

ANDREW'S INDEX CARD: GUIDELINES TO YOUR FINANCIAL LIFE

- Retain some cash (2-3 months' salary) for emergencies.
 - Separate your investment capital from your life expenses, and keep it safe and out of reach.
 - Start a savings habit, putting aside 5-10% of your monthly income.
 - Pay off debt, and only borrow money for return-producing assets.
 - Buy the necessary insurance cover for health, life, car, and house.
 - Invest in your and your family's education.
 - Enrol in a retirement plan (or a retirement annuity account) and start contributing capital.
 - Buy a house, but treat it as an investment decision based on rationality and not emotion.
 - Always pay close attention to all investment costs and fees.
 - If you have a financial advisor, require full transparency of fees and the disclosure of any conflicts.
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- Open a unit trust account so you can access a money market fund, balanced funds and riskier equity funds.
 - Open a stock brokerage account if you want to buy individual shares or exchange traded funds.
 - Set aside a small portion of your wealth (e.g. 5%) for high-risk/high-return investments.
 - If it seems too good to be true, then it is: Avoid scams.
 - Gambling is not investing.
 - Don't make loans to family or friends.
 - If you get married, sign an ante-nuptial contract.
 - Write a will and a living will.
 - Express your own values in your choice of investments and financial service providers.
 - Give back to society.
 - Form loving bonds with family and friends.

Guidelines for your financial life

Andrew Canter, CIO
15 July 2019

Guidelines for your financial life

Comments on personal financial planning, savings, investment, home ownership and more

This is an introductory framework for establishing a long-term personal financial plan and investment programme. As each of us have our own circumstances, risk-appetite, tax situation and financial literacy, this document cannot serve as a financial or investment plan. Rather, it is a set of guidelines for those new to the journey of thinking about their life's financial plan. This summary cannot cover all the factors that come into personal financial planning.

While many of the comments are widely applicable, it is written for people who are formally employed, broadly in the middle-class and in the earlier stages of their career: For example, a 24-36 year old, earning enough to save, and ready to be concerned about their long-term finances.

These are my personal reflections and represent "pointers I'd give to a friend". This is a living document, and your feedback, suggestions and questions are welcome.

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Beginning your financial plan


1. Manage your liquidity

Life liquidity: You will need to have cash on hand to manage living expenses and emergencies. When you start working, build up some cash to dip into for large *expected* expenses (e.g. car purchase, holiday, furniture purchase, family wedding) or *unexpected* expenses (e.g. home repair, a family funeral, changing jobs). A good guideline is to have 2 to 3 months' worth of your salary available. However, cash in your bank account tends to be easily spent so keep a smaller portion (e.g. 15%-20%) in a bank account, and the larger portion (e.g. 80%-85%) in a money market unit trust (see #12).

Note: Inevitably, you must have a bank account for transactions. You should shop for the lowest costs and fees, easy access to your money (e.g. ATMs, online functionality), cards offered (e.g. debit, credit, credit line), the interest rate offered on balances, and range of services (e.g. foreign exchange, links to unit trust account). The world of banking is becoming competitive, so you should have a range of choices.

Once you have built up your liquidity fund *and* you have established your monthly-saving habit (see #3), you should open a money market unit trust.

Note: You should avoid letting your capital sit idle in bank accounts or money market accounts for long periods. While money market funds earn more than bank balances, they are best used as a stepping-stone to higher yielding investments (see #13).



Thereafter, you can think about your **long-term** investment plan.

Accumulating for investment: To make long-term investments such as buying a house or putting a lump-sum into a riskier/higher-return unit trust you will have to build up a bit of liquid capital in addition to your life liquidity. Money ear-marked for long-term investment, should all be put in your money market unit trust.

2. Always separate your saved “investment capital” from your “life expenditure”

Savings should be sacrosanct, never dipped into for ordinary expenses. It’s best to keep your long-term savings in separate and distinct accounts (and also separate from your emergency cash/liquidity fund). Your long-term savings are for capital investments – which should be income- or return-producing assets.

3. Aim to save 5% to 20% of your income, preferably monthly

If you do not save, you cannot invest.

Spending avoided now, allows you to spend more later:

- a once-off saving of R100 saved at the age of 20, invested at a return of 10% per annum, grows to over R5000 at the age of 60;
- a recurring R100 saved *annually* from the age of 20 to 60, invested at a return of 10% per annum, grows to more than R60 000 at the age of 60.
- a recurring R100 saved *monthly* from the age of 20 to 60, invested at a return of 10% per annum, grows to more than R600,000 at the age of 60.

Compound interest is a powerful ally for savers.

Savings is a habit, and it is something you should start early in your career. Some research indicates that individuals should have saved 1x to 2x their annual salary for retirement by the age of 35 (see **Annexure 1**).

Saving is foundational to having a long-term financial plan. Start saving early. The more the better.

Note: During your life there will also be inflation in the cost of goods and services (as normally expressed in the ‘Consumer Price Index’ or ‘CPI’), and this inflation degrades the spending-power of your savings. The difference between the average return, say 10% (as in the example), and the inflation rate over the period, say 5%, is called the ‘real return’ or the return above inflation: In this example, a 5% p.a. real return (10% return minus 5% inflation).

If you save R100 at the age of 20, and earn a real return of 5% (a nominal return of 10% p.a. minus inflation of 5% p.a.) until the age of 60, it will have the spending power of only R740 in your 20 year old’s money. Put differently, the R5 000 in your account at age 60 would only buy as many goods as R740 at age 20! The point is that your investment returns must be *above* the inflation rate in order for you to successfully build up future spending power.

4. Avoid using high-cost debt, and pay it off as soon as possible

“Investment” is the **earning** of returns on your saved capital. “Debt” is the opposite of “Investments” in that you are **paying** interest on capital versus **earning** interest on capital. Thus, any investment plan has to start with managing your debt.

Borrowing (i.e. debt) should generally only be used for return-producing investments such as education, housing, or a business. You should never use debt (i.e. borrowing) for assets that depreciate quickly (e.g. clothes) or for consumables (e.g. food). Always pay cash for consumables such as food, clothes, entertainment or utilities.

If you use a credit card for convenience, then pay it off religiously every month. Longer-term use of credit cards, micro loans, personal unsecured loans, furniture loans/store credit, etc. are all forms of financial enslavement: They are a trap to be avoided.

