Money Made Simple

Managing your money – a guide for all New Zealanders

Sam Stubbs

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potton & burton
Simplicity

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Why this book?

Money is really important, because it gives choices in life. And a life with choices is a life with dignity.

But when you don't have enough money, you have far fewer choices about where you live, what you eat, what you wear, what holidays you have, and what your children can do.

So how do we get more money? Sometimes it's really difficult, especially if you're unemployed, on a benefit or just simply living week to week and barely getting by.

But whatever circumstances you're in, learning about money can help, because knowledge is power.

I come from Sunnyvale, in West Auckland. When I grew up, we were surrounded by what we would now call the working poor. Most of the parents had jobs, but were left with very little money to spare at the end of the week.

Because we were all in the same boat, I'm not sure that the kids felt poor. But most of the parents were struggling most of the time.

Many people on our street were renting too. They had no savings, and relied on government superannuation for their retirement. Financially, life was tough. And it was very hard when things went wrong. Unemployment rates were high back then, and losing a job was, naturally, devastating for the whole family.

My parents were school teachers and instilled in me a curiosity and a strong work ethic. There were other careers I could have

had, but I fell into the finance industry for what were, in hindsight, all the wrong reasons.

Like a moth to a flame, I was attracted to the money and glamour of this industry. For a kid from West Auckland, who had delivered newspapers first thing in the morning and stacked supermarket shelves at night, the thought of working in a shiny office tower, and a company credit card, was very seductive.

I've now spent a lifetime working for banks, investment banks, stockbrokers, finance companies and fund managers, all around the world. My career has been all about money.

I began with Fay Richwhite, an investment bank that, at the time, was arguably the most important finance firm in New Zealand. Among many high-profile transactions, they bought and sold the Bank of New Zealand and most of the railways.

Then I became a stockbroker and moved to Goldman Sachs, in London. But after four

high-flying years in that world, my conscience started kicking in. Were my efforts good for the many, or just for the few? Was I looking after my whānau in Sunnyvale, or just making the rich richer?

However, it still took a while to find what I really wanted to do. In between, I moved to Hong Kong, helping the best and brightest traders in financial markets set up successful hedge funds. Then I came back home to Auckland where I eventually became CEO of Tower Investments, a KiwiSaver default provider.

By now, having seen the finance industry operate globally, I was dissatisfied with the way it failed to help everyday people just trying to get by. It usually just sold them expensive and complicated products. I saw the industry as being about serving itself, by paying big salaries and bonuses rather than giving ordinary Kiwis the choices and sense of dignity that money can bring.

The kid from Sunnyvale wanted to do his bit and make a difference. So, with the help of my partner and some wonderful people, we got started. In 2016 we set up Simplicity, a nonprofit fund manager, owned by the Simplicity Foundation. We manage KiwiSaver and investment funds for many thousands of Kiwis, charge low fees, and give away 15 % of all fees to charity, which is already well over a million dollars every year.

Managing Simplicity is simply the best job I've ever had. I work with a group of amazing people, who all want to make a difference. I really love what I do.

And to me, it's simple – every New Zealander should have the power to improve their financial well-being. And to do that, knowing about money really matters, because knowledge is power.

I've been wanting to write down the simple truths of money for a while, because money

is actually pretty easy to understand and master. I wanted a book that filled the gap between short explainers on the internet and the more detailed books out there.

You can read this in one sitting, and, hopefully, get the basics of money sorted for life. It's for anyone trying to get ahead financially in life and navigate the financial world. It doesn't have all the answers, but there should be something for everyone.

This book was the idea of publisher Robbie Burton, from Potton & Burton. Its production has been paid for by Simplicity NZ Ltd, and will be used as part of our ongoing mission to educate New Zealanders about money. I've been paid nothing for writing it, and any profits from its sale will go to the Simplicity Foundation, which is focused on charities supporting children at risk, addressing poverty, protecting the environment and improving financial capability.

PART ONE

Three simple truths about money

SIMPLE TRUTH 1
We should talk about money

Many Kiwis don't like to talk about money. It might be because they think they don't know enough about it. And it might be a hangover from previous generations, who were told that discussing money wasn't polite.

Kiwis freely give advice on parenting, because they know this advice is important for the future well-being of children. But they are less inclined to pass on wisdom they have about money, even though it would help everyone's financial well-being.

In other countries, people are more open about how money impacts their daily lives – in the United States, I've heard people openly comparing how much they earn in a supermarket queue!

But money isn't discussed enough in New Zealand, not within families, and certainly not among friends and extended whānau. And yet, passing on some simple truths would really help a lot of people.

The sad reality is that ignorance about money can drive people into the arms of payday lenders, loan sharks and parts of the finance industry that are more interested in making money from you than for you.

Some of this is changing, however. Children are learning more about money at school and can easily access information and have the ability to invest in shares online. There are some wonderful education programmes available in schools now, and over 260,000

under-18s now have KiwiSaver accounts.

Adults, too, can learn the simple truths about money these days, including by reading this book. And by knowing the basics, and talking about them, you can have more money. It all starts with knowledge.

Money is actually easy to understand and master. It's like anything - putting in a bit of effort gets the results. And you don't have to have a lot to start thinking about it. As with any good habit, the sooner you start and the simpler it is, the better.

The media is quick to provide stories about people who have failed by frittering money away, losing it or having it stolen. I think that scares people into thinking it's all too hard. But it's not. There are many people who have mastered the basics, have enough money, and get on with enjoying life.

How to talk about money

Discussing money differs according to the audience.

With children, it can be in the form of games, or through everyday conversation. When I was young, I learnt all about the property market by playing Monopoly. It taught me the importance of the right location, getting on the property ladder, managing cashflow, mortgages, mortgagee sales, rents – and simply the randomness of life. You even go in and out of jail!

And today there are lots of other fun ways to educate kids. They can use 'money boxes' online, have their own KiwiSaver and bank accounts, and get easy access to online investing platforms. There are plenty of free resources online too, and good programmes at schools.

Even though they weren't financial 'experts', my parents talked to me, or in front of me,

about money. They didn't hide the reality when times were tough and things were tight. I grew up around everyday conversations about property prices, mortgage rates, deposit rates, and the general state of the economy. They made talking about money a natural, regular occurrence.

Kids are amazing at absorbing information, so talking about money matters when they're around is a great start for them. It makes talking and thinking about money a usual topic of conversation, and practice makes perfect.

The thing is, we all have a lot to offer in terms of these discussions. If you are working, paying bills, have bank accounts and credit or debit cards, buying insurance, buying groceries, running a car and dealing with all the many daily costs associated with living, you actually already know a lot about money. And talking about these things teaches your kids a lot about money. Discussing your experiences

with money as part of your everyday life demystifies it for children, so they can master it and not fear it.

