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QUARTERLY INSIGHT

InterPrac Financial Planning Newsletter Edition 1 2019

New year, new start

Summer has come to an end and those days by the beach may be feeling like a distant memory as the year really kicks into gear.

Our first edition for the year has a range of articles to inform, inspire and set you up for a successful and prosperous 2019.

We're covering everything from budgeting tips to deal with cost of living increases, to the need to consider your medium-term goals and even investment psychology – specifically how to avoid the pack mentality in your approach to investing. With Valentine's day just behind us, we also take a look at love, money and the importance of communication, before finishing on an important lesson outlining how to teach your kids about finances.

2019 also promises to be a big year on the national and global stage, with concerns about property prices and the upcoming Federal Election cause for much conversation.

With all that said, now is the perfect time to book in for a review. We can help you put your goals in focus and create a financial strategy that takes into account both external factors and your personal situation.

We hope you're enjoying the new year. Enjoy the read.

Family finances - the tick of approval?

Keep your household finances in the positive and reap the rewards.

As the prices of petrol, groceries, school fees, electricity and water all creep upward, families are under increasing pressure just to make ends meet.

So how can families cover the cost of everyday living and still manage to put some savings aside? One way they can get ahead is by treating their family finances like a business with assets, liabilities and cash flow as key indicators of financial health.

Budgeting is a crucial component of financial health. Many people have had a half-hearted attempt at budgeting or have started out with good intentions but then have given up. If this sounds like you, you're certainly not alone. The fact is most Australians do not demonstrate sound behaviour with money. Australia has one of the highest rates of credit card debt in the world. Too many of us are borrowing to live day-to-day.

It takes determination and commitment to maintain a budget and avoid the consumer trap. The purchase of a new flat screen TV, a new lounge, a new car or another pair of shoes may seem essential but people who are financially successful don't buy things until they can prove to themselves they can afford it. Their philosophy is "don't spend more than you earn".

Variations in income and/or expenses are inevitable but they are often enough to dissuade people from having a serious go at budgeting effectively. It can all seem too hard.

So what steps can you take to maintain a budget that's workable:

- Knowing what your family earns in a given month should dictate what discretionary income can be spent in the subsequent month. Ideally expenditure should lag earnings.
- Start saving - no matter how small the amount, having a regular savings program or having money automatically deducted from your account can make a real difference.

Just saving $35 a week ($5 per day) will grow to more than $5,700 after 3 years (assuming an interest rate of around 3%). If you could save $100 a week, you would have more than $16,000 after 3 years.

- Have achievable goals - Think of something you'd really like to change in your life and work as a team with your family to make it happen. It may be a weekend away, a holiday or a new piece of furniture but help the goal come to life by making it something specific. You may even decide to reward yourselves when you achieve particular milestones. It might be a dinner out when you reach a particular target. Just don't be tempted to reward yourselves before you've done the hard work!
- Schedule a regular household meeting. Successful businesses have regular team meetings to track their progress. This is no less important in the home. Have a regular conversation (ideally weekly) with your husband/wife/ partners and children to look at what money has come in and what money has gone out so far for the month. You could call it something like your 'money in, money out meeting'.

There are some things in life that we have little control over so it's liberating to make a conscious decision to change the things you can for the better. Today could be the beginning of a new financial life for you and your family! Or if you want to rely on luck - buy a Tattslotto ticket.

We think the best strategy is to take control. We'd give that the tick of approval!

Using technology to keep your finances in great shape

Monitoring fitness levels with a smart phone or tablet is the latest way to keep the body in good nick thanks to the availability of downloadable applications, known as apps. But there is also a growing number of apps to keep your personal finances in good shape.

While online banking has given bank customers the ability to check their balance and monitor ingoings and outgoings easily, today's finance apps go much further than this.

Some can aggregate information about when bills are on the way and flag how much money needs to stay in your account to ensure sufficient funds for payment on due dates. Others may help you keep a tighter rein on impulse spending.

One locally-developed app, Pocketbook, reveals if you have enough funds for an impulse purchase while leaving enough in the kitty for regular bills, simply by checking your smart phone.

The personal finance hub at the Australian Securities and Investment Commission, Moneysmart.gov.au,

is also backing the trend. It has developed two simple but smart apps to help guide budgeting, TrackMyGOALS and TrackMySPEND.

Access permitted

A good place to start the search for financial fitness tools is your bank. The large banks all offer free apps linked to customer accounts. Some offer budgeting while all have money management functions such as transferring between accounts and paying non-bank bills.

Some non-bank apps will also hook up with your bank information and produce graphics that display spending and saving. Some require a lot of data input and others are virtually effortless to use. Many are free but even the ones that need to be bought cost less than $5.