Compound interest is a powerful enemy against borrowers.

Borrowing money for a car, furniture or large appliances (e.g. a fridge) may be exceptions, in that you may need these items to establish yourself in a home and professionally. It is preferable to save money in order to buy such consumer goods, but if you must use debt then pay it off as soon as possible. Keep in mind that your cost of borrowing (e.g. the interest you pay) is very likely to be much higher than what you might earn on investments (e.g. the interest you might receive).

Note: Be highly conscious of all the costs of financing such goods – as furniture retailers are very effective at charging high rates, fees and costs for goods bought on “account”.

Note: Never underestimate the overall cost of having a car. Aside from finance costs, there is insurance, repairs, petrol, and traffic fines. The more expensive the car, the more costly it is to drive, maintain, insure and repair.

Note: Young people are often encouraged to borrow money to “build up a credit record”. There might be merit in having a general-purpose credit card (e.g. Visa, MasterCard) for convenience and track record. However, you should actively manage your credit card: Pay off your account every month (after all, that is how you establish a good credit record)!

5. Buy suitable insurance

Insurance coverage you should consider includes health, disability, life, auto, and home insurances. Life, health, “dread disease” cover (which offers payments in cases such as cancer or heart attack), and disability cover (which provides continuing income in case you become disabled and cannot work) are usually part of employer-based insurance schemes, and are often cheaper than you can buy on your own (see note under #7).

Life insurance is most vital when you have dependent children or parents who rely on your livelihood, or to settle your family’s home bond in case of your death. In those cases, it may be worth buying additional life insurance cover through your employer’s scheme. If you don’t have dependents, then you probably don’t need life insurance.

Note: If you have debt when you die, the debt will be repaid from the proceeds of your estate (e.g. the sale of your assets such as your house, car, investments, etc.). As a principle, your liabilities at the time of death cannot be transferred to your family members. Exceptions to that might arise depending on the terms of your marital/life-partnership arrangements (such as an ante-nuptial contract), joint bank accounts and, of course, if a family member has actually co-signed (or signed as surety) on a loan.

For car insurance, shop and re-shop insurance prices annually – car values depreciate over time and so insurance premiums should drop. For car or home insurance, consider choosing a higher deductible/excess (i.e. the amount you pay on any claim before the insurer pays; your share of the loss) as this allows you to pay less insurance premium, and puts you in an insurer's lower-risk group (thereby lowering your insurance costs).

6. Education is an investment

When you choose to buy further education (for yourself or your children/family) you are making an investment: You should assess the cost of studies (and debts you might incur) against the expected return on that investment. Such returns might take the form of higher expected earnings, better career prospects, and greater flexibility in your professional life.

Note: For tertiary/advanced education the world is quickly shifting toward educational alternatives such as on-line courses and free coursework. While some industries are more accepting of such alternative training certifications coupled with experience (e.g. technology sector), other industries still strongly favour formal (e.g. tertiary institution) qualifications (e.g. finance sector). Thus, your decision to spend money on advanced education must be informed by your chosen career and industry – and it may be more efficient to spend time & effort on education rather than money. For your children, evidence seems to indicate that the choices you make for primary and secondary education remains vital to their future success -- even though a "cost:benefit" or "return on investment" calculation is nearly impossible.

Basic investments

7. Your first investment is likely to be in a retirement scheme

You should maximize your use of tax-advantaged savings, such as employer pension/provident savings schemes, retirement annuities, or other long-term tax-free investments. These programmes are supported by government and businesses to encourage saving for retirement. (In all cases be conscientious about costs and fees, as detailed in #9 below)

Such savings programmes are designed to be:

- a form of 'automatic' or 'enforced savings' (e.g. it promotes regular monthly, automatic savings);
- slightly removed from you (e.g. safe from "piggy bank raiding");
- usually good value for money in terms of costs and fees;
- tax efficient (i.e. reduce your current tax bill);
- aimed at long-term saving for retirement; and
- (usually) invested into suitable medium-risk investments.

Note: While this document is written for South Africans, the principles are directly applicable to other countries. For example, the U.S.A. has pension plans, 401k plans and Individual Retirement Accounts, which operate on much the same principles as discussed here.

If you are a member of a company sponsored retirement plan or have opened your own retirement annuity account, you should aim to contribute as much as you can afford on a monthly basis. This allows you to gain the immediate tax reduction, and start earning returns to maximise your retirement nest egg.

Note: Up to annual limits (2019: 27.5% of your gross income, up to a maximum of R350 000 per annum) money taken from your current earnings into your retirement fund is not taxed in the year you earn it. Rather, the full capital is invested and you only pay tax years later when you make withdrawals from the retirement savings fund (at which point you should be paying a lower tax rate).

Most company retirement schemes allow you to elect to save 5%, 10%, 15% or 20% of your salary in retirement savings: You should contribute no less than 10% and, when in doubt, save more.

Note: Be conscious that deductions from your pay for employer retirement schemes usually include "risk benefits" – the insurance cover described in #5 (e.g. life insurance, medical insurance, disability insurance). As noted, this insurance is usually good value for money, is negotiated by your employer, happens automatically, and you generally need these insurances in your life. However, the costs of these insurances usually come off your chosen retirement savings: For example, if you elect to put 5% of your salary into the retirement scheme, you may find that 2% (or more) of the 5% is actually paying for your insurances – leaving only 3% for actual retirement savings. Thus, rather elect to put away 15% so that you will be actually investing 13% (15% less 2%) after the insurance costs.

Once you have joined your employer's retirement scheme or opened a retirement annuity account you will be required to choose from a (usually short) list of underlying investments. These will typically be a choice of two or three balanced funds (see #14).

Note: The phrase "Defined Contribution retirement scheme" can be confusing, but what it's really saying is that: a) you will choose how much to contribute to the retirement scheme and which funds to invest in (both choices are within a narrow range of choices offered by the scheme); and b) thereafter you get all the investment returns earned, but if you do not have enough money saved at retirement then no one is going to top-up your pension payment. Thus, you are responsible for managing your own retirement planning, and if it is inadequate then it is entirely your own problem.

