Building Wealth in Any Environment

With all the uncertainty surrounding investment at the moment, it was interesting that we had so much material for our recent seminar with Noel Whittaker, on the tried and true methods of building wealth no matter what the politicians get up to. Don't use the current uncertainty as an excuse not to save. If you need help with that please contact us at www.bantacsfinancialsolutions.com.au

Paying Off Loans

First up I am going to dazzle you with numbers that will show how you can get the bank to pay off $400,000 of your $500,000!

Back in the days when interest rates were double digits a 1% variation in the interest rate didn't make that much difference. But now you can expect 1% to reduce your annual interest bill by 20%. Reducing your interest rate from 5% to 4% can reduce the annual interest charge on a $500,000 loan from $25,000 a year to $20,000. That is an extra $100 a week in your pocket!

How much are you paying in interest at the moment? A simple phone call to the bank may get you that extra 1%. 3.9 percent is ball park these days.

Another way to reduce your interest rate by 1% is to switch your loan from interest only to principal and interest. I know it goes against conventional wisdom to pay off tax deductible debt, especially when you have debt that is not tax deductible. And some of you may think you can't afford principal and interest repayments. They aren't that bad; on a $500,000 loan it is just an extra $3,644 a year because of the interest rate reduction.

Consider you have an investment loan for $500,000 interest only at 5% the repayments are straight forward, $25,000 a year. If you change the loan to principal and interest over 30 years at an interest rate of 4% the principal and interest repayments will be $28,644 a year. Which is just an extra $3,644 per year or an extra $70 per week to actually pay off the debt.

This $3,644 extra in repayments per year is only $109,200 over 30 years so nearly $400,000 of your borrowings are repaid by the interest rate savings!

The idea is to go for as long a term as possible, because it is the interest rate you are after more than paying off the loan. Unless of course you can afford to pay off more. The longer term keeps the repayments as low as possible.

So, your repayments changing from interest only to principal and interest will be similar-but unlike interest only, the loan will be paid off at the end of the term.

If you already have a principal and interest loan, is the bank giving you the best rate available? A drop from 5% to 4% on a 30-year loan will reduce the term to 24 years and 4 months if you make the same repayments. Saving nearly $200k in interest.

Start your research by going to Noel's web site and using his loan calculators and the Canstar web site to see what sort of interest rates are available. Be well armed when you approach your bank. If you don't ask you won't get.

Noel's loan repayment calculator https://www.noelwhittaker.com.au/resources/calculators/loan-calculators/
Canstar compare interest rates www.canstar.com.au/home-loans

Having said all that, as you get closer to your retirement you hope to have some spare cash to start paying down debt. But is that the right move? Nice to have lots of money sitting in the offset account just in case. Consider what your risk is. Is it unemployment and are you already old enough to access your super? If so then your super is like a bank account, you can access as soon as you stop working. A bank account that can work much harder for you than the little interest saving on your housing loan and that provides you with tax concessions.

I usually have a lot of trouble persuading people to concentrate on super contributions and just pay off the remaining housing loan out of their super when they retire. It goes against the grain. But once again the numbers prove the strategy:

Assume you have $10,000 before tax to spare
$10,000 less 34.5% tax = $6,550
$6,550 x 4.5% = $294.75pa saved
Deductible Super Contribution:
$10,000 less 15% tax = $8,500
$8,500 earning say 7% = $595
Less Tax 15% = $506 plus growth

If you have already paid off your home, you might be tempted to pay off tax deductible debt. There is even more incentive in this case to contribute to superannuation instead

Pay Off Mortgage:
$10,000 less 34.5% tax = $6,550
$6,550 x 4.5% = $294.75pa
Less Tax @ 34.5% = $193 saved
Deductible Super Contribution:
$10,000 less 15% tax = $8,500
$8,500 earning say 7% = $595
Less Tax 15% = $506 plus growth

Just make sure you check that you qualify to make superannuation contributions.

So, there you go. It won't matter who gets into power next month or how the economy is going. Using the bank's money to build wealth is a pretty safe bet.

Planning for Retirement

Pat Hennessy from our financial planning arm gave an example of a client who had 15 years until retirement, with $200,000 already in superannuation. It was in a balanced fund with only the employer contributions being made. Forecasts showed he would have $677,000 in retirement.

Simply switching from balance to growth increased the forecast for retirement to $811,000. Taking this one step further by contributing $10,000 per year in before tax dollars for 15 years and the forecast was $1,032,000 for retirement.

We regularly see people in their 50s with only $200,000 in superannuation despairing that they will not have enough to retire on. It can be done; you still have time and probably a lot more disposable income at this stage in your life.

