

# A long-term approach to equity investing

JANUARY 2009

**BLACKROCK**

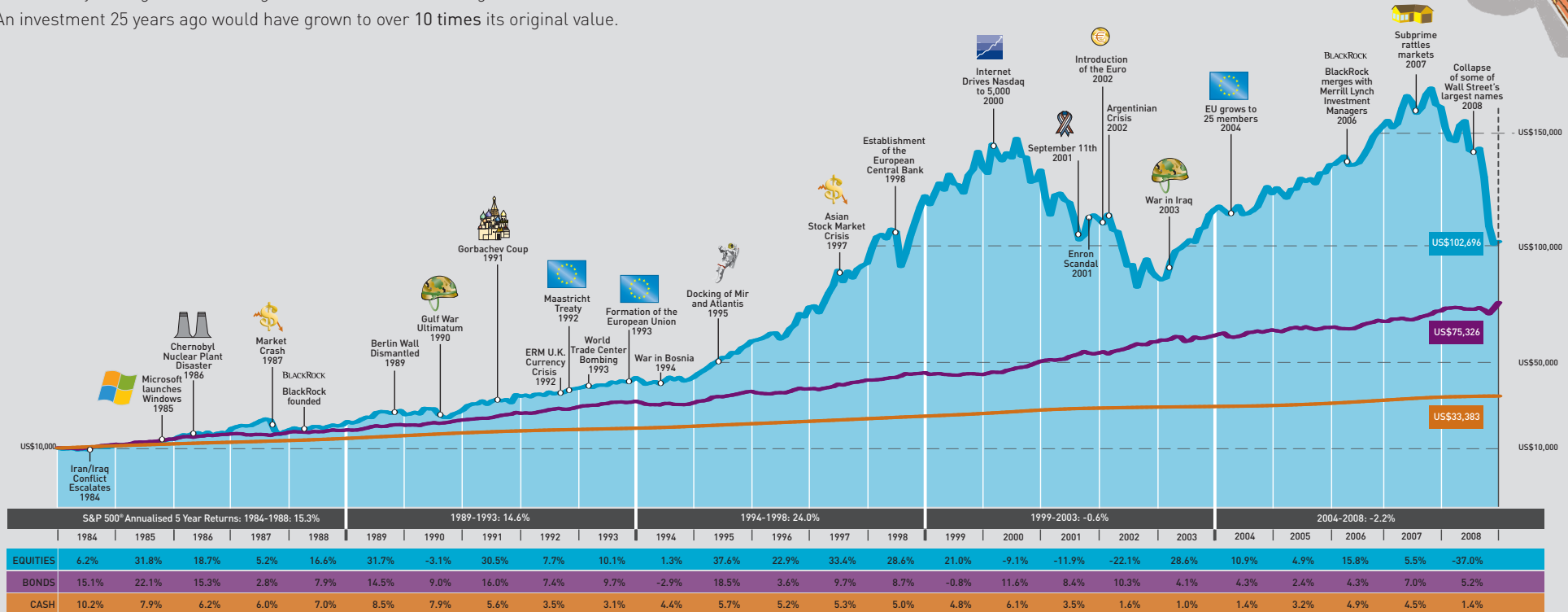
The financial markets have recently experienced significant volatility, which underlines the case for a long-term approach to investing in the stock markets.

Down periods, such as those recently seen, are an inherent aspect of equity investing. Unpredictable events and changes in investor sentiment can have a negative impact on markets. However, short-term declines should not detract from the long-term potential of stock market investing.

The chart shows that, even with the recent market volatility, an investment in the S&P 500 when BlackRock was founded 20 years ago, would have grown to over 5 times its original value.

An investment 25 years ago would have grown to over 10 times its original value.

