e book

A fresh approach to financial independence for women

pink investments.org

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Disclaimer

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Before acting on any information in this ebook, Ethical Financial Services Pty Ltd recommends that you consider whether it is appropriate for your circumstances.

Welcome

In the years I have been involved in the financial services sector I have spoken with thousands of women. I have learned that they want to be in charge of their own money and their own destiny. I believe this book can help women achieve this.

Personal finance is an important part of life. However, it can be an intimidating and often boring subject.

The financial services industry shrouds itself in its own secret language - a mass of mystifying jargon to bewilder the potential consumer and conceal poor value for money.

Governments are little help. They make topics such as Tax and Pensions, daunting and difficult to understand. For your benefit, throughout this guide, I have strived to eliminate the jargon. I have aimed to explain complex topics; and to demystify the secret language of the financial world.

I believe this guide will expand your knowledge and understanding of finance. It will enable you to move forward with confidence. It will empower you to make key financial decisions that will positively shape your financial livelihood throughout your life.

This book covers all the key topics of the personal finance world. You can purchase the guide in its entirety or choose to purchase individual modules that may be of particular interest to you. I guarantee that if you take the time you will be well on your way to a secure financial future.

Best Wishes

Yvonne Jenkins.

Director: Ethical Financial Services Ltd.

Introduction

Whether we realise it or not we are already on a financial journey. In today's society it is an unavoidable path. In order to pay rent, a mortgage, buy a car, food or clothes, money is needed.

Where our individual journeys may differ will depend on which route we take to achieve these things. But essentially we are striving for the same result – financial security.

Saving – Debt – Investment – Insurance – Retirement savings plans

It may seem like a complicated journey. But if we break down each aspect then a clearer understanding can be achieved. In fact each of these topics is linked in one way or another; and each aspect affects the degree of financial security we will reach. For example:

To have strong financial security upon retirement a substantial amount of pension savings is required. So, how do we achieve that substantial amount?

We **must** save.

We **should** have insurance.

We **should** avoid (bad) debt and,

We **could** invest.

Consider these 4 four points. Which of these apply to you?

Chances are that if you are reading this e-book then you are keen to take the journey to financial security. And believe it or not, most women have the traits in place to achieve this. Statistics show that:

- 88% of women say they have the ability to save (88% men)
- 91% of women say they have the ability to budget (men 90%)
- 83% feel confident with credit cards (men 84%)
- 88% of women say they can manage debt (men 90%)

(Financial literacy: Women understanding money 2008)

Introduction

It is clear that many women already have sound budgeting and saving habits. This is great; but we are only half way there. There is still half a journey to go.

Only 60% of women believe they can ensure enough money for retirement (men 65%) and only 63% of women believe they have the capacity to invest money (men 75%).

What's more 52% of women state that dealing with money is 'stressful and overwhelming' (men 43%).

These results show that women tend to be more confident in the day-to-day matters of budgeting and debt management, yet are less certain in their ability to invest. Why is this so?

Let's consider 2 things:

- Many women today are busy with a career and/or family responsibilities.
- Statistically women have a lesser understanding of financial language.

"I cannot afford to waste my time making money."

In general, women find making investment decisions to be stressful, difficult, and time-consuming.

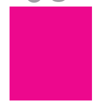
Treat this e-book as a guide to your financial security.

This e-book is written to maximise understanding. Each chapter is self-contained so you don't have to read the entire e-book to understand one chapter.

Importantly this e-book also includes a readily accessible glossary of terms to help you on your way. By rolling your cursor over an underlined word or phrase, you will reveal a pop-up glossary term.

This e-book is specifically designed with women in mind. It will shape your confidence and financial decision-making skills. It will educate and empower.

Managing Debt



Managing Debt

Managing your debt is a crucial factor in achieving financial independence.

As a financial topic, debt is simple. There are no secrets, but then, there are no easy solutions either. It isn't rocket science but it does take discipline to control the debt monster.

Acquiring Debt can be a slippery slope. No matter how much you pay each month, there still seems to be the accumulation of interest.

Stop your debts taking control of your financial life. Keep them at a steady level and reduce the chance of them getting out of control.

Debt should be kept at a maximum of 20% of take home pay. If your debt is running at higher levels than this, consider debt consolidation programs. Or use your mortgage to place your debts under one roof, with a lower interest rate.

Erratic cash management cuts across all income groups. In fact, a recent survey revealed that those with incomes above $100,000 more frequently over spent as compared with people on less than $35,000.

Budgeting is the cornerstone of good financial health. Simply put, if you are spending more than you earn, it will eventually damage any financial plans you have.

Given the availability of credit and the passionate consumer culture of the 21st Century, it is hardly surprising that we are taking on more debt and at earlier ages than ever before.

There are all sorts of theories about why we spend money we do not have!

Whatever the theories, it is a fact that overwhelming debt can cause great shame and frustration for many women.

Managing Debt

Causes of Debt

The causes of debt can be many and varied. It does not take a reckless person or a wild spending spree to create a debt crisis. Loss of income via unavoidable situations such as death of a partner, divorce, redundancy, long term sickness can precipitate a crisis. Extravagant use of credit cards may also precede a debt blowout. In recent years gambling is increasingly pushing women into debt.

Theories behind credit overuse

People nowadays do not see credit as debt. They believe they have the right to use whatever funds Banks make available to them.

Each generation uses money as a way of differentiating itself from parents. Therefore, today's adults are rebelling against the more thrifty generation.

Some people believe they will never be financially successful and act out this belief by spending wildly; a theory dubbed 'The psychic masochists'.

The 'adaptation-level phenomenon'

If we get a salary increase we think it is wonderful at first. But then we adapt to it and eventually we start to spend beyond our increased income. And so the cycle starts. We want bigger and better cars, homes, TVs etc... But they do not bring lasting contentment. This scenario can be very dangerous because our desires are expanding faster than our incomes.

Managing Debt

Causes of Debt

Many women leave college or university with heavy debt. Credit card companies and their smart marketing campaigns entice young students with all kinds of 'special deals'.

Students may start off using the credit card wisely, but the opportunity to expand their material wealth can become irresistible. Gradually MP3 players, phones, laptops and clothes start going on the card! Even tuition fees! It seems worth it. After all it is for their education!

But no one is educating them about the false freedom a credit card gives them. The implications are great. A wrecked credit card rating at college, can severely affect future attempts to get a mortgage or car loan.

Setting up your home can incur debt. Buying expensive household items on credit instead of buying them as and when you can afford them can send you into a debt spiral.

Some extraordinarily lavish weddings are paid for on credit. This scenario can set you up with debt from the very start.

Credit card spending plays havoc with rationality. It encourages impulse buying, bad-mood buying, good-mood buying etc. There are more debt triggers than ever before.

Catalogue shopping used to be a major cause of debt for many women, but with the advent of online shopping, it is easier than ever to spend a fortune by a simple click of a button. It can easily become an addiction.

