests in a range of investments managed by selection of investment managers. Our investment portfolios are diversified across different managers and different asset classes, which reduces the impact of any individual security or market which might be experiencing difficulty.

Market confidence is still at a very low level, and this underpins the cautious approach that we are currently taking. Even allowing for the recent rebound in markets, it is still very difficult to generate positive performance numbers in this environment. However, it is possible that the worst of the response to the economic downturn has already been reflected in markets, particularly share markets.

The Trustee continues to watch market developments very carefully in an effort to lessen, as much as possible, the impact of any market weakness, while still being positioned to benefit from any market rallies that may occur when confidence returns.

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