By contrast, historically many schemes were called "Defined Benefit retirement schemes" because the employer would guarantee a pension after retirement (for example, a guaranteed pension of 65% of your final salary adjusted upward by inflation each year), and it was the employer's risk and liability to pay your agreed pension. However, over the past 25 years "Defined Benefit" schemes have been almost completely closed, and employees have been migrated to "Defined Contribution" schemes -- thus transferring pension risk from employers to employees (i.e. you!).

If you change jobs, do not cash out your retirement savings: Transfer your accumulated retirement savings from the old employer's pension scheme to the new employer's scheme or invest it into a preservation fund. If you withdraw the cash (rather than transfer to a new retirement scheme), the money drawn from your retirement scheme is fully taxable in the year you withdraw it, and you will have restart saving for retirement!

Note: Your retirement scheme may form part of joint accrual if you are married in community-of-property (see #21).

In sum, you should assume that no one is going to look after your pension and retirement for you: You need to think about retirement planning for yourself.

8. Your next major investment is likely to be a home

Buy a home when you are professionally secure and stable, as well as financially ready to take on the responsibility. You should always view a house as an investment: Buy based on a good price by applying rational (and not emotional) metrics, such as:

- Price per square metre;
- Expected capital appreciation;
- Relative price for the area;
- State of repair and general condition of the property;
- Potential cost of repairs/upgrades (and age of the house);
- “Location! Location! Location!” and
- Rental income that could be earned on the property (or rent-payment-avoided if you had to rent the property).

Note: In buying a house, it is important to pay attention to timing (i.e. when you choose to buy): Property prices move in cycles, up-and-down or up-and-sideways, and are very sensitive to interest rates (e.g. when interest rates rise property prices tend to stagnate or fall).

Note: It is normal to start out by renting, as it allows you flexibility in your career and life, and it is often less costly than buying at any moment-in-time (both in terms of not requiring any capital investment, and in possibly requiring lower cash-flow each month than owning). But rent goes up over time, and you realise you are “paying off someone-else’s bond” with higher rental payments. If done intelligently, property is a sound long-term investment which tends to accrete value.

Purchasing a property is an investment on which you expect to earn a return: Therefore *it is* suitable to borrow money to buy a home. Buying a home is one of the few investments most people should make with borrowed money (although arguably investing in education is a suitable use for debt as well).

Note: Mortgage interest rates are much lower than other forms of borrowing you might access, such as car loans, credit card loans, or personal unsecured loans. For example, a home loan rate might be 10.25% versus 26.5% on personal unsecured debt [01/2018]. This arises because the lender has security over your house (i.e. they can take your house and sell it if you don’t pay back the debt!), and also due to competition in the housing loan market.

Before considering buying a house you will first need to consider what you can afford to buy. Some costs to consider are:

Up-front costs of buying a house: You will need enough liquid capital (see #1, #2, #3 & #4) in order to pay the deposit, bond registration costs, transfer duties (VAT) on the property, legal/conveyancing fees, moving costs, and home establishment costs (e.g. curtains, furniture).

Note: The transaction costs of buying & selling your house are very heavy. Summing up taxes, legal costs, inspections, and agents’ commissions the costs can be 8% (or more) of the value of the house you are buying or selling. So, while you should – over time – move houses (bigger, nicer) as you earn more, try not to trade houses too frequently.

On-going costs of owning a house: You can apply a bankers' rule-of-thumb that your total home expenses should not be more than $\pm 30\%$ of your total monthly income. In assessing that, be sure to include all the on-going expenses, such as the cost of the monthly loan repayment, municipal rates and taxes, all utilities and services, levies (for sectional title units), maintenance, home owner's insurance, and (if required for your bond) life insurance.

Note: You should budget to have annual maintenance expenses of at least 2.5%+ of the value of the house. This might be higher for older houses, or might be partially included in the levy in sectional title units.

Your first property investment is likely to be a small starter-home or apartment. It is not unusual for you to feel "house poor" since a) all your liquid capital has gone into the acquisition cost of the house, and b) much of your monthly pay cheque is going to home expenses (e.g. 30% of gross income) and income taxes (e.g. 30-35% of gross income). Don't be afraid of this as, so long as you have done your homework/consideration/house-shopping properly, you can usually rely on your annual pay increase to reduce the strain.

Some other home ownership notes:

- a. Try to put down a substantial deposit (that is don't borrow 90-100% of the home price) so you have flexibility later (e.g. in case of emergency needs, or job loss).
- b. A home is a good "commitment device" in that we tend to pay our mortgage monthly, and over time (as you pay down the loan) you will own a large asset (the house) debt-free.
- c. Do not use your home as an ATM by dipping into your home equity for consumer goods (see #4).
- d. In any case, it is very rewarding to own your home with no debt.

Note: A good long-term strategy is to pay off your primary house, and once you have a large amount of equity in your home (i.e. you have repaid most of the loan), you can consider using that borrowing power to buy another rental property. You can borrow against either your primary house, or the rental property, in order to build a portfolio of properties. However, all the rules of buying a house (above) apply to all property investments. Be aware that the capital-gains tax rate on your primary residence (i.e. the house you actually own and live in) is lower than for investment properties.

- e. A house is the single largest investment you are ever likely to make, so you should spend proportionally more time choosing a house than any other goods/services you ever buy.

Note: A good rule of thumb in all of life's spending decisions is: *The more it costs, the more time you should spend researching and thinking about it!*

Engage intently with the contracts around buying and selling properties. All these contracts can be changed (with a pen in hand) to suit your needs/desires: Despite what estate agents say, these are **negotiable** contracts, and are not carved in stone! When you are buying a property you usually sign an "offer to purchase", and that is a binding contract which can be enforced against you if you try to change your mind or simply walk-away from the purchase (in particular, if you have paid a deposit you may forfeit it). Before signing an "offer to purchase" pay attention to details, such as:

- estate agents' contracts;
- offers to purchase;

- commissions;
- what’s included in the price (e.g. pool cleaner, blinds);
- what’s excluded from the price (e.g. appliances); and
- transfer of ownership arrangements (e.g. timing of transfer, timing of occupation, occupational rent to be paid until transfer);
- any other conditions to the contract (e.g. inspections, loan approval, access).

Be aware that estate agents and transfer attorneys have a well-oiled machine for extracting costs and fees from buyers (and sellers) of property (see **Annexure 2**).