For older kids, pocket money and chores are part of their education about money. Mowing the lawns and washing cars, for example, can teach them that doing work can earn money, which can then be saved. My first paid job was stripping wires at a vending-machine factory. Time has never moved so slowly, and the 99c an hour I earned has never been so carefully spent! We never forget those first jobs.

It's good to encourage kids to get out and get work. It can be doing odd jobs for others or babysitting around the neighbourhood when they are older. It is all good experience and helps set them up for more jobs and earning opportunities. And you can then discuss with them where, and how, to save the money they earn.

Having your child set up a KiwiSaver account, where they can look up the balance and see what is invested, is all part of learning about money. Online investing platforms enable kids to invest their pocket money and watch what happens to it. It teaches them that financial markets go up and down, and, again, it demystifies money.

With adults, habits are hard to change later in life. But within your own family, it's never too late to begin the discussions and build that trust, so that everyone benefits. If you understand the simple truths of money and pass these on to others, everybody wins. It's one of the best things you can do.

SIMPLE TRUTH 2
It's how we think about money that matters

How we think about our money shapes how much we'll have, and how happy we'll be with it.

Many people think about their money only in terms of what they have to spend right now; that is, from one payday to the next. But doing this can make you feel less well-off than you really are and can lead to stress and anxiety.

A better way to think about your money is your **net worth**; what you would have left if you sold everything and paid off all your debts.

For many people that is more than they have in cash on hand.

If you make financial decisions based on your net worth, you'll be on the way to becoming richer. You'll start thinking about money in terms of increasing your net worth, not maximising your cash right now.

> **How to calculate your net worth: A really good tool for this is on the government-run 'Sorted' website.**

However, remember that your car or any 'toy' you might own (like a boat, bike or snowboard) should **not** be included when working out your net worth. Why? Because they don't hold their value, they depreciate. They might mean a lot to you and provide heaps of fun, but they usually become worth less and less over time and are hard to sell in a hurry. They are fun things, but not financial assets.

Once you know your net worth, you can start making better decisions with your money. This is because you may be better off than you think. And if this is the case, you won't have to worry so much about money. Reducing that source of stress makes life better.

Here's an example. You're living payday to payday, with nothing left over after you've paid the rent or mortgage. But perhaps you have money in KiwiSaver, or perhaps you've already paid off some of your mortgage. That means you have **assets**, and that means you have **choices.** And this makes you feel better about yourself. Then you can increase your net worth by saving a little more into KiwiSaver or paying more off the mortgage.

If all you're doing is focusing on how much you have to spend each week, it means you're ignoring important long-term decisions, like how to buy a house or save for retirement. But thinking in terms of your net worth can

lead to some good decisions about saving or paying off debt. And it will usually make you feel happier about money, because your net worth is usually a larger amount than you have in the bank.

And thanks to compounding returns, money turns into more money. More on that later.

A good example is home ownership. For those who have been able to buy a home, some think they don't own it until the mortgage is totally paid off. They think the bank owns the house.

This isn't true. Even though you buy a house with a mortgage, it's legally yours. The bank doesn't own it, it's just lent you money to buy it. You are the legal owner of your home.

Why is this important? Because if you own your home, you have an asset that can increase your net worth. And paying off your mortgage faster is a great way to increase your net worth. Having a higher net worth

changes how you think about money and gives you more choices in life.

The real benefit in working out your net worth, and thinking about your money in this way, is it can remove the stress of feeling poor. It shapes the way you act. Most people feel and act richer and happier when they do so. Thinking more about your net worth and less about your income means you're on the way to having more money.

> **A secret tip: Many rich people are asset rich, but cash poor. They keep just enough cash in the bank to fund their lifestyle (and have a rainy-day fund) but they have most of their net worth in assets, such as KiwiSaver, investment funds, property and shares, that earn income or increase in value. We can all do this by increasing our KiwiSaver contributions, even a little.**

SIMPLE TRUTH 3
Understanding compounding returns really matters

If there is one thing you should take from this book, it's understanding the power of compounding returns and compounding interest. You'll have a powerful ally in helping you reach financial freedom.

Albert Einstein supposedly called compounding returns 'the eighth wonder of the world'. Why? Because compounding returns is the money you make on an investment over time. It compounds up because the interest earned in one year can earn you a little more

the next year, and the next year, and so on. The amazing thing is that the increase over time becomes exponential, and your investment can become significantly larger.

Former US president Benjamin Franklin explained it best when he said: 'Money makes money. And the money that money makes, makes money.'

It works with other investments, too. Your home can increase in value because of compounding returns. Here's how.

Let's say a (crazy cheap) house is worth $100,000 dollars, and its value goes up 10% each year. You make $10,000 in the first year, so the house is now worth $110,000.

Next year it goes up another 10%, so you make another $11,000.

$110,000, plus an $11,000 gain means the house is now worth $121,000.

Next year, it goes up another 10%, so you make another gain of $12,100. $121,000

plus $12,100 means the house is now worth $133,100.

The house has gone from being worth $100,000 to $133,000 in just three years. That's a one-third increase in its value!

And even if the price rises are lower than that each year, the compounding effect of the rises is a powerful friend in increasing your net worth.

How to get compound returns working for your family

Here's another way compounding returns can work for you, from day one.

There are 23,741 days from the day we're born till the day we receive superannuation at age 65. So, if your parents saved $1 a day into a KiwiSaver account for you, from the day you were born until you turned 65, they would have put aside exactly $23,741 (the light area on the graph, over the page).

And let's assume you got a 4.5% return every year on the money you saved, which is about what the average growth KiwiSaver fund should earn over time.[1] Using the Sorted website calculator, that means your $1 a day saved will grow to over $136,000 by age 65.

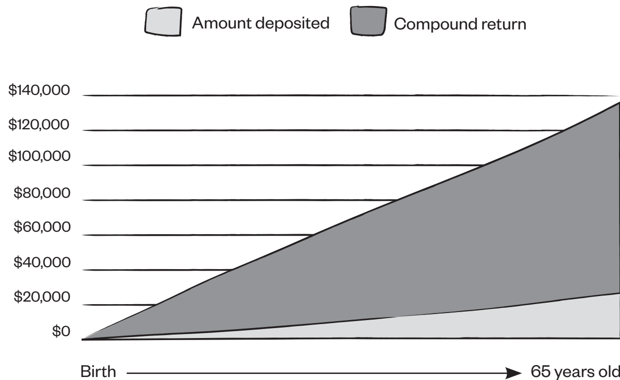
The dark-grey area on the graph is the extra money you would have because of compounding returns – in this case over $112,500.