Do not get seduced into store card discounts. Unless you pay the amount off in full at the end of the month, this can be a slippery slope! Store card discounts can lead to large ongoing debt balances which ultimately will cancel out the initial discount you received.

Debt does not put you in control. It is a chain around your neck.

Make decisions about what to buy and when to buy it with the money you have now, not with money you hope to earn in the future!

Managing Debt

Compound Interest

Compound interest is a powerful force that works either for you or against you. If you want this force on your side, you will have to exert considerable will power!

Let's consider two simple examples: a positive and a negative one.

Example 1: Say you save $75 every month, earning 5% interest. If you do this for five years, you will end up with $5,100 in emergency savings.

Example 2: Let's say you come up $75 short every month, over five years. Let's also assume that you routinely make up this difference with a credit card.

This is less than $20 per week deficit – hardly a symptom of reckless "retail therapy."

Nonetheless, at the end of five years and assuming an 18% credit card interest rate you will be faced with $7,200 worth of debt!

This is the difference between saving and paying down debt.

Saving is hard, but paying down debt, once it has accumulated, is $2,100 harder! This difference just gets bigger as time goes on.

While your bank savings work to make you more money, any outstanding credit card debt is likely to be working three times harder and charging a much higher interest rate than your savings pay.

There are probably very few debt-free people around today. Some debts are an inescapable part of life for most of us.

By saving money you have the force of compound interest on your side.

As a debtor, this same powerful compounding force works against you, and the higher the interest rate, the faster the momentum builds.

Managing Debt

Good Debt vs Bad Debt

Here are some basic debt management rules that will help to keep the lid on potential problems:

Take inventory of all the debts you have. Allocate as much of your monthly budget as you can to paying them off. This can be painful, because initially you see 'nothing' for your money! Perseverance is key!

Tackle the highest interest debts first. These are most likely to be your credit cards.

Be especially wary of double-digit debt. These are generally, credit cards and loans that charge 10% or more in annual interest. At this level, balances mushroom quickly, and it's hard to get a return on the borrowed money that beats this cost.

Good Debt – Yes it does exist.

Good debts, like some mortgages and student loans, combine two things:

Managing Debt

Good Debt vs Bad Debt

1) a relatively low, tax-adjusted interest rate; and

2) The potential to invest in something that, over the long run, will grow in value.

A fun exercise

Write down 5 uses of your money that will positively affect your life in a decade or more. For example: spending money on a good education, saving, paying off the credit card, paying extra into the mortgage, travelling to gain life experiences.

Now list 5 uses of your money that will have no beneficial affect on your life in the future. Impulse buying things you don't need, buying a new car every year, buying junk food, buying expensive celebrity magazines, paying late fees on bills.

The point to this exercise is to show which areas of spending enhances or impairs your life. With this understanding you can then redirect the cash flow to the important things and not fritter it away on the frivolous things.

For Example: Personally, what gives me gratification are travel, yoga, going to the opera, a decent hair cut and having a cash buffer in case of emergencies.

Over the long term, spending more than you earn will ruin your financial health!

What does not enhance my quality of life are: speeding fines, parking tickets, overdraft fees, buying fast food when I am on my own instead of cooking something etc.

Do not be a slave to debt. Set strict rules for yourself.

Managing Debt

The Personal Finance Divide

Over time, you'll find yourself on either the savings or the debt side of the personal finance divide. It doesn't take much to nudge you one way or the other, and once a direction is established, momentum can build. This is great if you're on the saving side of the divide. But if you're on the debt side, that momentum makes it harder and harder to achieve financial security.

If you want to end up on the savings side, make sure you spend less than you earn and tackle credit card debt quickly!

"Happiness is less a matter of getting what we want than wanting what we have."

D.G.Myers

Professor and author D.G.Myers wrote in a recent article about economic growth and human morale. Whilst I am not into 'airy fairy' theories, I feel that this is an important point. Contentment may well be at the root of why we spend and save as we do.

Being content with your current income. Choosing to live within its boundaries, will help you stay within your set budget and will prevent you from notching up credit card debt.

Making a deliberate decision, each day to be content can form the foundation to a sound financial life.

Mortgages: What you need to know

Mortgages
Understanding the Basics

For most women a home is the single biggest purchase she will ever make. Therefore it is vital to get the right mortgage from the very beginning.

There are an abundance of mortgage products around today. The whole concept can be a confusing minefield. Some mortgages will suit your needs better than others, but how do you decide which one is best for you?

A mortgage is a loan secured on your home, usually arranged for a term of 25 or 30 years. If all goes well, you'll make all necessary repayments and end up owning your home.

However, if something prevents you from meeting your payments, your lender can foreclose your home and sell it to pay off your debt. Basically your house is repossessed. Hence the warning, "Your home is at risk if you do not keep up repayments on a mortgage or other loans secured on it."

As such a mortgage is not something you should go into without due consideration.

Mortgages

Knowing What You Want

To find out what you want from a mortgage, you need answers to the following questions:

1) How much can you borrow?

2) How much can you *really* afford?

3) How do you want to repay your debt?

4) How do you want interest to be charged?

Buying a house is like everything else - once you start looking, you will invariably discover that the house of your dreams is more than you can afford. If you want to avoid disappointment, the first thing you need to establish is how much you can borrow.

1) Establish how much you can borrow

Salary Multiples

Most lenders use a formula to establish the amount they will lend you. Generally speaking, for an employed woman, a mortgage lender will let you have about three times your gross salary, sometimes a little more.

Never borrow more than you can comfortable afford to pay back.

If you are buying with a partner then they may add in the equivalent of his or her annual salary in addition to the amount they're prepared to lend you. Alternatively, they may lend you two and half times your joint income. This usually means you can raise a slightly bigger mortgage.

In the last few years lenders have been lending on extended multiples – sometimes up to five times income.

Any additional income from bonuses or commissions you receive may be taken into account as well. Do some calculations and work out how much you're likely to be able to raise via a mortgage. Is it enough, bearing in mind the price of real estate in your local area?

Mortgages

Knowing What You Want

Deposits

The next thing to consider is the **deposit** you'll need to buy the house. Usually a mortgage lender will loan you up to 95% of the value of the real estate. This means you'll have to come up with the remaining 5%. If you want to buy a house worth $100,000, you'll need a deposit of $5,000!

Now consider the following:

- Do you have any savings that you can use?
- Can you raise the money by other means, if you haven't?
- Can your parents help?

There are certainly lenders who will give you a 100% mortgage but you will almost certainly have to pay higher interest rates for these; because if you default on the mortgage, the lender wants to ensure that they get their money back in full.

The larger the deposit or 'down payment', the lower the rate of interest you are likely to pay; the larger your deposit, the less risk of you going into **negative equity**.