Note: House purchases benefit from various government/tax supports that promote home ownership. For example: 1) rental paid by you is not tax deductible for you, and it is taxable income to your landlord -- but your own “implied rent” on living in your own house is not taxed; 2) capital gains on your primary residence (when you decide to sell the house) are taxed at a lower rate (relative to other investment gains); and 3) in some countries the interest on your home loan is tax deductible.

In the long-cycle of your life: a) you will use debt to buy a house; b) you will move a few times to new locations and larger houses; and c) by the time you approach retirement your home should be fully paid off, allowing you to live rent-free (and debt repayment free) into your retirement years.

Getting ready to make discretionary investments

The sections above are your primary long-term savings vehicles -- you should establish these and stick to them. But what you really want to know is "How can I get rich quick!?" Making high returns on investments is a tricky affair – despite the success stories you hear (no one tells you when they lose money!). It is suitable to try to make long-term returns by making "discretionary investments": These are investments you actively choose, by exercising your judgement and taking meaningful risk.

Before you start making direct, discretionary (i.e. chosen), active investment decisions you a) need to know the key areas to focus on, and b) you need to have set up accounts in order to implement your investment plan.

Such planning and preparation prior to making investments always requires meaningful time and documentation: Do not be dissuaded by the paperwork!

9. Keep a close eye on all investment costs

All financial tools/products have some embedded costs and fees – which is reasonable since you are buying a service. As a rule, the more people between you and your investments, the more fees and costs are involved. Investment related costs go on year-after-year for decades, and add up to a big reduction in your investment returns.

Never be shy to ask, “What does it cost?”, “What are the fees?”, “How many layers of fees are there?” If you don’t understand the answers then you should be suspicious.

As with all purchase decisions in life, *if you don't know what you are paying for then you shouldn't be buying the product.* Do not be intimidated!

- a. Generally, you should not pay initial (entrance) fees on unit trust investments (go directly to unit trust managers, not via a broker).
- b. Brokerage fees on trading listed shares are negotiable: Shop around.
- c. Middlemen add heavy costs. If you feel you need financial advice to implement your portfolio (e.g. choosing which range of unit trusts to buy), rather pay a fixed, declared fee for the service instead of a continuing (e.g. annual) fee or a "percentage of assets" fee (see #10).
- d. Remember that anyone showing you an investment product is trying to sell you something –so engage with them in that manner (e.g. it doesn't matter if they are a friend/family... they are salesmen earning a fee!).

10. Assert a "fiduciary standard" with any financial advisor

Investments can be complex, and hiring someone to give you advice is suitable and reasonable. If you decide to have a financial advisor, ask him/her to commit to a *Fiduciary Standard, such as:*

"All the advice you are giving me, and all the products you offer me, are designed to help me achieve my investment and financial goals; you will tell me about any fees you earn on my investment decisions; and you will tell me about any other potential conflict of interest in giving me advice."

You may pay a visible, discrete fee for such service, but then you should get objective advice and not fee-driven advice.

11. Open a unit trust account

A good starting place for your savings and investments is to open a unit trust account. Unit trusts are a well-regulated, transparent, and suitable way for individual investors to implement an investment strategy.

Unit trusts pool investors' money and build up portfolios of assets in accord with each fund's name and purpose. For example, a "gold fund" will buy a portfolio of gold shares, while a "general equity fund" will buy a portfolio of the largest shares listed on the JSE, and an "emerging market equity fund" will buy a portfolio of shares in companies from emerging markets around the world. Such funds are an easy, efficient way for individuals to access fully diversified portfolios with relative ease (i.e. the fund manager chooses shares and constructs the portfolio of shares, so you don't have to).

Unit trusts can be equity funds (e.g. building up portfolios of listed shares); bond funds (e.g. building up portfolios of listed bonds); property funds (e.g. buying a portfolio of listed property shares); money market funds (see #13); balanced funds (see #14), etc.

Unit trusts can be “Active” or “Passive”: In Actively managed funds portfolio managers will perform research to choose particular shares which they assess will earn higher returns than other shares. In Passive funds the fund manager only seeks to exactly match the composition (and returns) of a market index (e.g. the JSE Top40 Index, the S&P 500 index) and does not apply any judgment. As you’d expect, fees for Active management are higher than for Passive funds.

Unit Trust funds should not have any entry/exit fees, but you will pay an asset management fee on the assets in the fund (generally ranging from 1-2% per annum for balanced or equity funds, and less for bond, income or money market funds).

Some advantages of opening a unit trust account are:

- a. You can access a range of investment funds, and are able to move money into or out of the funds, as well as switch between funds;
- b. Your initial investment can be in relatively small (e.g. R5 000-R10 000);
- c. If necessary you can access your capital within a couple of days. Although this should not be seen as permission to use your “investment capital” for your “life expenditure” (see #3), it does give you flexibility if you decide to make a big shift (e.g. buying a property, emigrating);
- d. Opening a unit trust account will give you access to a money market fund (as per #13), and a balanced fund (as per #14), as well as other – riskier or specialised – funds in which you may want to invest;
- e. By keeping most of your investments in one place, you can get integrated reports on your investment holdings as well as the performance of your assets, thus enabling you to monitor your investments more easily;
- f. To make regular savings easier (e.g. more automatic), unit trust companies can (with your permission) take a debit order off your bank account monthly (see #15); and
- g. Large unit trust companies can also offer products to access tax-advantaged savings (e.g. retirement annuities, tax-free savings accounts) (see #7).

Later, you will have to choose **what to invest in**, but first you must choose **where to keep your investments**. Here are some notes on choosing a unit trust management company:

- a. You should look for a large, stable, respected unit trust management company that has a reasonably wide range of funds (e.g. equity funds, international funds, balanced funds, money market funds, bond funds, income funds).
- b. You should check that they have a helpful, responsive, user-friendly call centre that can answer basic questions about products, fees and flexibility. Test this yourself. Keep in mind that call centre staff are not allowed to give actual financial advice: They are not financial planners and cannot tell you what to invest in.
- c. They should have a helpful, user friendly, logical website, with easy access to forms and information.

- d. They should be able to show you sample reports, market comments (e.g. market/economic reports) and fund investment reports (e.g. showing fund holdings, fund performance, book values, tax reporting, fund transactions) which are readable, useful and understandable.
- e. Looking at which funds you might invest in (see #13, #14 and #17), look at those funds' fees (compared to other unit trusts), and their investment performance (compared to other unit trusts and their market benchmarks).