Although the choice of apps in Australia that link with our banks is not huge, one that stands out for its connectivity is Pocketbook. The free version has limited functions but if you pay for the product it offers a variety of budgeting tools, including weekly income and expense summaries.

Whether you go for a standard app that allows bills to be paid from your financial institution or a fancy one from a software company, it pays to be aware of privacy issues.

Downloading an app involves agreeing to conditions that can include giving providers access to the private information on your electronic device and permission for them share it with a third party.

Keep it secure

Often people prefer to stick to their banks' products knowing they already have a secure relationship with a low risk of identity theft.

Greater security is also likely if the information you exchange with your app is done on a smart phone or tablet rather than on a PC. These devices are operated by systems designed to reduce the risk of online crime in a way that PCs with hard drives struggle to.

Even bank web browsers are more open to hacking on a PC than on a phone, unless you opt for extra protection from reputable software such as Kaspersky.[i]

If you prefer to manage your money on a smart device, it is vital to secure it and the app with a pin or password. Apps such as BillGuard, which scrutinises credit card statements for suspicious charges, won't work if a code is not applied.

Just like the multitude of health apps that help shed kilos or bulk up muscle, there are also apps designed to make your debt leaner or pump up wealth by tracking your investments.

The fast-growing list of tools to keep you financially fit will leave you breathless. But the pain of finding the right budgeting app could lead to big wealth gains in the long run.

i http://support.kaspersky.com/8056

Keep your eye on your medium term goals

If you are putting money away for retirement and next year's holiday, well done. But spare a thought for things you want to achieve a few years from now.

When it comes to setting financial priorities, medium-term goals often suffer from middle child syndrome, not taken as seriously as the oldest or indulged as much as the youngest.

The serious long-term goal of saving for retirement gets lots of attention, and rightly so. It's super important. And next year's trip to Bali will be so much fun, even if it does drain all your savings.

It's little wonder there never seems to be enough money left over to save for those in-between things you hope achieve in the not-too-distant future. Things such as your children's education, a home deposit, renovations or a new car.

Yet those medium-term goals – for spending approximately three to 10 years away - are just as important to the life you want to create for yourself and your family. So how can you make sure you've got them covered?

Getting started

The first step is to find time to think about your medium-term goals. Write them down with an estimate of what each will cost, your time frame and how much you need to save each month to achieve them. The more specific you can be the better.

These goals will differ depending on where you are in life, but whether you are 25 and saving a home deposit or 55 and wanting to buy a boat, you need a plan. Otherwise you might be tempted to use high interest loans and credit cards or simply borrow more than you can afford.

Next comes the reality check. To work out whether your medium-term goals are achievable, you need take stock of your current financial situation. Tally your income and expenditure to calculate how much you can afford to save and invest each month. There are plenty of free apps and online calculators that will help you do this.

Also look at what you owe. If you have any high interest debt, such as an outstanding credit card balance, you might consider paying this off first as the interest rate is likely to be higher than the return you could earn on your savings.

Weighing risk and reward

Setting an investment time frame is important because it has a bearing on how much risk you can afford to take. That's because the longer your investment horizon the more time to ride out short-term market fluctuations.

Say you are saving for a holiday next year. You can't afford to risk losing money in a sharemarket correction, so you park your savings in the bank. The interest rate may be low, but your capital is guaranteed.

With medium-term goals you can afford to take a little more risk for a higher rate of return. For example, over the five years to June 2018, Australian shares returned 10.3 per cent a year on average, listed property 12 per cent and Australian bonds 4.4 per cent. Over the same period cash returned 2.2 per cent a year, barely above inflation of 1.9 per cent.

Of course, the exact return you earn on your investments will change from year to year but historically shares and property do better over the medium to long term than cash or bonds.

Even so, the last thing you want is for your investment to fall 10 per cent just before you need to spend the money. The way to avoid this is to spread your savings across a range of investments and asset classes, reducing the risk of a large or untimely loss in any one of them.

Finding a home for your savings

Unlike long-term savings which are locked away in superannuation until you retire, you want your medium-term savings to be accessible. And unlike a bank savings account, you want an investment that will grow in value.

Two alternatives you may wish to consider include managed funds and ETFs (exchange-traded funds). These options allow you to diversify your investments across the full range of asset classes and can be bought and sold whenever you want.

Some managed funds allow you to get started with a small initial investment and then make regular weekly or monthly contributions. Depending on how comfortable you are with risk, you could choose a 'balanced' fund with up to 70 per cent invested in shares and property and the rest in fixed interest and cash, a high growth fund with a larger allocation to shares and property, or a conservative fund weighted towards bonds and cash.