Negative equity is a nasty situation that occurs when the value of your house falls to below that of your mortgage. This can happen and did during the last housing bubble in the early 1990's. There are signs that this is happening again in the current housing market.

Mortgages
Knowing What You Want

Associated costs of buying real estate

It’s not just a case of finding the deposit and knowing how much your mortgage payments will be each month. The moment you’ve found the home of your dreams and have had your offer accepted, you will find that more costs will surface.

The main points to think about are valuation, survey and legal fees and removal costs. In some countries you may also have stamp duties to pay. These are quite hefty additional amounts that you need to factor in to your costs.

2) How much can you really afford?

It's all very well coming up with the right figures when working out if you can raise a big enough mortgage and deposit. *But how much can you honestly afford?*

Mortgage lenders will use your *gross* income to determine how much they will lend you. But in truth you should use your take-home pay to calculate if you can afford the repayments. You really must gauge what you've got left after you've added up your current monthly commitments.

Create a realistic budget plan. Sit down and make a list of your income and outgoings. Work out what you'd really have available each month to comfortably fund a mortgage. There is no point paying your mortgage every month, only to find that you can no longer go out, buy clothes etc… You want to maintain a quality of life too!

Think about your current debts. Do you owe money for other loans, or on your credit cards? Can you re-arrange these debts to ensure that you're getting the best deals? Try to ensure that you have your debts well under control before you even start thinking about buying a house!

Mortgages
Knowing What You Want

As far as debt goes, a mortgage is a good type of debt, because your home can be considered a real investment, which should appreciate in value in the long term.

Think very seriously before committing yourself to a mortgage.

Remember that just because the bank will lend you money, it doesn't mean that you will realistically be in a position to repay it. Ensuring you are in control of your other expenses is vital. If you fail to make your mortgage repayments on time, then you are in trouble. The lender has first charge on your house. Simply put, because your house acts as the security (or collateral) against the loan, the lender can sell your home to recoup their money.

Once you've agreed to take on a mortgage you cannot escape its obligations. Well, not without going bankrupt, this is not a good idea.

It is essential that all costs involved when buying your home are well within your means. Ideally, you should be able to meet your general living expenses, make your mortgage repayments, and still have some spare cash to add to your savings.

> One rule of thumb is to aim for a monthly mortgage payment that takes up a maximum of one-third of your disposable income.

Remember to always have a cash emergency fund available. This is basic common sense. If you suddenly lose your job or get sick then you can pay your mortgage for a few months without too much worry.

Now that you have worked out what your price range is you can start to look for properties. You now need to decide on the right sort of mortgage for your personal circumstances.

Mortgages

Knowing What You Want

3) How do you want to repay your debt?

When repaying your debts you have two basic mortgage choices: **repayment** or **interest only**.

Repayment Mortgages

Repayment mortgages mean that when you make one monthly payment part of your repayment goes towards the interest charge and the remainder goes towards paying off your capital. Capital is the actual amount you borrowed at the time of purchase.

In the early years, your repayments go towards paying interest. In the later years, as the interest charge decreases, more capital is repaid. Your final payment clears your debt and you are mortgage-free!

Interest-only mortgages

Alternatively, you can opt for an interest-only mortgage. This means that your monthly repayments *only repay* the interest. You do not actually pay off any of the capital.

Interest-only mortgages can be an attractive option when considering investment properties, where you intend to sell the real estate within a few years.

Mortgages

Knowing What You Want

4) How do you want interest to be charged?

There is a confusing choice of mortgage products on the market. It is worth spending some time to fully understand each type, before you make an informed decision as to which is best for you.

Lenders charge mortgage interest in six basic ways:

1. Standard variable rates (SVRs)

A **standard variable rate** is the average rate paid by borrowers who aren't on a special deal. Although some lenders offer competitive rates, SVRs are generally above the stated bank base rate. Lenders love customers who can't be bothered to switch from their SVRs to a better deal. This is because they can make a substantial profit on such lazy customers. My advice is to *avoid paying the **s**tandard variable rate* unless you can't find a better deal elsewhere.

With a standard variable rate mortgage your monthly payments will vary depending on what happens to the base rates of your bank.

2. Discounted variable rates (DVRs)

Discounted variable rates offer a discount on the standard variable rate, and, therefore, you have lower repayments. Discounts may apply for as little as three months or up to five years or more. Be warned, the biggest discounts usually have drawbacks in the form of **redemption penalties**.

Redemption penalties are lock-in penalties. This means that you will be penalised you if you decide to pull out of the deal early. Some deals even include penalties that extend beyond the discount period. These are called as **redemption overhangs** and are worth avoiding.

With a discounted variable rate you are guaranteed to pay less than the standard variable rate. At the end of the day, if you need to know exactly what your payments will be each month, a fixed rate may better suit.

Mortgages

Knowing What You Want

3. Fixed rates

Fixed rates do what the name implies. Your rate is fixed for a pre-determined period despite what happens to the bank base rate and the lender's standard variable rates. These rates can be for any fixed time period, even for the full 25 years.

Many first-time buyers choose fixed rates to guarantee their payments in the early years, while they are adjusting to life with a mortgage.

However, be wary of the very low initial rates as they too carry redemption penalties.

4. Capped rates

Capped rates are variable-rate mortgages with a twist. They include a cap that puts an upper limit on the interest rate that you pay. This is usually at a rate well below the lender's standard variable rate.

As with **discounted variable rates** and fixed rates, most capped rates last for between two and five years. So, if your lender's **standard variable rate** falls below the level of your cap, you are required to pay the **standard variable rate**. If it doesn't, you simply pay the cap. Caps are useful if you think interest rates will rise during the life of your deal.

5. Trackers

With a tracker mortgage, you pay the central bank base rate plus a predetermined percentage.

For example, if the base rate is 6.75%, with a base+0.75% mortgage, you would pay 6.75 + 0.75 = 7.5% now. So, when the base rate is cut by 0.25%, the entire 0.25% cut is passed on to you.

Unlike a standard variable rate, where there is no guarantee you'll get the full effect of a rate cut. If you think the base rate will fall or stay low, trackers offer an attractive alternative to **standard variable rates**. But note that rates may not be as low as the best **discounted variable rates** or fixed-rate deals.

Mortgages

Knowing What You Want

6. Flexible, offset and current account mortgages

These mortgages are the most sophisticated and most adaptable mortgages around. You can overpay, underpay, take payment holidays and use your credit balances to reduce your interest bill.

The chances are you work extremely hard to earn your money. So make your money work just as hard for you. This is the theory behind this latest trend in mortgages. They are known as **flexible mortgages**, **current account mortgage**s and **offset mortgages**.

These mortgage types were first launched in the late 1990s and are already amongst the most popular mortgages on the market.

Although you may not be buying a new home at the moment the chances are that you can save a huge amount of money by switching to one of these new mortgages. This is especially true if you took out a traditional mortgage a few years ago.