Note: A "benchmark" is usually a broad market index to which funds' performance is compared. For example, if you buy a U.S. equity fund it might be compared to (i.e. "benchmarked against") the S&P 500 Index of the largest 500 shares; or a South African general equity fund might be benchmarked against the JSE All Share Index. Most funds and fund managers seek to have investment performance which is better than the fund's benchmark, and also better than most comparative funds. You should compare such investment performance over 1, 3 and 5 years.

You get a better night's sleep, more choice, and better service from a large and stable unit trust management company.

Note: You should resist the urge (or the advice) to have too many dispersed brokerage/bank/unit trust accounts or other financial products. Having too many accounts makes it very difficult to manage your affairs, makes your tax returns more difficult to prepare, and you end up with pockets of unmanageable, unreported assets. Also, every product has a different set of risks, returns, fees, and conditions – and that usually adds confusion to your financial affairs.

The broad statement that unit trusts are "safe" arises from their rules and regulation which are aimed specifically at protecting retail investors. However, you should be mindful that the investment risks of each unit trust fund vary depending on what each fund is investing in: For example, a money market fund holds very low-risk, low volatility, short-term loans, while an emerging market equity fund may have very high volatility during market panics.

12. Open a stock brokerage account (but only if you intend to buy/sell individual shares or Exchange Traded Funds [ETFs])

You only need to set up a stock brokerage account if you intend to invest in, or trade, individual shares or ETFs (see #17). The key to brokerage accounts is the commission rate (i.e. the transaction fee) on share trades. In South Africa, by comparison to global standards, commissions can be quite high. Brokerage commissions are usually quoted as a percentage-of-trade-value (e.g. a commission rate of 0.5% means if you buy R100 000 worth of shares, your commission fee will be R500). Brokers have many attributes they promote, but your important choice is between a) a lower commission rate, versus b) access to equity research services and advice. If you want a brokerage firm that provides share research you will pay a higher commission; if you do your own research then you can find a broker with a lower commission rate. Trading individual shares should really only be done if you think you have some particular insight, economic opinion, or company view.

Opening a brokerage account requires some effort in selection and documentation, similar to buying a house, or opening a unit trust account. However, if you don't have the account opened, when you are ready to make an investment decision you won't be able to take action.

Establishing your discretionary investment portfolio

13. Your first discretionary investment is likely to be to build up some cash for further investment, most likely in a money market unit trust or RSA Retail Bonds

You must have some liquid resources (see #1), but from a long-term investment point of view “cash is trash”: It always has the lowest long-term expected investment return, and offers the lowest return above the inflation rate. Thus, from a long-term perspective, it is usually your worst investment choice (but, of course, better than simply spending the money).

To reiterate some points elsewhere in this document:

- a. Except for a core holding for ready-liquidity purposes, you should minimise cash in your bank account.
- b. If you are building up liquidity for an investment (e.g. for a forthcoming house purchase, or to build up an investment sum) it is best to put it into a money market unit trust where you might earn, say, 7% instead of 0% to 3% in a bank account.

Note: A money market unit trust fund is a highly regulated, low-risk, liquid holding (e.g. you can get your money within 48 hours). Such a fund takes investors’ money, pools it, and invests in a range of bank deposits, treasury bills, corporate short-term loans, and the like in order to create a diversified portfolio. The advantages are that the fund provides diversity (e.g. as opposed to keeping all your funds at a single bank), earns a higher yield than an individual is likely to be able to earn, and such funds also have virtually no price volatility (unlike, say, a general equity fund that might rise or fall by 1-5% in a week!). There is a management fee, but this is usually small and the fund should earn a net return (after fees) which more than covers the cost.

- c. A big mistake we all tend to make is that when we have extra cash we put it in the bank, earning low (or zero) returns – but when we need cash we borrow from a bank, paying high rates.
- d. As a first choice, when you have extra cash, always pay off high cost debt (e.g. student loans, car loans, personal loans).
- e. An exception to the “pay off debt first” rule may be your home loan, provided a) your cost of borrowing is prime minus x (e.g. prime – 1.5%) and b) you are putting savings into another investment you expect will earn more than the cost of the home loan.

Note: The exception to “cash is trash” is when you sell risky assets (such as shares or a property) because you expect their values to drop. It is, of course, better to be holding cash in a bank account earning 2% than holding a share portfolio when it drops, say, 15% in a crisis. However, market timing (i.e. trying to trade in and out of the market to make gains or avoid losses) is incredibly difficult, and you should set and maintain a long-term, stable investment strategy (as described herein). Most long-term studies of investor returns indicate that market timing is a bad idea for most individual investors – as we tend to buy and sell at the wrong time.

- f. An alternative to bank accounts and money market funds are the RSA Retail Savings Bonds. These bonds are easily accessible government issued bonds that offer market interest rates with no fees. The bonds can have terms of 2, 3 and 5 years for investment amounts from R1 000 to R5 000 000. These should be considered fixed-term

investments: If you buy a 2-year bond, you will have to hold it to maturity, unlike unit trust holdings which you can sell at any time.

<https://www.gov.za/faq/money-matters/how-do-i-invest-rsa-retail-savings-bonds>

14. Your next most likely discretionary investment is in a “balanced fund” unit trust

The phrase “asset allocation” refers to an over-arching, long-term investment strategy for allocating your investments into different asset classes, such as shares, bonds, property, liquid-assets, as well as some international assets. For your discretionary investment portfolio, your asset allocation can be relatively simple: A portfolio of equities, bonds, money market assets, and properties.

For South African investors 15% to 25% of those funds should be in non-Rand assets.

Note: This balanced-fund discussion is about your discretionary investments. However, when considering your overall “asset allocation” you should include the value of each of your investments -- including cash, pension scheme, real estate (net of debt), etc.

This may sound daunting, but in order to access all these asset classes a balanced fund unit trust is a good, first long-term investment choice: If you know nothing else (or have to make an election in your pension scheme) – choose a low-cost, balanced fund managed by a credible, large, asset management company.

A balanced fund invests in a mix of asset classes, for example, equities (65%), bonds (20%), listed property shares (5%), cash (5%), and inflation-linked bonds (5%).

Note: These percentages are merely for demonstration, but are suitable for someone early in their earning years.