Build for Wealth Through Business

If you have a growing business, it might be hard to save for retirement and you are relying on the sale of the business to fund that retirement. That is not a bad idea at all, there are some wonderful CGT concessions if your business assets are less than $6 million or the business turnover is less than $2 million and the business is still operating. It is important to get advice about qualifying for these concessions at least 2 years before you sell. There is also a lot of wealth building to be had in simply preparing your business to obtain the best possible sale price. There are even government tax concession which can help you get your business ready. All of this is an area of expertise for Colleen Tarrant from Ban Tacs' Brisbane office.

Investment Strategies in Uncertain Times

Noel Whittaker had many gems to share, here is a bit of a summary.

Noel reminded us that if it sounds too good to be true it probably is. He said that it is consistent saving over your working life that will achieve a comfortable retirement without the need for high risk investments. It is more important not to make bad decisions that can take years to recover from.

The amount of years between starting to save and retirement is the most important factor in the amount of wealth you create. Noel gave the following examples of the benefit of compounding

- 2 years
  $1,000/month @ 4% = $25,000
  $1,000/month @ 8% = $26,000
- 35 years
  $1,000/month @ 4% = $900,000
  $1,000/month @ 8% = $2.5 million

So how do you start? You are in this for the long haul, so it is important to get the balance between spending and saving right and achievable. Key points Noel made was:

1) Keep a budget

2) A part of all you earn is yours to keep.
2) Save first. Spend second.
3) You don't miss what you don't get.
4) The average Aussie will pay their commitments, but never save a cent. This is where borrowing to invest may help.

To get started here is a link to a free budget planner https://www.moneysmart.gov.au/tools-and-resources/calculators-and-apps/budget-planner

Once you have worked out how much you have to spare each month, direct that towards the debt you have that is at the highest interest rate, until you have it paid off.

Then concentrate that amount and the amount you had to pay off the previous debt onto your next most expensive debt. Noel does not recommend paying off your home any quicker than over 10 years. Once you get down to just that, it is time to start investing your spare cash. To keep yourself on track, set goals, consider joining a mastermind group and pay for you investments out of your pay first, not spend first and just save what is left. There will never be any left unless you treat investing/saving the same as you would a debt.

Some tips from Noel to help you along your savings path.
1) If you get caught out and need to borrow for short term debt i.e. a car. It is the term of the loan that is

more important than the interest rate. Just get it paid off!
2) Pay half your monthly mortgage payment off your mortgage fortnightly. This will mean you pay an extra month off a year and what you don't get you don't miss.
3) Noel is of the opinion interest rates are going to stay the same or go down. So, don't go fixing the interest on your loan unless it is a better rate than you are currently getting.

Now counter to all this encouragement to save, here are some figures from the seminar that give you an idea of how much better off you could be if you spend a bit of money in order to qualify for the pension.
Browns

- Home $800,000
- Shares $710,000
- Bank $75,000
- Personal possessions $45,000
- Pension $500 a year
- Investment income $32,000 plus franking of $13,700.
- Total income $46,200 pa

Greens

- Home $800,000
- Shares $800,000
- Bank $75,000
- Personal possessions $45,000
- Pension ZERO
- Investment income $36,000 plus franking of $15,400.
- Total income $51,400 pa

Greens under Labor

- Home $800,000
- Shares $800,000
- Bank $75,000
- Personal possessions $45,000
- Pension ZERO
- Investment income $36,000 plus franking of ZERO
- Total income $36,000 pa

Shares:

Noel provided some very interesting figures on share market performance:

All ords
Decade Average Return

1880s +15%
1890s +7%
1900s +12%
1910s +8%
1920s +14%
1930s +10%
1940s +9%
1950s +14%
1960s +13%
1970s +10%
1980s +21%
1990s +13%
2000s +14%

If this has encouraged you to invest in the market as a whole rather than specific shares, you can do this through indexed funds. Noel strongly recommended not investing in overseas indexed funds. He said that you can expect an Australian indexed fund to return around 4.3% plus franking credits.

Property:

Noel is pretty sceptical about property investing. He purchased a Gold Coast unit in May 1990 for $500,000 and reckons it was worth $865,000 by April 2019. Alternatively, he could have invested $500,000 in the ASX Accumulation Index in May 1990 and by April 2019 have $6,690,000.

If you would like to try this test yourself, he has a calculator on his site https://www.noelwhittaker.com.au/resources/calculators/stock-market-calculator/

Noel doesn't like apartments at all and sees the value in the land under the building. He also pointed out that if you need money you cannot just sell off the back steps or stagger the sale to minimise the capital gains tax. So, it is important to have a share portfolio for liquidity.