It is possible to save thousands by reorganising your finances!

Your mortgage is one of the biggest financial commitments you'll ever make. Therefore it's vital to make sure you get the most cost effective product possible. At the moment your money is probably scattered around in several different places. For example:

- You may have money in a current account earning little or no interest at all.
- You may have savings earning some interest, only to see a large chunk of this disappear in tax; and
- You might have debts such as overdrafts, personal loans, credit cards or store cards. The rate of interest you pay on these could be anything up to 25%.

With this new type of mortgage, you put all these accounts together. This can be quite tricky to understand at first. Instinctively when we think about money we like to separate different items to make it easier for us to understand what money goes where. However, once you get the hang of the basic concept it's easy enough to understand.

Mortgages

Knowing What You Want

Rather than receiving interest on your current and/or savings account, you take this money and use it to reduce the amount outstanding on your mortgage.

You pay less interest as a result. Your mortgage interest is likely to be a lot higher than the interest you are earning on your current account! You can also add other debts, like personal loans and credit cards to your mortgage balance.

You will be able to pay off your mortgage faster and save thousands in the process by having your money working for you rather than against you.

Mortgages

New Mortgage Products

Just like an ordinary mortgage with the following new mortgages you can choose how to repay the capital and the interest. Although these new mortgage products use the same basic principle, they each work in a slightly different way.

Here is an overview of each:

Flexible

A flexible mortgage is the simplest of the three main types of new mortgage products. Many ordinary mortgages won't allow you to repay the capital early without charging you a penalty. Some allow you to repay up to 10% each year.

A flexible mortgage will allow you to make repayments whenever you like and allow you to benefit from these straight away in terms of lower interest payments.

> A flexible mortgage is best for people who receive large lump sums on a regular basis (from a bonus or commission perhaps) and who want to pay off their mortgage as quickly as they can.

The downside is that once you've repaid an amount you may not always be able to get this money back straight away (say if you then change your mind and you want to spend or invest it instead). You may need to get the mortgage company's permission.

Current Account

A current account mortgage combines your mortgage and your current account. You can transfer balances on savings, personal loans or credit cards into these accounts as well. Why would you want to do this?

Because your mortgage is secured on your real estate the interest rate you pay is much lower than you would pay on a personal loan or credit card. With a current account mortgage you pay one mortgage rate on all your debt. The interest rate is also likely to be higher than your savings or current account so you can save more interest on your mortgage by offsetting these balances.

Mortgages

New Mortgage Products

If you have a significant amount of savings and/or debt you could be substantially better off. The downside here is that it can be a little daunting to look at your bank balance and see that you are overdrawn by tens of thousands! It is just a matter of coming to terms with the fact that everything is now showing on one statement.

Offset Account

An offset account operates in a similar fashion to the current account mortgage. However; instead of combining all these accounts together, each is held separately.

This avoids the scary overdrawn bank statement!

You will have to manually offset your accounts. This means you would need to manually set up a system to make sure each relevant account was debited & credited on time; unless there is an automatic facility available. Therefore you need to be much disciplined to opt for this type of mortgage.

These new mortgage products are well worth exploring, because they could make you huge savings in interest payments over the term of your loan.

Mortgages

More Money Saving Tips

Removing the Private mortgage insurance or Mortgage Guarantee premium

If the amount you borrowed for your home was greater than 75-80% of its value, you will probably be paying a Private mortgage insurance or Mortgage Guarantee premium.(PMI/MGP). This in essence is an additional insurance premium to protect the lender.

These premiums are not small amounts of money. They can effectively increase your interest rate by between 0.3% - 0.95%. On larger mortgages this can amount to a lot of money!

You can easily get rid of this extra charge. If the value of your house has risen considerably since you bought it, get a new valuation done. Send this new valuation to your lender and request that they remove your Private mortgage insurance or Mortgage Guarantee premium.

Alternatively if you have a lump sum of money available, use it to pay off your mortgage. This can help to bring the loan to value ratio down below 75%; which means you would have a loan representing less than 75% of the value of your real estate. The Private Mortgage insurance or Mortgage Guarantee premium can then be removed.

A mortgage is a large debt, so if you can slash a percentage point or more off of your interest rate by refinancing, it is generally worth doing.

Mortgage Refinancing

In this situation, contact your existing lender and ask if you are eligible for the same special deals they are offering new borrowers. You may be surprised at how easy it is to renegotiate a new interest rate on your existing loan.

The equity in your home (what it is worth minus what you owe) can be a good source of low interest finance for you. If you have a lot of high-interest debt such as personal loans and credit cards, consolidate them into your mortgage and pay a low rate of interest for them all. However, remember that the collateral for these loans is your home.

Most lenders do not want to lose your business to a competitor. You can avoid fees associated with re-financing by negotiating a better deal with your existing lender.

Insurance

Insurance

Insurance is probably one of the more mundane subjects in the financial spectrum, but one you can not afford to overlook.

Life insurance is vital for the financial security of those who depend on you; your partner, or your family. It is a simple, inexpensive precaution against unexpected life events such as death, medical crises or total and permanent disablement.

Life insurance cover should underpin all your savings strategies, particularly if you have dependants. It is more than just protection and peace of mind - it's about time and money.

It can take years of hard work to buy a home, build a comfortable lifestyle, and accumulate assets. A fire, serious injury, loss of a partner or any number of unexpected events can cause havoc, setting you back emotionally and financially.

This is why insurance is an essential part of wise financial planning.

Many working and non - working women are drastically underinsured. For years non-working women's contributions were not given a monetary value when it came to insurance.
Thankfully this is changing now.

Insurance

How Life Insurance Works

Life insurance is a vehicle for protecting your beneficiaries; be they your partner and/or family members. It is based on a contract between an individual and an insurance company. This contract is known as a **policy** and is purchased to insure the life of a person.

The policy owner pays money called a **premium**, to the insurance company in return for a set level of cover. On the death of the policy owner, the insurance company pays a death benefit to a named beneficiary or to the estate of the deceased.

In most countries proceeds from a term insurance are free of tax.

The death benefit is paid directly to the beneficiaries, bypassing the need for costly lawyers.

Life Events

Most women tend to take out insurance only when an event forces them to! Life events that most often prompt action are: birth or adoption, marriage or cohabitation (where there are joint debts), buying a real estate, school fees planning, inheritance/estate planning.

It is important to review the levels of cover that you have on yourself and your partner. Most women tend to be drastically under insured, particularly mothers at home. It is important to note that just because you may not be earning a salary, does not mean that you should be insured for less! Your loss would be a devastating blow to the family. When everybody is grieving, is not a time that they need to be worrying about money!

Insurance

Types of Life Insurance

There are two general categories of life insurance:
Term insurance and **Permanent/Whole of life insurance**.