That's right, you'd pay in $23,741, and have another $112,500 because of compounding returns. See why compounding returns were called the eighth wonder of the world?

How come it's that good? Because you get a 4.5% return **every year, on every dollar, including the returns you earned the year before.** Remember what Benjamin Franklin said – 'The money that money makes, makes money'. Compounding returns work **for** you when you're saving.

1. www.fma.govt.nz/investors/resources/kiwisaver-projections. Returns are net of tax and fees.

COMPOUNDING RETURNS EXPLAINED



This graph shows the remarkable power of compounding returns. The light area represents $1 a day invested at birth until age 65, a total of $23,741. The dark area shows how compounding returns grow this investment by over $112,500 during this period, to a total of over $136,000.

The graph assumes 4.5% average return. Returns have not been adjusted for inflation.

Please note – performance of KiwiSaver, investment funds and shares may fluctuate.

But beware, compounding works **against** you when you're borrowing money, because you have to pay compounding interest. That's because any interest charged on a loan you don't pay, has interest charged on it every year too.

So you get compounding **returns** when you're saving, which increases your net worth. But you pay compounding **interest** when you're borrowing, which decreases it.

> **Those that understand compounding interest, earn it. Those that don't, pay it. — Albert Einstein**

For example, the Sorted website shows that a $500,000 mortgage, charging 4% interest, paid off over 30 years at $550 a week, will end up costing you another $358,778 in interest. That means you will have borrowed $500,000 but paid out a total of $858,778.

And it's even worse with personal and payday loans, which charge much higher interest. For example, the MoneyHub Personal Loan calculator shows a $10,000 cash advance on your credit card, charging 18% interest for 5 years, which you paid off at $254 a month, will end up costing you another $5236 in interest. You get $10,000, but you pay back $15,236.

Personal finance commentator Amanda Morrall calls credit-card companies and payday lenders 'financial vampires'. They prey on the vulnerable when they are having a tough time, offering quick money at very high interest rates. If you, or those you love, are in this position and can get out of these vampire clutches, then do it as soon as possible.

The best way to avoid payday lenders and credit companies is to never need them. And if you have any debt, paying it off as fast as possible is one of the smartest things you

can do with money.

So, get compound interest working for you, not against you.

Compound returns are your *friend*, increasing your wealth in the long-term through[2]

— term deposits
— KiwiSaver
— investment funds
— shares that pay dividends or increase in value

Compound interest is your *enemy*, reducing your wealth through

— credit-card debt
— loans that charge interest, like mortgages, personal, car and payday loans.

2. Please note – performance of KiwiSaver, investment funds and shares may fluctuate.

PART TWO

The eight golden rules of money

Over a lifetime of working in the money game, here are my eight golden rules. Incorporate some of these into your life, and you can go a long way towards being financially secure.

You don't need to do all of them to improve your finances. If you're on a benefit, or have very little left over each week, there are still improvements you can make that will start you on the right track.

GOLDEN RULE 1
Pay off your debts

Debt is like food. Sometimes it's good for you, sometimes it's bad. Debt in the form of a mortgage or a student loan is perfectly ok. But bad debt from such things as credit cards and payday loans, is like junk food, and can be addictive.

Lenders often make it quick and apparently painless to borrow money– it's delivered quickly to make you feel good. Some payday lenders could teach drug dealers a thing or two.

The problem with debt, however, is that interest payments can really add up, fast.

Remember, compounding interest is your **enemy** when you are borrowing money, and only your **friend** when you are saving.

If you didn't repay anything, $10,000 borrowed at 10% adds up to a total of $25,937 after 10 years. That means you would have to repay 2.5 times what you borrowed.

At 18% interest (which is what many credit-card companies charge), it would add up to $52,338 after 10 years and you would have to repay 5.2 times what you borrowed.

In reality, you're unlikely to borrow money without making any repayments, however, this example demonstrates the impact of compounding interest and how it makes any debt very expensive.

How to avoid getting into debt

— Cut up your credit cards

Credit cards were the first form of debt made easy, introduced to a gullible public in the 1970s.

The companies made it so easy to use them that it didn't feel you were actually borrowing money. But unless you pay off your credit card in full, each month, you are borrowing money, and at very expensive interest rates.

You can see just how much you pay in interest at www.interest.co.nz/borrowing/credit-cards

And you can learn about credit cards here at www.moneyhub.co.nz/credit-cards-basics

Personally, I don't have a credit card, just a debit card, which I can use to buy everything I need. This means I can only spend what I have.

There are some people who can manage their credit cards very well, and benefit from the reward programmes some offer. But you need to be very careful, and in most cases the benefits just aren't worth it.

— Only spend what you earn

This sounds easy, but for some people it can be really hard. You should always try to live within your means. There is lots of advice out there on how to do this, and save money too.

It starts with doing a budget – a simple plan to show what money you have or expect to receive, and how you expect to spend it. Here are two places to learn about this: www.sorted.org.nz/guides/planning-and-budgeting/budget-dont-fudge-it and www.moneyhub.co.nz/budget-planner

I also like to find ways of living more frugally while still having more fun. For that I go to a hilariously named website called Mr Money Mustache, www.mrmoneymustache.com

It's full of great ways to save money and change the way you think about having an

affordable life.

There's a dedicated group of followers of this philosophy in New Zealand called the Kiwi Mustachians, and their Facebook page is well worth checking out too.

The power of saving

The opposite of borrowing is saving. If you don't save money in some form, it means one small upset in life can have huge consequences. Some people get into horrible debt traps by not having money saved for when they really need it, and then relying on credit cards or payday loans instead. This is why everyone should have regular savings and a rainy-day fund. More on this later.

And once you've paid off debt and (if you own a home) your mortgage, you can start saving in earnest. How do you do that? I think the best way to save is with small regular amounts,

so you don't really notice the money leaving your bank account or wages. It's like any good habit you want to develop, such as losing weight or going to the gym. It's best to start slowly and painlessly, so it becomes a habit and not a chore.

Here are some simple ways of saving money. You can set up regular transfers into a savings account that you don't see or touch. Try to start with $3 a day, less than the price of a coffee. Every year, without even noticing it, you could have saved $1095, which compounds over time.

Or you could set up a KiwiSaver account and put the $3 a day into this. If you're aged between 18 and 65, the $1095 you saved every year would be topped up by the government every year by just over $500, which is free money. And you can also save for your children via their own KiwiSaver accounts. There is more on the wonders of KiwiSaver later in this book.