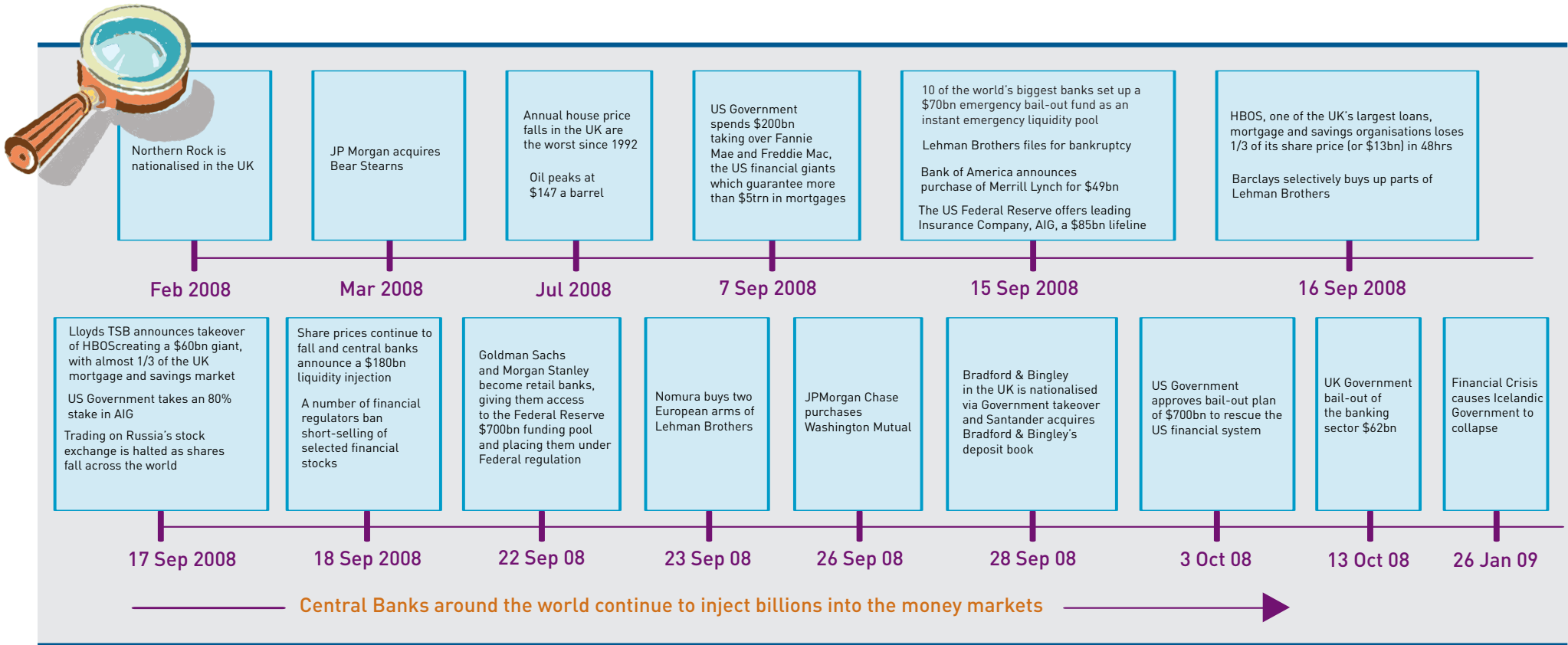
We take a look on page 2 at some of the events that have rocked the marketplace in 2008 and early 2009



Source: Ibbotson/Datastream. All data to 31.12.2008. The information provided is for illustrative purposes only and is not meant to represent the past or future performance of any particular investment or the indices. It is not possible to invest directly in an index. Stocks are represented by the S&P 500® Index, an unmanaged index that consists of the common stocks of 500 large capitalization companies, within various industrial sectors, most of which are listed on the New York Stock Exchange. Stock prices fluctuate with market condition and may result in loss of principal. Bonds are represented by the Lehman Brothers Aggregate Bond Index, an unmanaged market-weighted index that consists of U.S. government and agency securities, mortgage-backed securities issued by the Government National Mortgage Association, the Federal Home Loan Mortgage Corporation or the Federal National Mortgage Association and investment-grade (rated BBB or better) corporate bonds, all of which will mature within 30 years. Bonds held to maturity offer a fixed rate of return. Cash is represented by the annualized monthly yield on all actively traded Treasury bills maturing in 90 days quoted on a discounted basis in the secondary market. T-bills are guaranteed by the U.S. government as to payment of principal and interest and offer a fixed return if held to maturity. All returns assume reinvestment of dividends.