The table below sets out the main differences between the two:

TOPIC	Term Life	Permanent Life
Key strategy	"If you die"	"When you die"
Protection period	A Defined period	Usually until death
Level of cover	Typically low cost	Generally more expensive
Proceeds paid out	Generally Tax free	Not always Tax free
Investment options	No	Yes
May help build equity	No	Yes

Term insurance is bought for a specific period of time, whereas Permanent/ Whole of life insurance will provide cover up until death, regardless of age.

Insurance

Critical illness Cover

Critical illness insurance is designed to pay out a lump sum if a policyholder survives after the diagnosis of a serious illness. About 60% of such policies are sold alongside a new mortgage; typically to first-time buyers.

It is easy to see how a mortgage broker or bank adviser can emphasise the "fear factor" - we are far more likely to suffer a serious illness before retirement than we are to die. If you opt for critical illness cover, and have dependants, ask for a policy that also includes life cover, which effectively comes free in such contracts.

However, once you have made a claim on the critical illness policy the built-in life cover usually becomes invalid. As such you will need to ensure that you have enough stand-alone life cover to meet your needs.

Anyone looking to shop around and make comparisons between different providers of critical illness products will have an uphill struggle.

There is a "core" group of seven conditions that insurers have to include in critical illness policies:

- cancer,
- coronary artery by-pass surgery,
- heart attack,
- kidney failure,
- major organ transplant and
- stroke

However other types of illnesses and diseases can be covered. Exclusions and prices vary considerably.

Insurance
Critical illness Cover

Critical illness cover is one type of policy where you really should read the small print and all the exclusion clauses. However, if you approach an independent financial planner/adviser they can do this legwork for you.

The main point to remember when buying critical illness cover is a **guaranteed lifetime premium**. This means that the price you pay at the beginning (usually for 25 years for a mortgage-based contract) is fixed for the whole term.

As medical technology improves more people are surviving serious conditions; and insurers are faced with spiraling claims. To tackle this insurers try to push new policyholders on to "**reviewable**" premium contracts.

Reviewable premium contracts means the price you pay will change (almost certainly upwards) every five years. These price reviews will be based on the company's claims history and market forces - not on your state of health.

It is probable, that guaranteed rates will be phased out in the near future and prices overall for critical illness deals will go up sharply. So, if you are in the market for this type of policy, it may be a good time to lock in a guaranteed premium rate.

By pushing this easily-sold type of policy, advisers may not be telling customers about the other options, such as income protection cover. Critical illness cover will pay off your mortgage, but Income Protection insurance will pay you a long-term salary if you are unable to work. In many cases this is far more important.

For many women, critical illness cover gives peace of mind that the mortgage will be paid off if they cannot work. Critical illness cover is significantly cheaper than Income Protection.

Insurance

Income Protection

Income protection policies pay out a set amount of income over your claim period – which in serious cases can be right up to your normal retirement age! This is a specific insurance policy designed to protect one of your most valuable assets – your ability to earn income. A sudden loss of income can cause extreme hardships on your family or dependants. This is particularly important for the self-employed.

Many women never sit down and consider their lifetime earning potential. The following table might surprise you – it shows some hypothetical households:

Household Income	Age 25	Age 35	Age 45	Age 55
50,000	2 Million	1.5 Million	1 Million	0.5 Million
75,000	3 Million	2.25 Million	1.5 Million	1 Million
100,000	4 Million	3 Million	2 Million	1 Million
150,000	6 Million	4 Million	3 Million	1.5 Million
200,000	8 Million	6 Million	4 Million	2 Million

With income protection, 75% of your salary can be protected; as you are not meant to make a profit from it. But if you have critical illness and income protection you will get a payout from both.

Insurance

Income Protection

Few women have enough spare cash to pay for an "ideal" protection base of critical illness and Income Protection insurance. But many employees may already have protection as employers often give six to 12 months' pay to those on long-term sick leave. If your employer provides this, you can keep your premiums down by opting for a longer deferment period on your own policy. This will mean that payments on your individual policy will only start once your employer's cover finishes.

The most important piece of small print to check on an Income protection policy is whether it pays out if you are unable to do *any occupation*, or if it specifies that you can only claim when you can no longer carry out your *own occupation*. Any good financial adviser should point out the contracts that offer "own occupation" cover, as it is absolutely crucial only to buy cover that will pay up if you are forced to stop your own job.

Beware of contracts that only pay out if claimants are unable to pass three of six basic function tests (known as **activities of daily living**). The tasks include walking 200 meters, answering a telephone and taking a message, and writing legibly with a pen!

Such conditions make it hard to make a claim, even if you are genuinely unable to work.

Many insurers will only offer "own occupation" cover to those who are in low-risk, desk-bound jobs. Claims experience on income replacement contracts shows that the biggest groups of claims are for muscular-skeletal problems (often back problems, which tend to be suffered by manual workers) followed by anxiety-related conditions, including workplace stress.

Statistically women claim more frequently than men on Income Protection policies.

Insurance
What Should You Insure?

Your Assets

In essence, if you have assets that will be hard to replace without facing severe financial hardship, these assets should be insured. If you own a car, home, or other personal possessions , think about which of these are the most valuable. If these valuables were damaged or lost by accident or theft, would this lead to severe financial hardship? If so, you should purchase enough insurance to replace them.

Your health

Certainly you should look at insuring your health! Could you afford to lose it? If you become sick or disabled, temporarily or permanently, would you be able to support yourself?

How about your life? If you were to die suddenly, what kind of financial hardship would result? If there are people who can't afford to lose you, you should buy life insurance.

Home mortgage or vehicle loans

If you have a home mortgage or a vehicle loan, you have little choice but to buy insurance for these items. The lending institution will usually force you to get insurance and will dictate the coverage levels. In this case, it's not your financial hardship that lenders are nervous about; it's their own. You have their money, and if you can't pay them back, they'll want the house or car.

What insurances can I leave out?

Generally speaking, Mortgage life insurance, Insurance on outstanding credit card balances & Flight insurance.

These kinds of policies prey on fear, are not competitively priced and often have numerous exclusions. In most cases, the same coverage is built into your basic life and disability policies. If you've already set these up with reputable companies, there is no need to duplicate cover.

Insurance
Where to Purchase

The insurance market is extremely competitive. Today, you can buy insurance almost anywhere, especially simple products such as term life insurance.

Depending on the type of insurance you require, your options will include Internet websites; telephone numbers for direct insurance companies (those that don't work through agents); banks and brokerages. Of course, local agents are still an option - both independent (that represent a number of insurance companies) and representatives for a specific company.

Thanks to the Internet, you can access the latest facts and can enter the insurance transaction stage as a highly educated consumer.

Is price all that matters?

No. Remember, you buy insurance for times of need. You may hate to make the payments, but imagine how angry you'll be if, after making all the payments, you can't get paid out on a claim.
Aside from price there are three key issues to take note of:

Take out insurance with healthy companies. Check out the insurance company's financial ratings before buying. You can get these from Standard & Poors (www.standardandpoors.com).