GOLDEN RULE 2
Invest in education

Many people don't understand just how much education pays off over their lifetime. Whether it's an apprenticeship, vocational training or a degree that you earn, all can lead to a better job. Education is simply a great investment.

When economists analyse the best investments you can make, they generally come back to education. How many years' study you have, and how well you are paid, are closely linked.

Research in New Zealand shows that a

university degree is worth about $1.3 million extra in lifetime earnings. No matter how big the student loan is, that's a great return! The same is true for almost any training that leads to a job and is certainly the case for trades training.

And it almost doesn't matter what you get educated in. The highest achievers in any occupation tend to be those who are the most studied, trained, practised and educated. And when you master anything, the money arrives. Even occupations that pay most people less, still pay well when you're at the top of your game. The best musicians get paid better; likewise, the best actors and hairdressers.

One of the best things we can do for our communities is to encourage kids to stay at school. The longer, the better. Every year at school is one rung further up the ladder of financial freedom. The numbers speak for themselves.

How much should we borrow to learn?

A student loan is a tough reality for many to face. This is the first generation in New Zealand to have to borrow for their education. Like all debt, it's best to keep the loan as low as possible, without suffering for it. But if you're considering not getting a degree, doing some training or taking on an apprenticeship because you're worried about being in debt, that can be a big mistake.

Remember that student debt generally has no interest placed on it, and you start repaying it only when you are earning over a set amount. Over time, jobs where you have had to borrow more to get educated will have the cost of the student debt factored into what you are paid.

As a rule, the more expensive the education, the better paid the job. Think how much debt a medical student racks up, but how

well they are paid over their lifetime. It's the same for lawyers, engineers, accountants and architects.

So if you think about student debt as an investment in your future with a great return, it puts it into some perspective. Don't worry about borrowing to learn, if that's what you need to do.

GOLDEN RULE 3

Buy a house if you can, and pay it off as fast as possible

New Zealand encourages home ownership. There's no capital gains tax on your main home, no stamp duty, and borrowing for the home you live in is the cheapest borrowing you can get.

And a home is about the only possession you can enjoy while it increases in value over the long term. The same isn't true for cars, boats or clothes, which tend to decrease in value.

The long-term trend in house prices is nearly always going up. In the last decade, the average house has doubled in value. Owning a house is a great way to increase wealth and have a store of value for the future. And it's an asset that you can improve, and add value to yourself.

In New Zealand, buying a house, and paying down the mortgage as fast as you can, is the most reliable way to get financially comfortable. Once you are fortunate enough to buy a home, make sure it's insured, and get life insurance for at least the balance of the mortgage. Then, if the worst happens, your loved ones get the home debt-free. More on insurance later.

Paying off the home loan as fast as you can also ensures you pay less interest so it has as little impact as possible on your net worth.

And perhaps the best thing about owning a house is you get to enjoy it every day, and no

landlord can kick you out. It means your family is safely housed, your kids can go to the same school through the years and keep the same friends, and you and your family can build a life within a neighbourhood and a community. There is a lot of dignity in being able to choose where you live, and living there a long time.

What if I can't afford to buy?

The sad reality in New Zealand is that there is a shortage of housing, and many struggle to afford the house prices. The big hurdle is getting a big enough deposit. That's why getting into KiwiSaver early really helps. One of the best things you can do as a parent or grandparent is to sign up children into KiwiSaver as soon as possible.

But even then, buying a home is not always possible. So here are some other ways to get on the property ladder:

— Shared equity
Can you buy a home with other friends or family? This is becoming more common, and it gets you on the property ladder earlier. You need to be very careful with whom you buy, and even if you know them well, make sure the contract you have is watertight, including what happens if one of you wants to sell. You need to get legal advice before agreeing to shared home-ownership, and that includes with your partner.

— Buy a smaller home
It's frustrating when you're not able to get exactly the place you want, but very few people do, at least initially. So think about how small a place you could live in, if that's the difference between buying and renting. You can always expand and extend it further down the track, but at least you're on the property ladder.

There is also a growing market in tiny

houses, as well as moveable homes. There are some surprisingly good options out there, and some great stories of couples and families who have chosen this path.

— Live further away

Can you afford to move a little out of town? Often housing is more affordable further away from the centre of a town, or in a town rather than the bigger cities. It might not be your first choice, but if you want to be on the property ladder, it's a start.

— Rent forever

In New Zealand the laws have generally favoured landlords, meaning tenancy agreements have typically been short-term, with lots of homes being sold quite frequently in a rising property market. So long-term renting has been seen as less desirable.

However, this is changing, with stronger

tenant protection coming into place, and tenants having more and more long-term rental options.

New Zealand is starting to see what is common in the rest of the developed world, which is more long-term rental properties, owned by pension funds and large asset managers, which will rent high-quality apartments at fair prices. For pension fund managers (e.g. KiwiSaver funds) it's a sensible long-term investment, and for tenants it provides higher quality, more secure rental options.

It is not uncommon in places like Germany, France, the United States and Australia for people to rent the same place their whole life, and it should be able to work here in New Zealand as well.

GOLDEN RULE 4

Get into KiwiSaver

KiwiSaver was started by the government in 2007, as a way for New Zealanders to save for retirement. It was designed to help people save, and it does just that. You can choose the provider and fund you want, or one can be chosen for you as a default member.

It's a trusted place to invest

KiwiSaver, like other retail investment funds, is regulated, so it's well structured and managed with a lot of oversight. Every scheme has

a licenced, independent supervisor (such as Public Trust), which is itself closely monitored. Because the supervisor holds all the investments on your behalf, no fund manager can ever touch them.

The assets your KiwiSaver fund owns will increase and decrease in value as the financial markets move. However, the simple truth is that KiwiSaver is a well-regulated and supervised place for your investments. Since KiwiSaver started, governments are very committed to New Zealanders' ongoing confidence in it.

It's easy and useful

You can access your KiwiSaver savings in times of significant hardship, serious illness and to buy your first home.

And perhaps best of all, saving in KiwiSaver happens directly from your pay. Studies show

that you save more easily when it happens automatically, as opposed to trying to put money aside every time. It's out of sight, out of mind, and it really adds up.

It's voluntary

KiwiSaver is a voluntary scheme, so you don't have to belong if you don't want to. But the advantage is, if you receive a salary and are in KiwiSaver, both you and your employer put money into a fund for your retirement.

The returns

The power of compounding returns means a little saved in KiwiSaver adds up to a lot over time. According to the Sorted KiwiSaver calculator, the average Kiwi on an annual salary of $50,000 and saving the minimum amount each year (3%) in a balanced fund,

from age 18, could end up with savings of over $270,000 by the time they reach retirement. It's a painless way to save, and it could transform your retirement years.