# Key turning points in 2008/2009

A more detailed look at the turn of events which have changed the face of the financial industry in 2008 and early 2009



## In Summary – The big names lost or under new ownership

### Lost

Bought out – **Bear Stearns, HBOS, Merrill Lynch Wachovia**  
Bankrupt – **Lehman Brothers**

### Rescued

**AIG, Fannie Mae, Freddie Mac, Northern Rock, Bradford & Bingley, Fortis**

### Acquisitions

**Lloyds TSB (+ HBOS)**  
**Bank of America (+Merrill Lynch)**  
**JP Morgan (+ Bear Stearns + Washington Mutual)**  
**Barclays (+ parts of Lehman)**  
**Nomura (+ parts of Lehman)**  
**Santander (+ parts of Bradford & Bingley)**

## A Glossary

### Subprime mortgages

A 'subprime' borrower typically has a poor credit rating and/or very low income, which means that they represent a higher risk to the mortgage lender. To compensate for the higher risk, the lender typically charges the subprime borrower a higher rate of interest. In the five-year period after 11 September 2001, a combination of very low interest rates and strong house prices led to a sharp increase in the number of subprime borrowers in the US.

**The recent issues:** As the US Federal Reserve steadily increased interest rates and the US housing bubble burst towards the end of 2006, many subprime homeowners began to default on their mortgages and some faced repossessions.

### Mortgage-backed securities

US mortgage lenders repackage their mortgage debt in investment vehicles called mortgage backed securities (MBS) which are then sold on to banks and other institutions that receive a kind of interest payment for investing in them. These MBS might bundle some subprime mortgages together with less risky mortgages.

**The recent issues:** Some of these securities contained a diversified mixture of high- and low-quality debt, but were given high credit ratings by the ratings agencies, in the belief that the risk of failure was low. When the cash flow into such vehicles stopped due to some borrowers defaulting, the securities dropped in value, resulting in substantial losses for those who had invested in them. Since loans tended to be bundled together, it was not clear to investors how much 'toxic' debt each MBS held, resulting in widespread lack of confidence in the instruments. This came to a head in Q3 2007 and has culminated in billions of dollars in write-downs from financial institutions around the world. The crisis has had a knock-on effect on credit markets and the wider global economy.

### Credit crunch

A term used to describe a sudden reduction in the general availability of loans (or 'credit') to both companies and consumers, or a sudden increase in the cost of obtaining loans from banks.

**The recent issues:** Until the scale of the bad debt in the global financial system becomes known, banks have reduced the availability of credit to each other and have made credit more expensive by raising interest rates. Accordingly, the London inter-bank offered rate (LIBOR) – the rate at which banks lend to each other – has increased dramatically at various periods since August 2007. The collapse of world-famous banks such as Bear Stearns and Lehman Brothers has only increased the lack of confidence among banks.

### Short selling

A practice whereby an investor takes a 'negative position' in a company, believing the share price will fall in value. The investor can sell stock that he/she does not own, with the aim of buying the shares back at a later date at a lower price. The investor later returns the stock to the original owner – pocketing the difference as profit.

**The recent issues:** Many investors, notably hedge funds, use shorting techniques with the objective of achieving returns from falling share prices. In September 2008, regulators in several countries temporarily banned the practice of shorting from a list of financial stocks. The regulators made this move as they believed it would guard against further instability in the financial sector.

### Toxic debt

Bankers call the bonds that are most vulnerable to losses 'toxic debt', or 'toxic waste'. Since subprime mortgages were packaged together with other quality debt in opaque vehicles such as Mortgage Backed Securities (MBS's), it has become difficult to price the true value of each MBS. Indeed, these loan packages may not be able to be repaid, because the value of the assets against which they are secured (e.g. US houses) has fallen dramatically.

**The recent issues:** Because banks are not entirely sure how much toxic debt is on their own and others' balance sheets, they remain unwilling to lend to each other. Instead, they are preferring to rebuild their balance sheets by storing cash to buttress themselves against any future shocks.

### Deleveraging

Many companies use borrowed money (leverage) to fund their operations. Deleveraging refers to a company's attempt to decrease its borrowing levels by settling portions of debt.

**The recent issues:** Companies that are highly leveraged may be at risk of bankruptcy if they are unable to make payments on their debt. Given the recent high-profile bankruptcies such as Lehman Brothers, numerous financial institutions are currently trying to bolster their balance sheets by deleveraging. The effect of this is to reduce the amount of credit in the financial system. Since both companies and consumers now find it harder to obtain loans, the ultimate result is a slowing down of the economy.

# Keeping a long-term outlook during turbulent markets is important

## Here's why:

### You can take advantage of the downturns ...

By viewing market declines as good buying opportunities, it is possible to enhance your portfolio's long-term returns when the market rebounds. While nobody can predict exactly when markets will decline or rebound, a strategy of adding to holdings when they are "on sale" may provide significant advantages over a strategy of pulling out of the market when prices are at their lowest.

