galileocapital
Challenging Conventional Wisdom

NEWSLETTER

Monthly Newsletter – December 2013

Festive greetings!

As 2013 draws to an end, we at Galileo Capital are filled with a sense of gratitude and appreciation for the contribution that our clients and associates have made to our business over the past 12 months. Thank you very much for choosing us to be your financial planning partner!

May the closeness of friends, the comfort of home, and the knowledge that your best interests are always at the core of our business renew your spirits over this holiday season.

All the very best for the festive season and we trust that 2014 will exceed your expectations.

-- The directors and staff of Galileo Capital

Sleep therapy may help with depression

A series of closely watched studies of the relationship between sleep and depression, which will be released next year, seem to be showing that curing insomnia in people with depression could double their chance of a full recovery

If the figures hold up to scrutiny, this may be the most significant advance in the treatment of depression since the introduction of Prozac in 1987. Depression is a more common mental disorder than most people realise and more than half of sufferers also have insomnia.

Doctors have known for years that sleep problems are intertwined with mood disorders. But only recently have they begun to investigate the effects of treating both at the same time. Antidepressant drugs like Prozac help many people, as does talk therapy, but in rigorous studies the treatments administered individually, only slightly outperform placebo pills. Used together the treatments produce a cure rate – full recovery – for about 40% of patients.

Adding insomnia therapy to an antidepressant would sharply lift the cure rate, according to two very small studies. If successful, the principles learned there may be applied to much larger studies to find out whether the results stand up to more rigorous testing.

Doctors have long considered poor sleep to be a symptom of depression that would clear up with treatments, said Rachel Manber, a professor in the psychiatry and behavioural sciences department at Stanford, whose 2008 pilot trial of insomnia therapy provided the rationale for larger studies. “But we now know that’s not the case,” she said. “The relationship is bidirectional – that insomnia can precede the depression.”

Musical training is brain training

Early musical training seems to have a lasting, positive effect on how the brain processes sound. That’s the finding of a study that appeared in the Journal of Neuroscience in November.

As people grow older, they often experience changes in the brain that compromise hearing. For instance, the brains of older adults show a slower response to fast-changing sounds, which is important for interpreting speech. However, previous studies show that these age-related declines are not inevitable – recent studies of musicians suggest that lifelong musical training may offset these and other cognitive declines.

In the current study, out of Northwestern University in the US, researchers found that the more years study participants spent playing instruments in their youth, the faster their brains responded to a speech sound. And that was significant because neural timing is the first thing to go in the ageing adult.

The finding confirmed that – like sound financial planning – the investments that we make in our brains early in life continue to pay dividends years later.

Index investing in volatile markets

As the stock market maintains the excellent rate of growth that started in 2009, some investors are starting to question whether there are inherent dangers in their indexed investments.

Many critics of index investing claim that it's worth paying a fund manager when the stock market is expensive, as the fund manager should select assets that will not fall as much as the index in the event of a market crash. This is a topic that is very relevant to us, as many of our clients have a significant exposure to indexed investments.

As always, when we attempt to understand issues like this, we rely on objective information rather than emotive arguments. We have reviewed the market crash in 2008 as a good example of how indexed investments perform in rising and falling markets. The table below shows what happened in the two years preceding the crash, the year of the crash and the following two years of recovery.

This is a five-year period, which is the minimum period for any investment in shares, indexed or not. We compared the index performance vs. the average performance of unit trusts that invest in shares.

	Rising Market	Rising Market	Market Crash	Market Recovery	Market Recovery	Average Annual Growth
	2006	2007	2008	2009	2010	Return
All share index	41.2	19.2	-23.2	32.1	19.0	17.666
Ave equity unit trust	36.7	17.6	-22.9	27.2	18.5	15.428

It is clear that the indexed investment will fall by the same amount as the average unit trust but the index recovers more quickly. This puts paid to any arguments by fund managers that index investing is somehow more "dangerous" than managed investments. It also reinforces our view that an indexed investment will beat the average over any period longer than five years. For longer periods of time, we believe that an indexed investment will actually be in the top 25% of all funds.

Some fund managers have added value to their investors over the long term. Over the last 10 years, the best unit trust in SA has grown by 25% per year while the index has grown by 20% per year. This means there is scope for investors to search for fund managers that have the ability to beat the market, because a handful of them have done so in the past.

However one cannot simply rely on this, because very often, fund managers are unable to replicate their performance, and nor can their replacements when they retire and change industry.

The large majority of our clients have a significant allocation to indexed investments and some clients are 100% invested in indexed funds. We are comfortable that they will achieve good growth over the long-term and have a high probability of being in the top 25% of all funds.

When it comes to long-term investment decisions, we constantly deal with probabilities. For investors who want as much certainty as possible, we recommend indexed investments. Investors who are willing to take more risk with less certainty, potential outperformance generated by fund managers might be attractive.

In summary, there is no single strategy that is sure to succeed in all conditions, we have to tailor your investment strategy to your requirements, personality and circumstances.