Look for an efficient and speedy claims service. Low premiums are just the input side of the equation. If the output side is stingy and antagonistic, low premiums can be worse than no premiums.

Consider price and convenience. Many insurance companies will give you a great deal on premiums if you buy multiple policies from them.

Be diligent and shop around because premiums for the same cover can vary dramatically.

Insurance
Where to Purchase

When it comes to agents, premium payments, and company red tape, there are advantages to keeping things simple. If you've had good experiences with a particular company, be sure to check for multiple policy discounts and compare quotes accordingly. Many Banks, insurance companies & brokers offer significant discounts when you combine certain policies.

Whatever you do, don't lose your insurance bets by skipping premium payments. Since insurance has little impact on daily life, it is easy to overlook these premiums. Be diligent in paying your premiums.

Do not even think about an investment strategy until your dependants have sufficient insurance cover.

Investment

Investment

Savings and investment are very similar. With savings, you are putting away regular sums of money on a regular basis. Investment is generally understood to mean a lump sum.

When it comes to women and investing, one of the basic problems is the overwhelming choice of options.

There is an abundance of investment options available; stocks, Bonds, Mutual funds, options, exchange traded funds, real estate etc. Most of these investments have worthwhile value under certain circumstances.

The key is to establish your own individual circumstances and have a clear understanding of each option available to you. Only then can you start the elimination process and make an informed decision.

There are some key elements to investing. Whether you are investing a lump sum or saving regularly, these key elements are pertinent. Take time to consider these fully, before making any investment decisions.

Many women steer clear of investing because they cannot get the unbiased information they require to make an informed decision.

Investment

Key Elements to Investing

Your willingness to take risk

The term **risk** when related to investments is often misunderstood.

In fact the total loss of your money is not a realistic possibility for most of the investments that a private investor would be considering. Yet when asked, many women associate the word risk with the possibility of total loss. **Volatility** is probably a better word to use when describing the risks associated with investment.

The key question you must ask yourself is:
Can you live with volatility in the interests of longer-term growth potential?
If so, how much volatility can you accept?

If you cannot cope with volatility you must avoid higher risk investments. You may be sacrificing the potential for greater returns, but you will have peace of mind.

How much risk can you accept?

This is a very personal thing; but it is a factor within your control. You can choose to take no risk and keep everything in cash. Or at the other end of the risk spectrum you can choose an elaborate options strategy. Or you can choose something in between.

Most women are not speculators. They feel comfortable with lowering their risk by spreading their investments between different asset classes such as stocks, bonds, real estate & cash. This then reduces the overall exposure to any one asset class.

Risk is within your control and should be fully understood before selecting any investment

Investment

Understanding Risk

Taking excessive risk when looking for a big return is the number one reason why investors lose their money. They get too greedy! Alternately, taking no risk at all can mean no potential for real growth.

It is crucial to understand the trade-off between investment performance and risk. In order to pursue higher returns, you must be willing to assume additional risk. While stocks and real estate might offer higher long-term returns than fixed interest and cash, they also expose you to higher levels of risk, particularly in the short term.

Holding diversified investments (a mixture of investments) across all asset classes can moderate the overall risk of a portfolio. But, no matter how well diversified your portfolio; there is no way to eliminate risk.

Some important investment risks to consider are:

Inflation risk

Rising prices due to inflation can erode the real value, or purchasing power, of investments. Over long periods in the past, returns from stocks have beaten inflation by larger margins than fixed interest or cash investments.

If your investment earns 6%, but inflation is 4%, the actual or **real return** is only 2%. This risk is particularly relevant for cash investments where the possibility of negative real returns can be quite high.

Investment

Understanding Risk

Market risk

This is the risk that stock, real estate, fixed interest or cash markets will decline in value. The stock market is influenced by investors' changing expectations of the economy and individual companies.

The fixed interest market is influenced by expectations about interest rates and inflation. For example, during October 1987 the major stock markets dropped by around 40% and in the first half of 1994, the fixed interest markets dropped by about 6%

If you had invested in either of these asset classes during these periods, you are likely to have made a loss.

Currency risk

If you include international investments in your portfolio, fluctuations in the value of the various foreign currencies against your home currency, can seriously affect the return on your investment. This can either go in your favour or against you. For example:

Say you invested in British Telecom in pounds sterling and the pound grew against the US Dollar. Then you would benefit. If the value of sterling fell, then you would lose on the currency exchange.

A weaker home currency increases the value of foreign holdings, which will benefit the investor with international investments.

On the other hand, if the value of your domestic currency rises, the value of foreign assets falls.

While specific asset classes (types of investments) can be risky in the short term, time has a moderating effect on market risk. Holding a diversified portfolio of investments across different asset classes and different geographic regions can reduce market risk.

Investment

Understanding Risk

Political risk

Like changes in the value of a country's currency, political changes can also have an impact on the value of overseas investments. For instance, a change in economic policy, trade restrictions or the nationalization of industries can lead to market declines. As a result this will affect returns from overseas investments.

Credit risk

For funds that invest in fixed interest and debt securities there is a **credit risk**. This defines the possibility that an issuer will fail to repay interest and principal in a timely manner (also known as **default risk**). For example:

If a company such as Enron goes bankrupt the issuer (Enron) will fail. In a managed fund, credit risk is reduced because a number of different issuers are usually represented; so all your eggs are not in one corporate basket.

Investment

Understanding Risk

Manager risk

Manager risk is defined as the risk that the funds you have chosen will under perform due to bad choice of investments by the fund manager.

Knowing your personal risk tolerance is very important. This will help determine the range of assets (or **asset allocation**) you have in your portfolio.

We are all different and so there is a diverse spectrum of risk tolerance.

For example:

At the low risk end of the spectrum we could imagine a woman who only holds Cash and Term deposits in her portfolio.

At the high risk end of the spectrum we could imagine a woman who holds Bio technology stocks and options.

> Most of us will fall somewhere in the middle of the risk spectrum; with a diversified portfolio of cash, bonds, real estate and stocks.

Knowing your own risk tolerance can help you make informed decisions about the type of portfolio that will suit you. Everybody has a different attitude to risk.

Investment
Understanding Risk

Generally, as we get older we are more risk adverse. This means that if we do invest we are inclined to select minimal risk investments. Age matters because the longer the investing time frame the easier it is to overcome the effects of any investing mistakes.

As we get closer to retirement, we can not afford to lose the gains that we have made over the years. However, for a woman retiring at 60, she may live for another 25-30 years; so there is an argument that she should maintain at least some portion of her net worth in stocks.

The real trick is to know how much risk you can tolerate comfortably, and invest your portfolio accordingly. Evaluate risk wisely and keep high-risk investing to a smaller part of your portfolio.

The highest investing risk results from not doing your research. Each investment into direct stocks requires thorough homework, otherwise you are just gambling.