Your balanced fund should be holding 15% to 25% in non-Rand (e.g. US\$, Euro, Yen) assets, which protects a part of your wealth from local currency risk. Foreign currency exposures do not change your overall asset allocation: For example the balanced fund’s 65% in equities may be split into 50% in SA equities and 15% in non-SA equities (and similarly for other asset classes).

Note: For overall asset allocation, younger people (who have many years of earning and saving ahead) can bear higher exposure to more volatile listed equities, while retirees (who cannot bear large capital losses, as this would impair their lifestyle) should have more fixed-interest assets (such as bonds, inflation linked bonds and money market assets).

A good rule of thumb is that your asset allocation between equities and fixed-interest should be to subtract your age from 110, and that is the percentage to have in shares (e.g. If you are 30 years old, then $110-30=80\%$ equities; if you are 70 years old then $110-70=40\%$ equities). (This used to subtract your age from 100, but with growing longevity the rule of thumb has shifted).

15. A good investment strategy to employ is a “rand-cost-averaging” approach

If you save the same amount of money monthly (into your retirement plan and your discretionary investments), then when stock prices are high you buy fewer shares (which are more expensive), and when stock prices are low you buy more shares (because they cost less). As noted above, your savings habit should be regular and on a schedule (e.g. monthly): You can set up debit orders/automated investments from your bank account to your unit trust account so you don't have to think about it or take any particular action.

16. Now you've got your core financial and investment plan!

Having followed the steps above, you now have –

- some liquidity on-hand for life's needs and surprises;
- segregation of your life expenses/liquidity needs and your investment capital;
- established a habit of saving 5-20% of your monthly pay;
- been using those savings to build up your net worth by paying-off debt, contributing to your retirement scheme, and transferring money to your investment account;
- bought necessary insurance on your life, health, home and car;
- established some sort of retirement savings (probably invested in a balanced fund);
- bought your own home (with some debt against it, but being paid down regularly); and
- invested into a money market fund (for liquidity) and a balanced fund (to access a blend of asset classes and non-Rand assets).

So, what next?

17. Risky investments?

Hereafter, you might make some other investments. The younger you are, the more risk you can bear in order to earn higher returns (see the guideline note under #14). In the first instance such riskier investments will most likely be in either a) individual shares (i.e. equities) (see #12) that you follow or have some insight into, b) specific sector unit trusts such as a technology fund, a resources fund, an offshore equity fund, etc., or c) some other high-risk venture or speculation.

- a. Unless you have some particular insight about certain companies, you should generally stick to very low-cost passive unit trusts or Exchange Traded Funds (ETFs).

Note: An ETF is very similar to a unit trust – you can buy or sell shares of a pool of diversified assets. However, instead of accessing these via a unit trust management company which transacts units once-per-day (usually at 16:00), ETFs are listed on the JSE, so can be traded during the day. However, in addition to an embedded asset management fee (similar to unit trusts) you will also need a brokerage account with a stock broker, and you will pay commissions on transactions. Essentially, ETFs are unit trusts which are useful for people who want to buy and sell during the day (which should be very few people).

- b. If you feel you have particular investment insights about companies or sectors, then you might trade individual stocks or sector funds.
- c. Keep emotions away from investment decisions: Too many people get scared and sell at the bottom (low prices) or chase high prices at the top of market cycles.
- d. Keep in mind that for every buyer there is a seller (and vice versa): You should assume that the person selling to you (or buying from you) knows more than you do.

Up to now your money is in several pools:

- Bank Account
- Money Market Fund
- Retirement Scheme
- Unit Trust Account and, within that, some unit trust funds with higher risk profiles (e.g. equity funds, offshore equity funds).

You might now add to this list a pool called:

- Risk Money

This additional limited pool (e.g. maybe 5% of your assets) can be used for higher-risk tactics, such as buying individual shares (on which you have an opinion), supporting a small business, speculating in commodities or crypto-currencies, etc.

But keep in mind that about 95%+ of all start-up businesses fail, and speculations frequently go awry, so your Risk Money pool should be limited to money you can afford to live without (i.e. money you are willing to lose).

Additional good investment sense

18. Avoid scams!

Here's a solid rule of investing: *If it seems too good to be true, then it is!* For a start, when considering any investment proposal look at the "Prime Rate" of interest posted by the banks: If someone is 'guaranteeing' or 'projecting returns of' anything above the Prime Rate, then the proposal is already suspect – and the more return they are 'guaranteeing' or 'projecting' the more likely it is to be a scam. For example, if someone says you'll earn a 'guaranteed 20% p.a.' then you probably have a 90+% chance of this being a scam, and above that you may be looking at a fraud.

Just the word 'guarantee' should tip you off to risk: Always ask "Who is offering the guarantee?", and assess their credibility. The only so-called 'risk-free' investments are in government issued securities, and they are only risk-free because the government can, literally, print money to pay you back.

19. Gambling

Gambling of any sort (e.g. lottery, casinos) is a rigged-game which is specifically designed to take your money by degrees. Gambling is not investing!

20. Don't extend loans (debt) to friends or family

Almost universally, making loans to friends and family ends up breaking up relationships. As a starting point, if the person were credit-worthy they would be able to access money from other sources (e.g. credit card). Practice this phrase: *"I never lend money to friends or family because it usually creates conflict, and I value those relationships too much to put them at risk."* However, if you feel you really want to support a friend, then consider giving them money.

Sometimes, a friend or family member has an investment or business idea which may be worthy of you becoming a partner (that is, a shareholder). In such cases, apply your best judgment, agree on the terms of your partnership and, if you proceed, you should consider such investments part of your "risk capital" (see #17).

As a hard rule, for a friend/relative never lend or invest more than you can afford to lose.

21. Marriage & Marriage Contracts

Relationships go through cycles -- they have beginnings and endings: Statistics show that many marriages break up. In South Africa, the law recognises three types of marriage contracts: Civil Marriage, Customary Marriage and Civil Union, each with its own specific requirements and legalities. Thus, before getting married, it is wise to take advice to help you decide how best to arrange your marital affairs. One way to do this is to sign an ante-nuptial contract before you get married. Such an agreement should cover your agreements about complex issues such as ownership of your pension scheme, properties, earnings during your time together, employment-related incentives, arrangements in case of death or divorce, etc.