Another approach might be to set up a direct debit from your pay into a dedicated savings account and every time your balance reaches, say, $5000 invest in an ETF. Some of the new investment apps allow you to make regular contributions into ETFs tailored to your risk profile, from your smartphone.

If you would like us to help create an investment plan that includes all your important life goals, the long, the short and everything in between, give us a call.

CASE STUDY

A 5-year home run

Tom and Jess, both 26, want to save a deposit of $80,000 to buy their first home in five years' time. They already have $10,000 in a joint savings account and decide to invest this in a managed fund.

They are comfortable with a relatively high level of risk without being too aggressive. So they select a diversified fund with 70 per cent in shares and property and the remainder in fixed interest and cash, with expectations of earning an average return of 6-7 per cent a year.

After drawing up a budget, they are confident they can afford to contribute an additional $220 a week ($110 each) into the fund which would see them reach their target.

Investing and avoiding the 'pack mentality'

We're all familiar with the stories of legendary investors. They're the men and women who make their fortunes by decisions that are often complex, sometimes contrarian, but always able to be explained in hindsight. They make and preserve their wealth in good times and in bad. And it's not simply because they had a lot of capital to start with.

Many of us yearn to have the cold, hard robotic logic of the world's most successful investors. Unfortunately, we ordinary folk are governed by something a bit more basic. Something that even those stock market legends had to struggle through at the very start.

How does psychology influence the way we invest our money?

Investor psychology is a subset of behavioural psychology. It overlaps with fields such as behavioural finance and behavioural economics. As the name suggests, it focuses on the observable behaviour of investors. Many academics relate investment decision making to other decisions with the same characteristics. Important decisions that are driven by deep-seated emotions such as fear and greed.

In other words, irrational decisions.

These choices aren't made by analysing the numbers, but by looking at what everyone else is doing, and being driven by the prospect of loss (or reward). Several quantitative analyses suggest that about 90% of investors sell within 10% of the bottom of a market cycle. The same proportion buys within 10% of a peak. This is a pattern of group behaviour known as escalation of commitment. You've probably heard of the 'sunk cost fallacy' – that's a big part of it.

This type of group behaviour can push up the market value of stocks to extreme levels very quickly – a.k.a. a bubble. People want to get in on (what they perceive as) a good thing "before it's too late". And it can cause a crash when people see the first price dips and try to get out before they lose it all. Think of the Chinese stock market bubble and the dot comm bubble in the late 90's.

The good news is, there are ways to avoid being swept along with the herd. It's all about self-awareness. That includes knowing when you're out of your depth and need to seek advice.

CONSIDER THE FOLLOWING

- Before you buy in to a 'hot' opportunity, ask yourself whether confirmation bias could be making it more attractive. Just because similar investments have done very well, doesn't mean this one will. See, for example, the wildly popular IPOs for certain tech stocks.
- Before you sell just to 'get out quick', consider the alternatives. Is this stock likely to recover? If so, how long will it take? What is the opportunity cost of sticking in there for the long(er) term?
- Consider contrarian opinions. Alternatively, be your own devil's advocate. Don't make a major decision without giving yourself time to gather and consider a well-rounded set of data interpretations.

- Before deciding what to do with an individual stock, take a holistic view of your portfolio. How will buying (or selling) this one stock affect the rest of your portfolio? Is it, in context, a good fit for your needs?

- Look at long term data to get a better idea of whether a share price dip is the beginning of the end, or just a temporary correction.

- Overcome your fear of doing something different investment-wise by tapping in to our expertise. If you don't know the first thing about technical analysis, we're happy to help. Set an appointment or contact us and we'll get you started.

Love and money - maintaining financial harmony

As a wise man once said, "I don't know what they want from me. It's like the more money we come across, the more problems we see."[i]

If this rings true for you, chances are your most important relationships are marred by conflicts about money. It's not something you want to deal with at any stage of life. When you've worked hard to build your wealth, you want it to engender comfort and security – not tension and fighting.

From divorce to the deathbed, cash is first on the agenda

It's a common theme in any divorce story. Aggrieved former spouses make dramatic statements about "taking them for all they've got" or "making them pay". Couples on the verge of a split often 'lawyer up' and call their accountant before they contact a counsellor, psychologist or emotional confidante.