There are lots of websites with answers to KiwiSaver questions. Try www.sorted.org.nz the government-owned website, and www.moneyhub.co.nz.

Mary Holm, a media commentator, writes books with a lot of information about KiwiSaver. Some of her books are listed at the back of this book.

Why you should have KiwiSaver

While being in KiwiSaver is optional, there are some very good reasons to have it.

If you're in KiwiSaver, your employer has to contribute at least 3% of your salary to the fund you choose, or the one chosen for you as a default member. How much you receive

will be in your employment contract. Some employers give it as part of your overall pay, some include it on top of your normal pay. You'll have to contribute a minimum 3% from your salary or wages also.

And if you're between 18 and 65, for every $1 you put in your KiwiSaver fund (whether via your pay or directly to your provider), the government will give you another 50c, up to a maximum of $521, every year.

So for example: You put $20 a week into KiwiSaver. The government gives you $10 a week – free! If you only put in $10 a week, the government would still give you $5 a week, free. It pays another half on top of your contributions, up to a maximum $521.

Let me say it again, in bold, with another exclamation mark. **This is free money!** It's why every adult **MUST** have a KiwiSaver account, and, if they can, put in at least $20 a week of their own money.

Another way of thinking about it is, in KiwiSaver the money the government puts in gives you an instant 50% return on your $20 per week contribution. Do you know of any other investment that pays you a 50% return up to $521, risk-free, every year? It's a great incentive to be in KiwiSaver.

And even if you're self-employed or not employed and don't receive employer contributions into KiwiSaver, you should still have an account and put in $20 weekly, so you get an extra $10 a week from the government.

The $20 a week must be from you, and not from your employer. Check this by signing into your KiwiSaver account and looking under 'member contributions'.

And it's worth knowing that the government does not pay its contribution weekly, but annually. That means that once a year you will get a very pleasant surprise in your KiwiSaver account.

Like other similar retail funds, there are usually some tax advantages, too, because for many people, gains in their KiwiSaver account are taxed at a lower rate than their personal tax rate.

And if you save in a diversified KiwiSaver fund, for example, a conservative, balanced or growth fund, you will have the additional benefit of a diversified group of investments from all over the world. More on that later.

Why kids should have a KiwiSaver account

Although children aren't eligible for the $521 government subsidy until they're 18, there are still very good reasons to be in KiwiSaver.

Firstly, it enables compound interest to work for them. Using Sorted's savings calculator, you can see if you put one dollar a day into a KiwiSaver growth fund from the day your

child was born, by the time they turned 18 they could have almost $10,000 saved. $2 a day could turn into $19,000+ and $3 a day over $29,000. What a great start to their financial freedom.

Secondly, KiwiSaver is a great way for your child to save for their first home. They can withdraw nearly all of their savings for a first home deposit, and may be eligible for a government first-home grant too.

Thirdly, with the KiwiSaver account being in their name, it's their money, and they will have a sense of ownership about their savings and see where it's invested. Having a KiwiSaver account is critical for vulnerable children, as well, as the money is generally locked in under the child's name. There are only a few reasons KiwiSaver money can be accessed, and these are all subject to a high level of oversight.

Fourthly, when your child becomes older and starts working and earning, they can

immediately start their own saving via KiwiSaver. They will have an account that contributions automatically go into. They will know what they're investing in, and they will be on their way to financial security.

What KiwiSaver fund should you be in?

Having been in the industry for over 30 years and worked for many different companies, I have a clear view on what type of fund you should be in:

- it depends on how long you have until you need the money, either for your first home or in retirement (see opposite page)
- it should charge very low fees (see page 64)
- it should be diversified and predominantely passively managed (see page 72)

There are several online tools to guide you to the right type of fund for you.

For KiwiSaver, the most popular one is on the government's Sorted website under 'KiwiSaver Fund Finder'. The KiwiSaver fund type identified there can be good for non-KiwiSaver investing too.

The website MoneyHub provides good information about KiwiSaver funds too, along with many other types of investment.

How long do you have until you need the money?

How much you need to save for retirement depends on the lifestyle you want, and how long you think you'll need the money for.

Most people will live longer than they think. The average life expectancy of New Zealanders is 80 for men and 83 for women. But if you reach 65, average life expectancy goes

up to 86. This means your retirement savings would need to last an average of 21 years, and perhaps much longer.

So your investments need to return as much as possible over the long term, so they last as long as possible in retirement.

Often, when people are younger, they put their money into conservative funds so they can feel comfortable that they're protecting their capital. This might be the right choice if you need **all** of your money in the short term as you are planning to buy your first home.

But most people need higher returns over the long term and need their savings to last longer. So, they can become more comfortable about putting their savings into balanced or growth funds that have some higher risk investments, such as shares. And because many KiwiSaver members won't be able to access their savings until they retire, they can afford to invest in balanced and growth funds

that return more over time.

To work out how much you'll need to save, you can go to the Sorted website here **www.sorted.org.nz/tools/retirement-planner**

To understand your appetite for risk or to work out what type of fund is best for you, try Sorted's fund-finder here **www.sorted.org.nz/tools/kiwisaver-fund-finder**

MoneyHub has some excellent comparison guides here **www.moneyhub.co.nz/kiwisaver**

Ethical investing is something more and more KiwiSaver funds offer. Some achieve it by excluding investments in certain industries eg, fossil fuels and weapons. Some try to invest in companies actively doing good. Other KiwiSaver managers also donate fees to charity or are not-for-profit charities themselves. If ethical investing matters to you, Mindful Money has a comparison website here **www.mindfulmoney.nz**

GOLDEN RULE 5

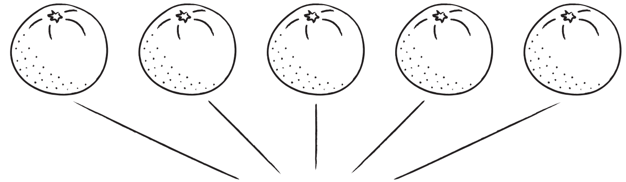
Stop paying high fees and high interest

There are fees everywhere in the finance industry: payment and dishonored payment fees, credit card fees, merchant fees, account fees, management fees, membership fees, origination fees, early repayment fees, foreign exchange fees, brokerage fees, portfolio-monitoring fees, performance fees, administration fees, KiwiSaver fees, and they go on and on.

Each of the fees is designed in a way to make you think you're not paying too much,

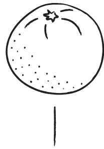
but they really add up.