### You don't want to miss the market's best performing days ...

Over every market cycle, there will be up days and down days. Missing even a few of the stock market's best-performing days can result in significantly lower returns than the market index. Often, a few very good days account for a large part of the market's total return. By trying to time the market and potentially getting this wrong by even a small margin, you may potentially miss out on market rallies that can substantially improve your overall return and long-term wealth.

## Here's how to do it wisely:

### Be diversified

Rather than trying to pick a single investment type, diversifying across asset classes may decrease your investment risk and enhance the long-term return potential. Not all investment types perform in exactly the same way during similar time periods. Investing across multiple investment strategies, styles, sectors and regions reduces risk and enhances the potential for investing in the best-performing asset class while reducing the impact of investing in the worst-performing products. See below for a ten-year snapshot of S&P 500 Sector and Asset Class Returns, demonstrating how this strategy can be especially important in a difficult market environment, when sector rotations and market fluctuation happen continuously.

### Let professional investors do the hard work

History has shown that markets can be volatile, but you do not have to navigate these challenging times alone. BlackRock has the experience, investment insight, global resources and breadth of investment products to help you stay the course and meet your financial goals. With an unwavering focus on risk management across all our portfolios, you can feel reassured that your assets are being managed by some of the most experienced and best prepared investment professionals in the industry.

% Ten-year Snapshot of S&P 500 Sector Returns<sup>1</sup>

Sector	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Composite	78.74	57.18	3.48	-4.26	47.23	31.54	31.37	36.80	34.40	-15.43
Consumer Discretionary	25.25	37.05	2.78	-5.45	38.19	24.28	16.84	24.21	22.53	-22.81
Consumer Staples	25.17	25.70	-5.74	-11.13	37.41	19.86	6.47	20.99	19.38	-28.98
Energy	21.50	16.78	-6.40	-14.64	32.19	18.03	6.46	19.19	16.31	-30.49
Financials	21.04	15.68	-8.95	-18.82	31.03	13.24	4.91	18.64	14.18	-33.49
Health Care	19.14	5.88	-10.39	-22.10	28.68	13.20	4.42	18.63	12.03	-34.87
Industrials	18.72	-9.10	-11.89	-23.82	26.26	10.89	3.58	15.80	11.95	-37.00
Information Technology	4.11	-15.72	-11.95	-26.34	25.63	10.88	2.32	14.36	7.15	-39.92
Materials	-9.18	-20.00	-12.25	-29.99	15.06	8.16	0.99	13.29	5.49	-43.14
Telecommunication Services	-10.66	-38.81	-25.87	-34.11	11.57	2.56	-5.63	8.42	-13.21	-45.66
Utilities	-15.09	-40.90	-30.44	-37.41	7.08	1.68	-6.36	7.53	-18.63	-55.32

% Ten-year Snapshot of Asset Class Returns<sup>2</sup>

Asset Class	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Fixed Income	51.29	22.83	14.02	10.25	48.54	23.71	14.02	26.86	11.63	5.24
International	43.09	19.18	8.44	-9.64	47.25	22.25	12.65	23.48	11.43	-28.92
Large Cap Core	28.25	11.63	2.49	-11.43	46.03	20.70	12.65	20.80	9.13	-33.79
Large Cap Growth	27.30	8.25	2.33	-15.66	42.71	20.22	12.10	20.22	7.05	-34.92
Large Cap Value	21.26	6.08	-5.62	-16.19	40.06	18.33	5.82	18.37	6.97	-37.00
Mid Cap Core	21.04	-3.02	-9.23	-20.48	39.17	15.71	4.91	15.80	5.60	-38.44
Mid Cap Growth	18.23	-9.10	-11.71	-20.85	38.07	15.48	4.71	15.26	5.49	-38.54
Mid Cap Value	12.72	-11.75	-11.89	-22.10	31.79	14.31	4.55	13.35	1.99	-39.22
Small Cap Core	-0.11	-13.96	-12.73	-23.59	28.68	10.88	4.15	11.01	-1.42	-41.46
Small Cap Growth	-0.82	-22.08	-20.15	-27.41	25.66	6.13	4.00	10.66	-1.57	-43.06
Small Cap Value	-1.49	-22.43	-21.21	-30.26	4.10	4.34	2.43	4.33	-9.78	-44.32

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Data as at 31.12.2008. Source: Datastream.

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