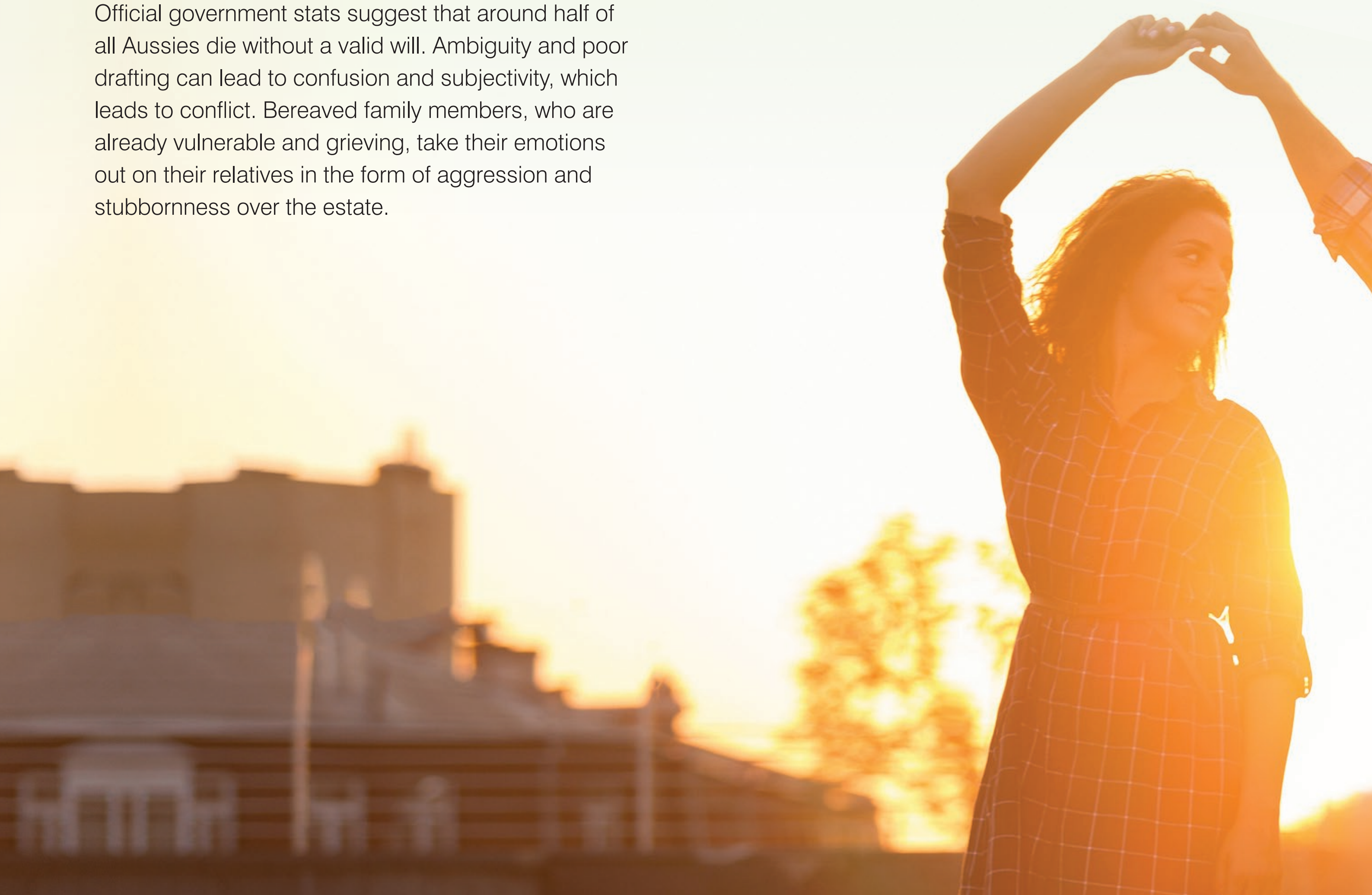
The same goes for when a loved one passes away. Official government stats suggest that around half of all Aussies die without a valid will. Ambiguity and poor drafting can lead to confusion and subjectivity, which leads to conflict. Bereaved family members, who are already vulnerable and grieving, take their emotions out on their relatives in the form of aggression and stubbornness over the estate.

Dirty little financial secrets

According to a survey by American Express, 40% of women and 33% of men have hidden purchases from their partners.

Closer to home, back in December last year an ME Bank survey[ii] found similar results. Around 6% of Aussies keep a bank account or loan secret from their partner. And high earners are the worst offenders – nearly a quarter of all those earning over $200,000 a year have a secret savings account.

If you're tired of debates and secret-keeping, you're not alone. But you don't have to keep rehashing the same old arguments.



HERE'S HOW

1. Take a few deep breaths before you react.

If something traumatic has happened, chances are you won't be in a great frame of mind to make an important financial decision. Give yourself a bit of breathing space after an accident, argument, or death in the family. And make sure everyone else involved agrees to do the same.