How can fees be that big a deal? Let's use KiwiSaver as an example, and explain with some oranges. Let's assume that each orange represents 1% and that the KiwiSaver fund you invest in makes a 5% return a year, before fees, after tax. That's five oranges.



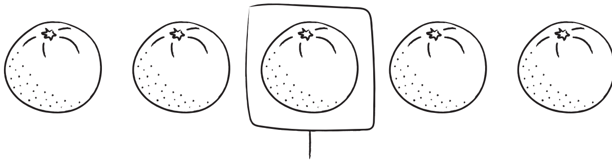
Assumed long-term KiwiSaver fund returns at 5% a year.

And let's assume the average KiwiSaver balanced or growth fund charges a fee of 1% every year. That's one orange. It doesn't sound much, does it?



Average fund fee 1%

It's actually a fortune, because for every $5 you make, you pay $1 in fees. That's 20% of everything you make. That's more like a tax!



In this example a 1% fee is actually 20% of everything you make

Just how lucrative is this for the finance industry? The FMA Annual Report noted that KiwiSaver fees alone in 2021 were $650 million. If you assume there are 5 million people in New Zealand, that's an average of over $130

per person, including small children.

The Sorted website shows that the average Kiwi, working from 18-65 on a salary of $50,000 paying the minimum 3% into a KiwiSaver balanced fund, with their employer paying another 3%, will pay an average of $39,068 in fees over their lifetime. And an average of $56,690 if they're in a growth fund. That's more than they will spend on electricity or a mobile phone.

Average lifetime costs:

KiwiSaver fees	**$39,068[1]**
Power bills	**$37,200[2]**
Mobile phone charges	**$35,900[3]**

The average Kiwi could pay more in KiwiSaver fees than for power or their mobile phone.

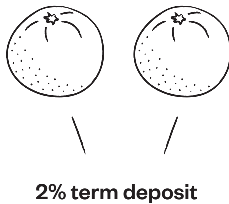
See page 96 for notes on calculating average lifetime fees.

I bet most KiwiSaver providers don't advertise that!

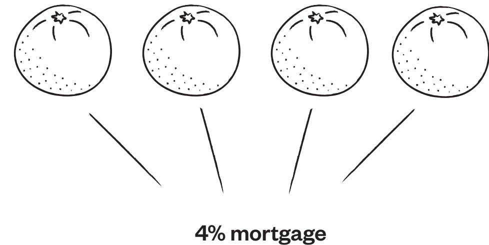
It's simple, fees can make a big difference to how much you have in retirement.

The banking industry is very profitable too. For example, in 2021, the banks in New Zealand made over $6 billion in profits. That's well over $1,000 for every New Zealander. Here's how they do it.

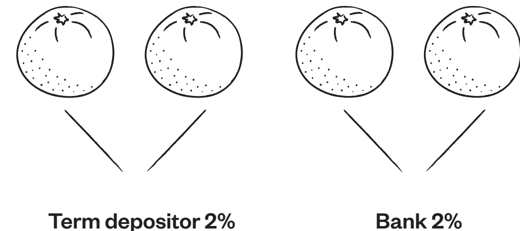
Banks take deposits and give loans. And make a lot by being in between the depositor and borrower. Let's go back to the oranges. Say the bank pays 2% interest on a term deposit.



The bank takes those deposits and lends them out as a mortgage at (say) 4%.



So, who gets what from the 4% interest paid on the mortgage?



This means that the people supplying the money to lend, the term depositors, get 2%, and the banks get the other 2% for arranging

and servicing the loan.

Hold on – depositors are supplying the money, but the bank makes as much as they do!

And it's worse with personal loans and credit cards, where they still pay depositors low term deposit rates, but use that money to make even bigger returns from higher interest rates.

Banking is about the best money-making machine there is. Remember, it's our money they're lending.

A banker might say that this is an over-simplification, and that there are capital requirements, bad debts, branches to keep open, and so on. There is some truth to this, but only some. Banking in New Zealand is a very profitable business, and we pay for every cent of it.

Perhaps the worst of all are payday lenders. They can charge up to 50% interest per year, yet they get the money to lend at a much

lower rate.

It's simple – higher fees mean you pay more, make less, and have compound interest working against you.

For example, paying an interest rate of 3% instead of 4% per year on a $500,000, 30-year mortgage could save you $100,000.

So be paranoid about the fees and interest you pay. They really matter for your financial well-being.

GOLDEN RULE 6
Choose diversified, passive funds

If you already have a KiwiSaver account or have paid off your debts and are ready to save outside KiwiSaver, one of the best things you can do with this money is to put it into a fund that diversifies its investments and is predominantly passively managed.

Diversification is a free gift

With investments, there's no better piece of advice than 'don't have all your eggs in one

basket'. The only exception to this is your own home.

Why should you diversify investments? Because the unexpected can happen, and this means no one event or catastrophe can lose you all your money.

COVID-19 is a great example. Who knew that would happen? During the lockdowns, some companies, such as retailers, lost a lot of money, while others, like medical supply companies, made money. So even in a crisis, if you had invested in both, the gains from one would have helped offset the losses in another.

With investments, diversification is a free gift. It costs nothing, and it protects your investments over the long term. When people understand the advantages of diversification they're likely to be less concerned when markets drop suddenly. A lot of money can be lost when people sell out of fear, but when you

know you have investments spread all over the world, you are less likely to panic.

It's also important to check that your investments really are diversified. Many people lost money by investing in different finance-company debentures before 2008. They thought they were diversified, but the whole industry collapsed, and so did their savings.

The simple truth is that you don't have to pay anything more to properly diversify your investments. Most KiwiSaver funds have thousands of investments in many countries, all done for you.

No one has any real idea which investments will win and lose over the long term. Investment managers do their research, but at best, they're making an educated guess. And when people tell you about their winning investments, they often forget to tell you about their losing ones. One of the issues

with the finance industry is many people are talked into the next best thing by fund managers, stockbrokers or financial advisors. But in reality, they have no more chance of beating the overall market than a monkey with a dartboard.

On the next page is a very useful chart, produced every year by Mercer (global business consultant and fund manager). You can read the words if you want but looking at the asset classes (in different shades) tells you everything. Each represents a different type of class of investments e.g. shares, commodities, property etc. For each year, the ones at the top did the best, the ones at the bottom did the worst.

As you can see, it's a random mess. Just follow one asset class through the years and you can see that returns are all over the place.

The lesson from this is it's impossible to pick which investments will win and lose in any year.