It is best to not rely on common-law or the government to decide your and your spouse's financial fate. Sadly, often when the love ends, the fights begin.

22. Death and Dying

You should write a will to specify how you want your assets (your "estate") to be divided amongst your heirs, and who is authorised to manage your estate (the "executor"). If you die without a signed will ("intestate") then the government will appoint an executor to manage your estate: That executor may be expensive, and may not care about you, your wishes, or your heirs' circumstances -- they must follow rigid rules, thus delaying the clearing up of your affairs, while your heirs (i.e. your family) remain frustrated.

Simple wills can be obtained at a very low cost (or even free of charge) from banks or other financial services firms. It is unfair (and unnecessary) to leave your heirs with uncertainty

and/or problems. Your will should be kept by your executor and possibly with a trusted friend/colleague (but generally not with someone who is a beneficiary of your estate).

Review your will regularly – especially after major life changes (e.g. financial changes, marriage, divorce, children, etc.) you should make a new will and remember to revoke the old will.

It is also a very good practice to write a living-will (also called an advance-directive) – which specifies your desires for end-of-life care (particularly if you cannot speak for yourself at that time), and may also give your instructions as regards organ donation. This will assist your doctors and family to make potentially difficult decisions on your behalf, based on your written wishes. It is important that your heirs/family are aware of (and have a copy of) your living-will/advance-directive so that they can access it quickly if necessary.

Note: Some financial services firms or lawyers will assist you to write your will (and your living will), but may seek their own appointment as your executor. You will need someone trusted and independent to be your appointed executor, but – as with all things – executor’s fees are negotiable and you can agree the executor’s fees in advance. Will and living-will templates can also be found on-line.

Note: For both your will and your living-will, the signature process is very important for the documents to have any force. Notably, when you sign the documents there must be an actual person there, with you, to act as a witness to your signature (this is true for many contracts, and is referred to as “witnessing”. Your will should be signed by yourself and witnessed by at least one other person (who is not a beneficiary of the will) in your presence. Your living-will signature should be witnessed by two people, in each other’s presence (along with you), and neither of those people should be a family member, beneficiary, trustee or executor of your estate.

23. Express your values in your investments

You can express your personal values through your selection of investments. With a bit of mindfulness and effort, you can choose funds or companies (or even financial services providers) who act responsibly, ethically, and in a manner which is sustainable. For example, you may be able to find funds that invest in developmental investments (e.g. infrastructure or social services) or avoids “sin stocks”. You may assert your own beliefs by avoiding investments in tobacco, alcohol, gambling, pornography, factory-farmed animals, armaments or (in an era of global warming) carbon emitting industries. Even if it seems difficult to make such investment choices, you can ask your service providers (financial advisor, fund manager/s) to give reports on their sustainability practices. In short, you should be conscientious about how your hard-earned, long-saved money behaves in the world: Choices are in your hands.

24. Support the social safety net

We live in a society, from which we all benefit and in which we all have a role to play. Thus, we should each contribute to society: Generally that means paying your share of taxes and contributing time or money to charitable organisations.

Note: Contributions to registered charitable organisations are tax-deductible in South Africa, reducing your income tax.

25. Be connected to people who matter to you

Financial security and control of your financial destiny can offer some peace of mind, and a degree of freedom. But all research shows that our best investments are in the relationships in our life. The more we love and are loved the longer we live, the healthier we tend to be, and the happier we are.

Annexure 1: The Power of Compound Interest

The power of saving and compound interest: The case of twin brothers Iqbal and Reza

On his 20th birthday, Iqbal started a unit trust investment with a contribution of R1 000 per month. Reza could not start immediately, so on his 27th birthday he initiated the same investment of R1 000 per month. At the same time, Iqbal stopped contributing and was never able to contribute again. For the full duration of all their investments, they both received the same return of 10% per annum.

Reza and Iqbal both retired on their 60th birthday. Iqbal had R3 261 705 in his account, while Reza had R3 115 075. This is despite the fact that Iqbal had contributed only R84 000 and Reza R396 000.

*This is a reminder of the importance of saving and investing from an early age to fully harness the power of **compound interest**.*

From Andrew Bradley, CEO of Old Mutual Wealth.

<http://www.destinyman.com/2016/05/17/teaching-children-basic-investment-literacy/>

You need this much retirement savings at your age and income

PAUL KATZEFF 3/23/2018

Are you saving enough for an affordable retirement? Knowing how much to save for retirement is a key question in planning. Yet many people don't know how to figure out the right amount of retirement savings and don't even try, even though knowing is important to their financial health.

But here's a practical, fast way to get a rough idea of whether you're on track, and it's easy-to-use.

It provides an estimate of the figure you'd come up with if you went the longer route of making a budget, calculating how much of your expenses will be each year in retirement and then crunching those numbers.

All you need to do is see if your retirement savings match a specific percentage of your yearly income. That percentage changes, depending on your age. It also changes, based on your income.

And except when you are relatively young, that percentage is actually a multiple of your income. For example, if you are 35 years old and your annual income is \$50,000, you should have 90% of your annual income saved to be on pace to build the right size nest egg by retirement at age 65, according to research by J.P. Morgan Asset Management.

How Much To Save For Retirement: At various ages, your nest egg should be this many times larger than your household income. "Enough" means:

- *your savings have at least an 80% chance of lasting 30 years after you retire.*
- *your nest egg averages 6% average annual growth.*
- *you continue to save 10% of your income yearly until you retire at age 65.*

Are You Saving Enough For Retirement?							
	At this income:						
	\$50,000	\$75,000	\$100,000	\$150,000	\$200,000	\$250,000	\$300,000
At this age:	You'd need this multiple of your income:						
35	0.9	1.6	2.0	2.6	3.0	3.4	3.5
40	1.6	2.4	2.9	3.6	4.2	4.6	4.8
45	2.5	3.4	4.0	4.8	5.5	6.0	6.2
50	3.5	4.6	5.3	6.3	7.1	7.7	8.0
55	4.7	6.0	6.9	8.1	9.1	9.7	10.1
60	6.2	7.7	8.8	10.2	11.4	12.2	12.6
65	8.1	10.0	11.3	13.0	14.5	15.5	16.0

Source: J.P. Morgan Asset Management

<https://www.investors.com/etfs-and-funds/retirement/you-need-this-much-retirement-savings-at-your-age-and-income/>