Reward

Reward is the potential return on an investment. Many investors only ever focus on Reward, when making their investment decisions. However; Reward is the only element completely out of our control! Therefore it is very dangerous to base any investment decision on the promise of reward alone.

Investment
Understanding Risk

Time

Establish a time scale that is appropriate for you. Your time horizon is crucial in determining the type of assets to include in your portfolio.

Time has a moderating influence on market risk. The longer you hold a quality investment, the more likely it is you will earn a positive return. In your 20's or 30's you have plenty of time before retiring. This long time horizon allows you to ride out short-term market downturns.

Generally the longer your investing time frame, the greater risk you can assume.

Remember though, time is an element you can control. You decide when you buy and when you sell a stock or fund. You decide when you start saving and when you take your money out.

Always be realistic about your time frame. Apply steady attention and effort regardless of what the markets are doing in the short-term.

Objectives

Before you start building your investment portfolio, you will need to determine what your investment objectives are and the time frame in which you will need to achieve them. In an ideal world, we would all want high consistent returns with zero volatility! However in reality, our objectives boil down to what we require from our investments - growth, income, or a bit of both?

A clearly defined investment objective helps provide the focus you will need to maintain your long-term investment strategy. Whether you are investing for the first time or reviewing your existing investments, clearly defined goals and time horizons will enable you to build an effective portfolio.

Investment

Understanding Risk

Cost

It is important to be aware of how much your investments cost to purchase, sell and to manage. If you buy a fund from a full service broker you could pay up to 4% front-end load (includes a commission to the broker).

On the other hand, if you are able to buy your funds direct, you will pay much lower fees. With the advent of internet (online) stock dealing services, you are able to buy and sell stocks and funds, more cheaply than before. But you must know what you are doing before you purchase this way. The costs of running your portfolio can make a huge difference to your eventual fund at the end of the day. High costs can chip away at the overall returns over time.

Reward, time, objectives and cost - all of these variables will have direct impact on the type of portfolio you can set up.

If you have a clear understanding of your risk/reward tolerance, time horizon, investment objectives and involved costs, then you are in a strong position to start constructing your portfolio.

Investment

Establishing Your Portfolio

Major Asset Classes - in brief

Before you can establish an appropriate portfolio of investments, you must understand the various **asset classes** (or categories of investment). It is also important to understand their levels of risk and performance trends.

Major asset classes include:

Cash

Cash securities generally provide a stable capital value and current income by way of interest payments. These are typically short term investments with a low risk of capital loss.

Fixed Interest (Bonds)

Governments, corporations and local government authorities issue fixed interest investments, also known as Bonds. Bonds typically offer higher returns (yields) than cash, but their value can fluctuate, if they are not held to maturity. When interest rates rise, bond prices fall and vice versa.

Real Estate

Investors can buy directly into an investment real estate, but this is an illiquid investment; meaning it's hard to sell quickly. For inclusion in an investment portfolio investors tend to buy real estate indirectly through companies or unit trusts that specialise in this area. Listed real estate stocks can be easily traded on the stock market.

Stocks

Stock investments give you part ownership in a company and, in some cases, a right to receive dividends from these companies. Stocks tend to be more volatile than the other asset classes. However, over time, they can provide higher long-term returns than fixed interest and cash.

Investment

Establishing Your Portfolio

A summary of the major asset classes.

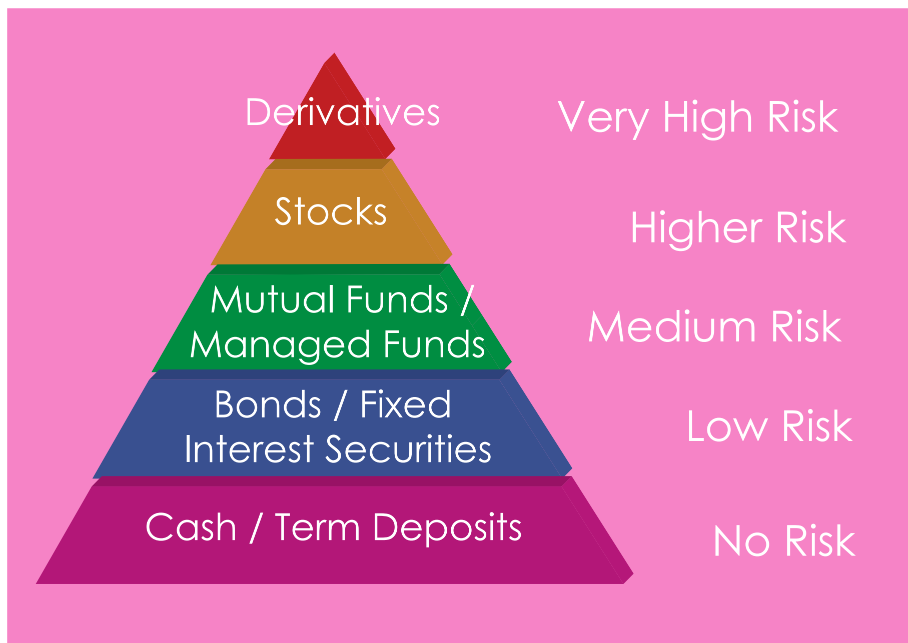
Asset Classes	Investment Time Frame	Perceived Risk	Type of Return	Type of investment
Cash market	Short term, usually up to a year	Low	Income, No Growth:	Money market trusts, bank deposits and short-term bank bills.
Fixed Interest (bonds)	Short to medium term Usually 3 to 5 years	Low to Medium	Income, some growth	Treasury notes, debentures, fixed interest trusts and mortgage trusts
Real estate	Long-term Usually 5 years or more	Medium to High	Income & Growth	Commercial office, hotel and retail listed real estate trusts
Stocks	Long-term Usually 5 years or more.	High.	Growth, Some Income	Stocks listed on domestic and international stock exchanges

Investment

Establishing Your Portfolio

The Investment Risk Pyramid

I find it helpful to be able to visualize the potential risk and rewards from different asset classes. Therefore I have created a risk pyramid, which may help to illustrate low risk investments (at the bottom of the pyramid) through to the higher risk investments at the apex of the pyramid.



We have just seen a summary of the major asset classes. However it is important to fully understand each type. Let's now have a detailed look at each asset class.