	2017	2018	2019	2020
Best	Emerging Market Equities (UH) 34.6%	Global Private Equities (IRR) (H) 18.2%	NZ Equities 31.6%	Global Private Equities (IRR) (H) 14.9%
	NZ Equities 23.6%	NZ Direct Property 11.1%	Global Equities (UH) 26.9%	NZ Equities 14.6%
	Global Small Cap Equities (UH) 20.3%	NZ Equities 6.0%	Global Equities (H) 26.7%	Global Equities (H) 11.2%
	Global Equities (H) 20.2%	NZ Government Bonds 4.6%	Global Small Cap Equities (UH) 25.4%	Emerging Market Equities (UH) 10.9%
	Global Equities (UH) 20.0%	NZ Cash 2.0%	Global Listed Infrastructure & Utilities (H) 23.7%	Global Small Cap Equities (UH) 8.7%
	Australian Equities (UH) 18.4%	Global Bonds (Aggregate) (H) 1.8%	Australian Equities (UH) 22.5%	Global Equities (UH) 8.6%
	Global Private Equities (IRR) (H) 16.3%	Emerging Market Debt (UH) -0.3%	Global Listed Property (H) 21.4%	NZ Direct Property 5.7%
	Global Listed Infrastructure & Utilities (H) 15.7%	Hedge Funds (Defensive) (H) -1.2%	Emerging Market Equities (UH) 17.7%	NZ Government Bonds 5.4%
	Emerging Market Debt (UH) 13.0%	Global Listed Infrastructure & Utilities (H) -1.3%	Emerging Market Debt (UH) 13.1%	Global Bonds (Aggregate) (H) 5.4%
	NZ Direct Property 10.0%	Global Equities (UH) -3.2%	NZ Direct Property 10.1%	Australian Equities (UH) 4.3%
	Global Listed Property (H) 8.5%	Global Listed Property (H) -3.7%	Global Private Equities (IRR) (H) 9.4%	Hedge Funds (Defensive) (H) 3.7%
Worst	NZ Government Bonds 5.5%	Global Equities (H) -7.1%	Global Bonds (Aggregate) (H) 7.5%	NZ Cash 0.6%

This chart (part of a bigger table) shows how each class of investment performs very differently from year to year, making accurate predictions of what will win and lose impossible.

Table reproduced with permission from Mercer. Full disclaimer page 97

No one I've ever met could pick what the winners and losers will be in the year ahead. For nearly everyone, the best strategy is to own a little of everything, in a well-diversified fund.

By way of example, I have traded many investments, in many financial markets, over the years. So, what do I personally invest in now? A diversified KiwiSaver Growth Fund that is predominantly passively managed.

Passively managed funds

A passively managed fund (sometimes called an index fund) means the fund manager isn't trying to pick winners. Rather, the fund manager is simply choosing to invest in the whole market. Because this doesn't require the same amount of effort as an active fund manager, the fees are considerably lower.

Financial markets are very efficient. For every buyer there is a seller, with someone

winning and someone losing every time. And no one can win for that long. Both the buyers and sellers pay fees every time, so both can end up losing over time. And even if a fund manager has a winning streak for a while by picking winners, they will retire, and you will have to try and pick the next winning manager.

> **FACT: in a widely quoted study, investments selected by a monkey throwing darts at a dartboard got higher returns than fund managers.**[1]

The inability to beat the market is well known by the finance industry. The most comprehensive studies, called SPIVA, are produced by Standard & Poor's. They show that in every part of the world, in every asset

1. 'The Surprising Alpha From Malkiel's Monkey and Upside-Down Strategies', by Robert D. Arnott, Jason Hsu, Vitali Kalesnik, and Phil Tindall, *The Journal of Portfolio Management*, Summer 2013.

class, over the long term, you cannot beat the market. Check out the studies at www.spglobal.com/spdji/en/spiva

The SPIVA studies show that if you are investing for 10 years or more, the chances of an 'active' manager beating the market after fees are below 20%. That's a bad bet, because you have less than a 1 in 5 chance of winning. And studies show that the longer you invest, the worse your chances of picking winners are. Some famous hedge fund managers do manage to beat the market, though if they do, they are typically closed to new investors. And while many fund managers can beat the market over the short term, once fees are taken into account, far fewer do. And often managers have got lucky, or taken excessive risk, and want to tell you how good they've performed in the short term. But in my experience, the minimum period you should pay attention to for returns is five years or more.

So, I make sure the fund I invest in, whether KiwiSaver or non-KiwiSaver, is low-fee, diversified and predominantly passively managed. It should have thousands of investments in many countries.

There is another reason why I choose a diversified, passive fund. It's a psychological issue called 'loss aversion'. It means we hate losing a dollar more than we love making one. And the worry about losing money makes us act from fear, and that often ends up badly. You listen to what's in the press and scary predictions from friends, and sell your investments, often at the wrong time.

Being invested in a diversified, predominantly passive fund means that no matter how bad the news, you don't have all your eggs in one basket. That will make you more comfortable in sitting out the bad times, and not selling out of fear. You know you will have some losing investments, but some winning ones

too. And if you're saving a little each week and the markets go down, you're buying the same investments you bought last week at a cheaper price. That's like buying investments on sale. The technical term for this is dollar cost averaging, and it's a powerful reason to save a little each week in a low cost, predominantly managed fund.

GOLDEN RULE 7
Have a rainy-day fund

Almost everyone gets into tough financial situations from time to time. Whether it's a funeral, job loss or medical problem, we all get caught out by unexpected expenses.

But, if you save a little each week into a rainy-day fund that you don't see, then, if you really need the money in a crisis, it's there. That saves you from the clutches of payday lenders, personal loans and credit cards.

One way to get a rainy-day fund is to set up an account you don't normally see on your banking website or app, and put in a little each week. Or you could send the money to a trusted relative.

'Out of sight, out of mind' is the best way to think about it. The trick is to almost forget it's there but have the money accessible if you really need it.

I think a sensible amount to aim for is 1% of your net wealth in a rainy-day fund or build up to two months' income. Start small, save a little each week, and then forget about it.

And if you get into serious hardship, you can draw down on your KiwiSaver. But don't only rely on that because it's your KiwiSaver supervisor who decides whether you get access to your money for hardship, not you. Their definition of hardship may not be yours.

GOLDEN RULE 8
Have some basic insurance

Most people in New Zealand have too little insurance, and some have too much. For example, about 70% of adults don't have any life insurance. Yet it's also possible to be over-insured and pay thousands in unnecessary premiums every year. That might be great for your insurance agent (who usually gets more commission if your premiums are higher) but could be bad for you.

The way to manage insurance is to treat it as something there in case of potential disasters, not for lifestyle preservation. If you want full insurance for every time your mobile phone gets dropped, you will pay a big price for it.