Annexure 2: Buying or selling a house

Annoying things estate agents tend to do

1. They don't generally really care about transaction price, as long as the deal gets done and some commission gets generated.
2. They are usually in a rush (for their fee, and so as to not risk losing the deal or mandate)
3. They always seem to apply both price pressure and time pressure (to both buyer and seller).
4. They always seem to "talk the market" against the seller (e.g. they talk price "up" to win the mandate, and talk it "down" to set expectations and then push you to accept an offer).
5. They tend to form relationships of loyalty with the buyer, while notionally working for the seller.
6. They seek long exclusivity periods in their sales mandates.
7. They seek to minimise commitments about their sales/marketing efforts.
8. They will sometimes exploit conflicts (e.g. as between husband and wife) to push the deal to closure.
9. They usually try to draft contracts so that their fee is payable by either of the buyer or seller, and without regard to actual settlement of the transaction (possibly forcing the parties to conclude the deal).
10. They always try to earn their commission rate on the entire transaction value (e.g. they get 5% of any amount, even if that amount is so low it could have been achieved by the seller alone).
11. They often try to impose their own service providers such as bond providers, attorneys, inspection services (e.g. electrical, beetle, plumbing, gas, electric fence inspectors).
12. They try to get buyers' deposits paid into trust accounts under their control/purview.

House offers to purchase: Pitfalls and guidance

1. Ensure you are dealing with a registered estate agent, and that they show you're their estate agents' fidelity fund certificate number (which means they are bound by the Estate Agency Affairs Board code of conduct).
2. Never use the estate agent's standard offer-to-purchase: It's a contract and you must read, negotiate, and amend it!
3. Ensure the house is fully inspected by yourself, and all material defects are cleared-up identified, or warranted. Make particular notes about key issues you identify (e.g. damp, electrical problems, cracks, etc.) and specify their repair.
4. You should always make an offer to purchase subject to an independent review of electrical/beetle/plumbing/gas/security and maybe structural engineering.
5. If you are worried about nearby construction, or maintenance of sunlight/views, you may make a condition that a town planner checks the zoning of the house and area, and any potential construction risks nearby (e.g. a petrol station built next door, or a tall building being erected to block your view).
6. Do not just accept the agents'/sellers' service providers for required inspections (check references and make it a condition of the offer to purchase that you can replace inspection agents).

7. Give yourself the right to nominate which trust account (and which party) holds your deposit (do not just accept the agent's trust account).
8. Ensure the house must be delivered to the buyer vacant: You do not want the hassle of evicting a tenant.
9. Keep the deposit offered to the seller as low as possible (e.g. 5% or even less, and in no event more than 10%). Remember, your down payment on the bond may be much more, but you don't have to put that as deposit. The potential loss of your deposit is the single biggest force which impedes you from withdrawing from the transaction if you find something you didn't expect (or wasn't disclosed).
10. Ensure the agent's commission is only due and payable when the house transfer is finalised (otherwise the agent can potentially keep their commission even if the deal fails -- and can legally claim their fee from your deposit)!
11. Ensure your offer conditions are noted (e.g. offer subject to mortgage bond approval, sale of existing house, independent inspections, structural inspections, town planner's opinion, etc.).
12. Ensure you get originals of the Certificates of Compliance (gas, beetle, electric fence, electrical, water, alien-invasive species etc.).
13. Leave plenty of time to make your deposit (e.g. don't get into a jam to make a deposit of money you don't have on hand).
14. Try to appoint your own conveyancer and NEGOTIATE the conveyancing price. Or, as a condition put in that you get to negotiate the price with a conveyancer appointed, and have the right to ask for a different one. (Note: In SA the seller appoints the conveyancer, but the buyer pays the conveyancing fee: An inherent conflict!)
15. Conveyancers' fees are always negotiable, from 20% to 50% off the "scheduled" prices (depending on the size/price of the property). The work is the same for a cheap or expensive house, so it does not have to be a fixed scale (while transfer duties do rise with property value).
16. Set a low occupational rent in case you end up paying it for a while. Ideally have an occupation date and no occupational rent.
17. Be cautious of any clauses against you that include penalties, interest, etc. (delete them).
18. Once your offer has been accepted, the seller should not be allowed to accept other offers (even at a higher price).
19. Identify all ancillary items you want to include in the price, such as appliances, curtains, pool cleaners, sets of keys, combinations to safes, etc. Also be sure it is clear what is not included in the sales price.

Annexure 3: The Index Card (as referred to on cover page)

This financial summary was inspired by Harold Pollack's "*Index Card: 9 Easy Rules for Personal Finance – Everything you need to know about money*" based on the idea that all the key elements of financial planning could be fit on an index card!

<https://www.forbes.com/sites/zackfriedman/2017/03/09/9-money-rules-index-card/>

https://www.washingtonpost.com/news/wonk/wp/2013/09/16/this-4x6-index-card-has-all-the-financial-advice-youll-ever-need/?utm_term=.4473da94a05c

Andrew's Index Card: Guidelines to Your Financial Life

- *Retain some cash (2-3 months' salary) for emergencies.*
- *Separate your investment capital from your life expenses, and keep it safe and out of reach.*
- *Start a savings habit, putting aside 5-10% of your monthly income.*
- *Pay off debt, and only borrow money for return-producing assets.*
- *Buy the necessary insurance cover for health, life, car, and house.*
- *Invest in your and your family's education.*
- *Enrol in a retirement plan (or a retirement annuity account) and start contributing capital.*
- *Buy a house, but treat it as an investment decision based on rationality and not emotion.*
- *Always pay close attention to all investment costs and fees.*
- *If you have a financial advisor, require full transparency of fees and the disclosure of any conflicts.*
- *Open a unit trust account so you can access a money market fund, balanced funds and riskier equity funds.*
- *Open a stock brokerage account if you want to buy individual shares or exchange traded funds.*
- *Set aside a small portion of your wealth (e.g. 5%) for high-risk/high-return investments.*
- *If it seems too good to be true, then it is: Avoid scams.*
- *Gambling is not investing.*
- *Don't make loans to family or friends.*
- *If you get married, sign an ante-nuptial contract.*
- *Write a will and a living will.*
- *Express your own values in your choice of investments and financial service providers.*
- *Give back to society.*
- *Form loving bonds with family and friends.*

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