2. Understand your money management personality.

Are you a spender or a saver? It's important to understand your own attitude towards money, and how that affects your discussions and behaviour towards others. For example, if you're worried about a family member's seemingly frivolous spending habits, be conscious of your own biases.

3. Ensure you have a valid will.

Unfortunately, many free templates and will kits aren't enforceable under Australian law. For your peace of mind, and your family's future, we can collaborate with your solicitor to help you make sure you've got all the assets in your estate covered and accounted for.

4. Use both names – on your assets and your debts

Putting savings accounts, investment portfolios and other assets in both names can be more conducive to cooperating on the management of those assets. Nobody gets to say "I'm the boss of that" or "that's not my problem".

Putting both your names on utility bills and mortgages means you're mutually obligated to cooperate on working out how to meet your responsibilities.

When it comes to wider family wealth, such as a family business, make sure the asset is structured so that responsibilities (and benefits) are clear. For example, make sure you formalise the way profits from that family business are distributed between family members.

5. Make a budget – and stick to it

Making a household budget, and personal budgets, is a task that too many people skip. Not having a written, agreed-upon budget can mean that people whose finances are tied together are not on the same page about how money is being spent. And that's a recipe for conflict.

If you would like to discuss any of the points raised in this article, or any other issues related to conflicts over money, please contact us.

i That 'wise man' was infamous '90s rapper Biggie Smalls. The words come from his Billboard No. 1 song, 'Mo' Money, Mo' Problems'.

ii https://www.mebank.com.au/media/1591228/-infographic-for-money-and-relationship-research.pdf

Money lessons for kids

What do Bill Gates, Warren Buffet, Sting and Nigella Lawson have in common apart from wealth? This mismatched bunch is part of a vanguard of rich parents who have vowed not to leave multi-million-dollar legacies to their children.

While some wealthy parents may believe their progeny are not equipped to handle wealth wisely, others simply want their kids to learn how to strive to get ahead just as they did.

In many families, children have become used to seeing their parents spend effortlessly. Instead of paying for purchases with hard-earned cash, transactions happen invisibly via a credit card.

The unintended consequence, regardless of a family's financial position, can be the creation of a generation with little concept of saving before spending.

Pennywise parenting

A recent Galaxy Research survey on attitudes to teaching money smarts to children revealed a gap between the generations on some issues, but broad agreement on others.[i]

The youngest group, Generation Y, was most likely to agree with the statement that kids should be allowed to enjoy their childhood and that financial literacy will come with time.

There was broad agreement though that kids learn by example and that they should be encouraged to get a part-time job outside the home when they are old enough.

The government and banks are also doing their bit to encourage financial literacy among small fry. Financial watchdog Australian Securities and Investments Commission (ASIC) says teaching children how to budget and save will provide them with the skills needed in a world where managing money is more complicated than ever, due to the advent of easy credit and online shopping.

Appy saving

In addition to offering savings accounts tailored to children, many financial institutions publish tips on their websites designed to help adults teach kids about money.

There are even mobile phone apps that can train children to understand the value of money. One of them, iTunes' Pay Pig, allows chores to be listed, priced, ticked off when complete and it even prompts parents to make an electronic transfer into their kids' accounts when a task is done.

Among the tips ASIC provides is explaining to children when out shopping how items are priced (see box).

When utility bills arrive, this is an opportunity to explain that services such as electricity, gas, mobile phone plans and the internet cost money and that if these accounts are not paid, the services they take for granted could be disconnected.

Talking about budgets and planning for future expenses can teach children about the costs of everyday family life and how important it is to put money aside for regular bills.

Lessons for life

Once they leave school, make sure they comprehend the HECS system which allows them to "borrow" from the government to complete their studies then repay the loan from their future salary with adjustments for inflation.

Training children in good money habits is one of the most responsible gifts a parent can give their offspring. Not only will it keep them off the debt treadmill in adulthood but it will give them the necessary tools to create their own financial destiny.

TEACH YOUR CHILDREN:

- How to seek out value for money to avoid impulse buying
- That an item "on sale" is not a bargain if they don't need it
- How to keep track of mobile phone usage costs
- To value the concept of earning before spending by giving them pocket money
- If a deal sounds too good to be true, it could be a scam
- The difference between credit and debit accounts
- To identify their spending "needs" as opposed to their "wants"
- By modelling good spending and saving behaviour

Source: www.moneysmart.gov.au

i Hands-on best for teaching kids money smarts, TAL Life Ltd press release: December 9,2014. http://www.adviservoice.com.au/2014/12/hands-best-teaching-kids-money-smarts/

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