Also, having too much insurance costs. This is particularly so with the life insurance industry. Insurance brokers tend to sell too much life insurance to too few (on huge commissions), while ignoring the rest of the population who can't afford it. And why can't they afford it? One big reason is because life insurance costs too much, partly because the commissions paid to insurance brokers are so high.

Like in all professions, there are some really good life insurance brokers. But I feel for them because they are swimming with sharks. Even though the insurance industry has undergone some positive regulation changes lately, the worst life insurance brokers still only care about their commissions.

With insurance, I look at the MoneyHub or

Consumer websites. They are a good source of information.

While acknowledging everyone's circumstances are unique, if you have others who are dependent on you, my rule of thumb is you should have your life insured for the value of any mortgage, plus two years' income.

And you should have your house insured for its replacement value, as well as your car and any expensive possessions. In all cases, my advice is to go for the highest deductible amount (the amount you pay before your insurance plan starts to kick in) to keep the premium lower.

One other 'must buy' in insurance is travel insurance, especially for medical issues overseas. You do not want to be caught out very sick in a country that won't pay your doctor's bills. They can be huge, up to $10,000 a day in some countries.

Using financial advice

Most people need financial advice, but few need a financial advisor. For most people, reading books, newspaper columns or blogs goes a long way towards learning what they need to about money. There are some suggestions at the end of this book.

There are some very good financial advisors out there, and there are times when their advice is really useful. Generally, the more complex your circumstances, the more you could use an advisor.

But be careful, because many advisors are paid commission by providers, so they can be biased in their advice.

There is a clear difference between an advisor getting paid a commission as opposed to those charging a fee. Would you get medical advice from a doctor who was paid commissions from the drug companies? I hope not!

If you are getting financial advice you should always ask an advisor this question, word for word:

> 'Are you receiving any form of commission, compensation, remuneration or incentives from financial-product providers, in any form whatsoever?'

Ask them to answer just yes or no. No fancy statements or disclosures, just yes or no. If they say 'yes', run a mile.

I would only use advisors that charge a fee

for their service, just like a lawyer or accountant does. And I would be focused on the fees they charge, and the fees you pay in the products they recommend. As well, their advice should focus more on your overall financial wellness, and less on any financial products.

Remember, any fee charged as a percentage of your investments disappears forever from your savings, meaning compound interest works less for you. This is another reason to select low-fee, passively managed investments.

Conclusion

My whole working life has been about making and investing money. Having worked for banks, investment banks, stockbrokers, insurers, finance companies, hedge funds, the whole lot, I've learnt that the important things about money are actually very simple.

And even though I could be called an industry 'expert', the golden rules in this book are exactly the ones I apply to my own life.

My partner and I own our home. My KiwiSaver fund is diversified, passive, and with low fees. I have a rainy-day fund, I don't have

credit cards and I have travel, home and contents and car insurance.

If I had a mortgage and young children (mine are grown up) I would have some basic life insurance too.

That's it. I sleep really well at night and don't worry about money.

Money is simple. Understanding the three simple truths about money, and applying the eight golden rules, will help you master money, and give you the choices and dignity that more money brings.

Thanks for reading this book. It's been fun, and a privilege, to be able to share. And thanks to my employer, Simplicity, for paying to produce and distribute it.

Learn more

These are my favourite sources of information and advice, written by people I respect, and who I think are balanced in their view.

Books

The Barefoot Investor by Scott Pape – if you read only one book, read this. It's easy to understand, is based in the real world and outlines sensible ways to master money and enjoy life. Scott Pape is a legend.

Rich Enough? and *A Richer You* by Mary

Holm – the Kiwi barefoot investor, Mary Holm has been giving sensible advice for many years. She is unbiased, unimpressed by spin and fair. Her books are an easy and popular read, as are her columns in *The NZ Herald* and she makes regular radio appearances.

Money Matters by Amanda Morrall – this is the best book I've read for understanding money as a part of a well-rounded life. My partner Amanda talks about getting into your financial flow ie. making money work for you and your chosen life. The details are a little out of date now, but the concepts are timeless. She has a fun blog too - Amandamorrall.com

Websites

Sorted (www.sorted.org.nz) is the government-owned website. Sensible and reliable, it is run by people who know what they're doing and want the best for ordinary Kiwis.

MoneyHub (www.moneyhub.co.nz) A veritable treasure trove of good ideas and sensible advice, and very easy to read and understand. Every time I go to this site, I learn something.

The Happy Saver (www.thehappysaver.com). Another fount of good, sensible, unbiased advice, written in plain English. There is a podcast too, with a wide range of subjects.

Mr Money Mustache (www.mrmoneymustache.com) A crazy name, but a crazy amount of good advice. Kiwi supporters have a Facebook page too - Kiwi Mustachians, which is full of good advice and opinions.

Podcasts

NZ Everyday Investor – Darcy Ungaro hosts many interesting interviews with experts, on many subjects.

The Happy Saver – complimenting The Happy Saver website (see above).

Cooking the Books – Frances Cook presents her radio show as a podcast too, with a wide range of interesting views on many money subjects.

Notes

Page 67. Calculating Average Lifetime Fees

1. Average fee for a person investing in a KiwiSaver Balanced Fund, from age 18-65, on a salary of $50,000, paying 3% into the fund per annum, with their employer paying another 3%. Assumes a salary increase of 3.5% per annum, and that fees do not change over their lifetime. Fees are not adjusted for inflation. Calculated as at 23.06.2022.
Source - Sorted Fund Finder. sorted.org.nz/tools/kiwisaver-fund-finder

2. Assumes average $785.55 spend on power, paid from age 18-65, based on annual household spend of $2,121, and 2.7 persons per household. Not adjusted for inflation.
Source - MBIE Household sales-based electricity data 2021 www.mbie.govt.nz/building-and-energy/energy-and-natural-resources/energy-statistics-and-modelling/energy-statistics/energy-prices/electricity-cost-and-price-monitoring/
www.stats.govt.nz/news/new-data-shows-1-in-9-children-under-the-age-of-five-lives-in-a-multi-family-household

3. Assumes $40 per month charge for a medium user, from age 18 to 65, not adjusted for inflation.
Source - Commerce Commission 2021 Telecommunications Annual Monitoring Report. comcom.govt.nz/__data/assets/pdf_file/0019/279100/2021-Annual-Telecommunications-Monitoring-Report-17-March-2022.pdf. This is a like for like comparison only, based on current fees charged. These figures will change if providers change their fees over time.

Page 77. Mercer Periodic Table of Investment Returns Disclaimer

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