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A QUICK LOOK AT INDEX VERSUS ACTIVE FUNDS

This Practice Essentials provides a brief overview of the S&P Indices Versus Active (SPIVA[®]) Australia Scorecard, our semi-annual report on the relative performance of indices and actively managed funds. This unbiased comparison of index versus active funds may provide financial advisors with the information they can leverage when considering the investment goals for their clients' portfolios.

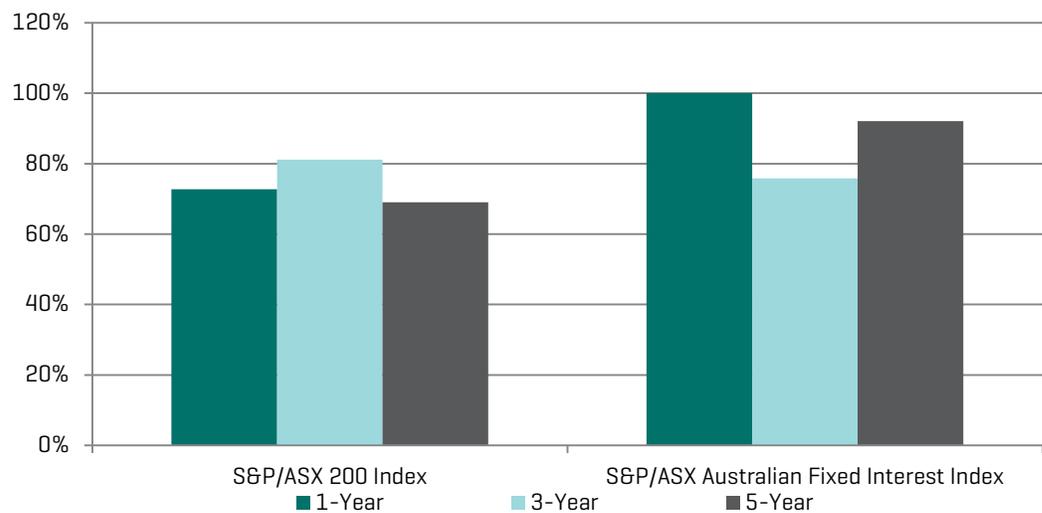
The SPIVA Australia Scorecard tracks the number of actively managed funds that beat their comparable benchmarks over one-, three- and five-year timeframes. The scorecard corrects for a survivorship bias in order to conduct a meaningful study of active retail fund performance relative to the appropriate benchmark for each peer group.

At least 70% of active retail funds underperformed the benchmark over the past year.

Most Active Funds Underperformed their Benchmarks

A majority of active funds underperformed their respective benchmarks across all asset classes studied in the Mid-Year 2012 SPIVA Australia Scorecard (see Exhibit 1). With the exception of the Australian equity small-cap category, at least 70% of active retail funds underperformed the benchmark over the past year. The same is true for the three-year period.

Exhibit 1: Percentage of Active Funds that Underperformed the Comparable Index



Source: S&P Dow Jones Indices, SPIVA Australia Scorecard Mid-Year 2012. Data as of June 30, 2012. Charts and tables are provided for illustrative purposes. Past performance is not a guarantee of future results.

Australian Equities: S&P/ASX 200 Outperforms

Over the past five years, approximately 69% of active retail Australian equity general funds underperformed the S&P/ASX 200 Accumulation index. The portion of underperforming funds increased to an even larger majority across the one- and three-year time periods, with at least 72% of active Australian equity funds failing to beat the index.

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Australian Equities Small Cap: Superior Active Performance

Active Australian equity small-cap funds significantly outperformed the benchmark across all periods studied in the SPIVA Australia Scorecard. Both the equal-and asset-weighted average returns of the active fund category far outperformed the S&P/ASX Small Ordinaries index across all periods studied. Over the past five years, almost 80% of active Australian equity small-cap funds outperformed the index.

International Equities: Active Underperformance, Large Funds Languish

Almost 90% of active international equity general funds underperformed relative to the benchmark over the past year. Over both three- and five-year periods, at least 72% of international equities general funds did not beat the index. The asset-weighted returns of this category are also converging closer to equal-weight returns for the first time since the SPIVA Australia Scorecard was introduced in August 2009, suggesting that larger funds are not performing as well as they did in previous periods.

Australian Bond Funds: Low Survivorship Rates

The S&P/ASX Australian Fixed Interest Index outperformed all retail Australian bond funds over the past year. Similarly, 92% of funds in this category underperformed the index over a five-year period, which is also consistent with the poor survivorship rates for the category. Over the past five years, active Australian bond funds suffered the lowest survivorship rate across the universe of funds studied in this report, as approximately 30% of active bond funds failed to survive.

A-REIT Funds: Strong Survivorship Rates

The S&P/ASX 200 A-REIT Index outperformed approximately 86% of active Australian A-REIT funds over the past year. However, the portion of active funds that underperformed falls to approximately 65% over a five-year period. Active Australian equity A-REIT funds had among the highest survivorship rates when compared with the other active categories covered in the SPIVA Australia Scorecard.

All active retail Australian bond funds studied in this report failed to beat the S&P/ASX Australian Fixed Interest Index over the last year

Understanding before Investing

The results of the SPIVA Australia Scorecard show that indices have generally tended to perform better than retail active funds. However, it also illustrates that there are active funds that do outperform. Certainly, investors need to take special consideration in determining which investments are most appropriate for their personal needs and requirements.

The Nobel Prize-winning professor William F. Sharpe sums it up:

Should everyone index everything? The answer is resoundingly “no”. In fact, if everyone indexed, capital markets would cease to provide the relatively efficient security prices that make indexing an attractive strategy for some investors. All the research undertaken by active managers keeps prices closer to values, enabling indexed investors to catch a free ride without paying the costs.

Thus there is a fragile equilibrium in which some investors choose to index some or all of their money, while the rest continue to search for mispriced securities.

Should you index at least some of your portfolio? This is up to you. I only suggest that you consider the option. In the long run, this boring approach can give you more time for more interesting activities such as music, art, literature, sports, and so on. And it very well may leave you with more money as well.¹

¹ Sharpe, William F. “Indexed Investing: A Prosaic Way to Beat the Average Investor” www.stanford.edu/~wfsarpe/art/talks/indexed_investing.htm

Exhibit 2: Percentage of Funds Outperformed by the Index

Fund Category	Comparison Index	QTR (%)	One-Year (%)	Three-Year (%)	Five-Year (%)
Australian Equity General	S&P/ASX 200 Accumulation Index	72.59	72.73	81.12	69.01
Australian Equity Small-Cap	S&P/ASX Small Ordinaries Index	16.00	15.79	20.73	20.78
International Equity General	MSCI World Ex Australia Index	84.25	88.37	80.99	72.92
Australian Bonds	S&P/ASX Australian Fixed Interest Index	90.32	100.00	75.76	92.11
Australian Equity A-REIT	S&P/ASX 200 A-REIT Index	93.59	86.42	88.37	65.12

Source: S&P Dow Jones Indices, Morningstar. Data as of June 30, 2012. Charts are provided for illustrative purposes. Past performance is not a guarantee of future results.

Exhibit 3: Survivorship

Fund Category	No. of Funds at Start	Survivorship (%)
QTR		
Australian Equity General	262	93.51
Australian Equity Small-Cap	75	94.67
International Equity General	127	95.28
Australian Bonds	31	100.00
Australian Equity A-REIT	78	93.59
One-Year		
Australian Equity General	265	92.45
Australian Equity Small-Cap	76	93.42
International Equity General	129	93.02
Australian Bonds	31	100.00
Australian Equity A-REIT	80	91.25
Three-Year		
Australian Equity General	286	84.27
Australian Equity Small-Cap	81	83.95
International Equity General	141	83.69
Australian Bonds	33	84.85
Australian Equity A-REIT	85	85.88
Five-Year		
Australian Equity General	282	81.56
Australian Equity Small-Cap	76	82.89
International Equity General	143	76.92
Australian Bonds	38	73.68
Australian Equity A-REIT	85	82.35

Source: S&P Dow Jones Indices, Morningstar. Data as of June 30, 2012. Charts and graphs are provided for illustrative purposes.

Exhibit 4: Equal-Weighted Fund Returns

Index/Peer Group	QTR (%)	One-Year (%)	Three-Year Annualized (%)	Five-Year Annualized (%)
S&P/ASX 200 Accumulation Index	-4.68	-6.71	5.65	-4.00
Australian Equity General	-5.62	-7.58	4.29	-4.27
S&P/ASX Small Ordinaries Index	-15.30	-14.61	3.39	-8.89
Australian Equity Small-Cap	-10.54	-7.15	11.22	-3.47
MSCI World Ex Australia Index	-3.83	0.10	3.01	-6.10
International Equity General	-5.38	-3.63	1.22	-7.22
S&P/ASX Australian Fixed Interest Index	4.78	13.09	8.91	8.51
Australian Bonds	3.86	10.35	8.28	7.20
S&P/ASX 200 A-REIT Index	8.76	11.04	12.27	-12.26
Australian Equity A-REIT	7.96	9.83	11.02	-12.85

Source: S&P Dow Jones Indices, Morningstar. Data as of June 30, 2012. Charts are provided for illustrative purposes. Past performance is not a guarantee of future results

Exhibit 5: Asset-Weighted Fund Returns

Index/Peer Group	QTR (%)	One-Year (%)	Three-Year Annualized (%)	Five-Year Annualized (%)
S&P/ASX 200 Accumulation Index	-4.68	-6.71	5.65	-4.00
Australian Equity General	-5.28	-7.09	4.45	-3.80
S&P/ASX Small Ordinaries Index	-15.30	-14.61	3.39	-8.89
Australian Equity Small Cap	-10.00	-6.02	11.62	-3.03
MSCI World Ex Australia Index	-3.83	0.10	3.01	-6.10
International Equity General	-5.21	-2.97	1.05	-5.02
S&P/ASX Australian Fixed Interest Index	4.78	13.09	8.91	8.51
Australian Bonds	3.94	10.94	8.77	7.63
S&P/ASX 200 A-REIT Index	8.76	11.04	12.27	-12.26
Australian Equity A-REIT	7.60	9.76	11.06	-12.22

Source: S&P Dow Jones Indices, Morningstar. Data as of June 30, 2012. Charts are provided for illustrative purposes. Past performance is not a guarantee of future results

For more information on the SPIVA Scorecard, please visit:

www.spindices.com/resource-center/thought-leadership/spiva

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