Investment

Major Asset Classes - in detail

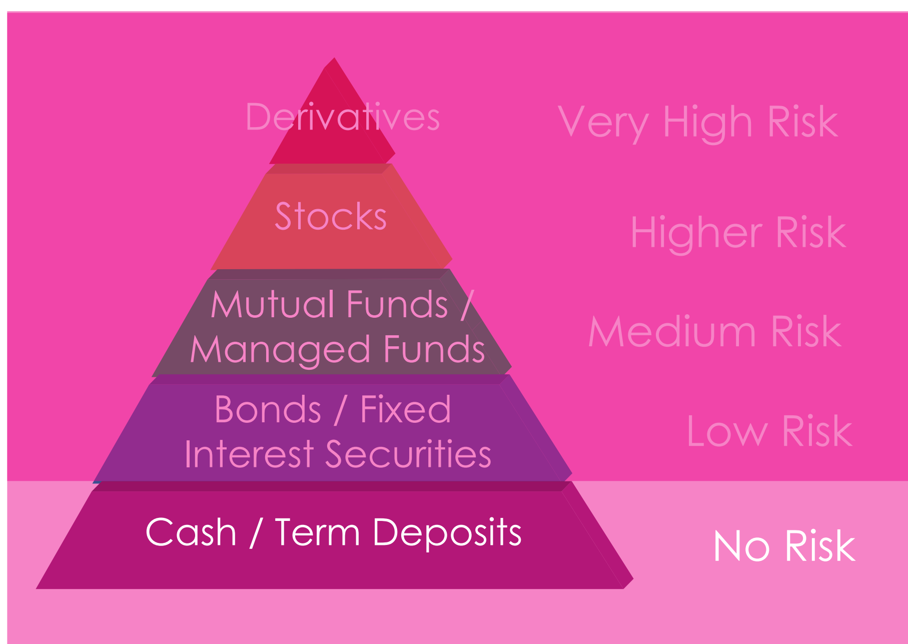
Cash Buffer/Emergency Funds

With any investment strategy, a healthy Cash fund should be established before any other investments are selected. Cash can provide a solid, safe foundation for your portfolio; but this security comes at a price. It usually offers only slightly better returns than inflation.

You must have contingency funds set up for life's unexpected disasters. This is wise, as then you do not have to sell your longer-term investments at a time that is not be appropriate or advantageous to you.

Then if disaster strikes, it is a lot easier to focus on the matter at hand. Whether it is getting a new job, recovering from illness, or mending the roof, you won’t be as worried about how you're going to pay your bills. This is particularly important if you have a mortgage.

However, be warned! Do not take a big wad of money and let it collect dust in a savings account, or in a box under your bed!



Investment

Major Asset Classes - in detail

In a long-term portfolio you do not want to keep a high percentage in cash. Inflation will erode the real purchasing power of your money. In fact many women have found that they have outlived their cash nest eggs!

Consensus varies as to how much of a cash buffer you should maintain. Generally speaking I would aim to save a minimum of three months' worth of expenses for emergencies, preferably six months.

Put your money into a liquid, interest-bearing account such as a **money-market account.**

Money-market accounts

Money market deposit accounts are offered by Banks. They usually require a relatively low minimum balance. They also offer investors a limited number of transactions, without suffering a penalty.

Money market deposit accounts are safe; you get a better rate of interest than on your working/cheque account and the money is very liquid. This is important to remember because your cash buffer needs to be readily accessible should circumstances dictate.

Alternatively you may wish to consider a **money market fund**.

Money market funds

Money market funds are offered by brokerages and Unit Trust groups. These funds invest in highly liquid, safe securities such as short term government securities and commercial paper (short term obligations issued by corporations).

Typically, the returns on money market funds are better than on a money market account. Your money is readily available should you need it quickly. However, these are funds they are not absolutely safe because they are not backed by government guarantees.

Investment
Major Asset Classes - in detail

Term deposits

Term deposits are debt instruments with a specific maturity, which can be anywhere from 3 - 60 months. They are mostly offered by Banks, but some brokerages now offer them too. Whilst term deposits will pay a better rate of interest than the money market account (around 5% at the time of writing) your money is tied up for the specified time. **Term Deposits** are fine for keeping a cash element in your investment portfolio, but avoid being tempted by using a term deposit as your cash buffer.

The whole idea of having an emergency fund is that it is readily accessible. Online high interest accounts can be used for this purpose and typically pay around 4% (at the time of writing). Do not expect to get rich on this portion of your money. Accept that it is there in case of emergencies. If and when you need to dip into your emergency fund, do not forget to replenish the fund as soon as possible!

Remember that emergencies DO crop up, so it's a good idea to have a cash buffer of some size at all times.

Investment

Major Asset Classes - in detail

Bonds/Fixed Interest Securities

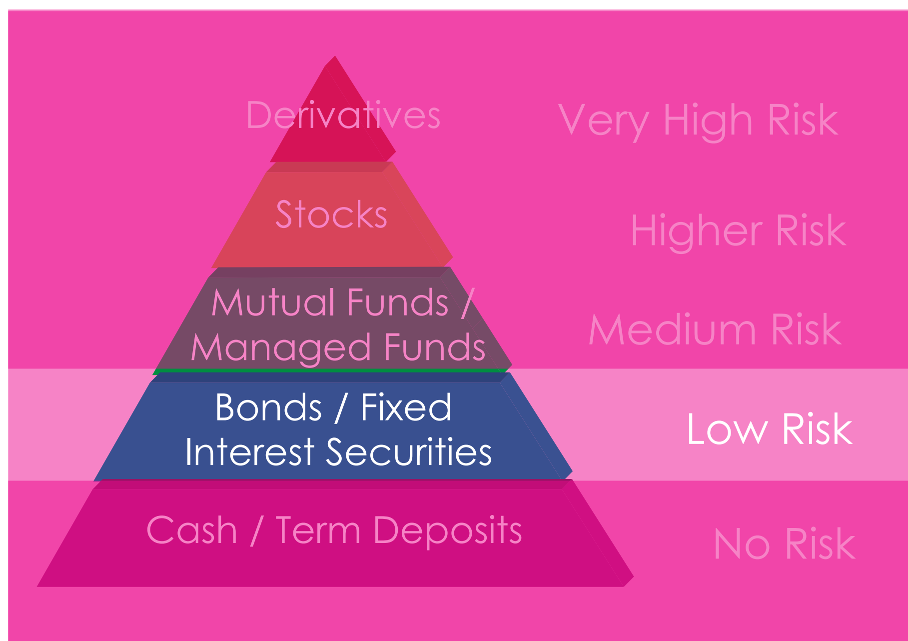
This is an asset class that is often overlooked. Many investors are confused about what Bonds are and the terminology involved. When the Stock market goes into turmoil it re-emphasizes the need for diversification and asset protection.

Bonds/Fixed Interest Securities can provide some much needed stability in a portfolio, so it is worth spending some time on familiarising yourself with them.

What is a Bond?

In essence Bonds are IOUs issued by a Government or corporation in exchange for Cash. They are debt instruments issued in order to raise capital for the government or the corporation involved. They are **tradeable loans**. Investors in a Bond expect to have their original capital repaid in full at the maturity date.

Bonds are issued as an alternative to borrowing from Banks. Each Bond is identified by the name of the issuer, the coupon and the redemption date. Fear not! I will explain these terms shortly.



Investment

Major Asset Classes - in detail

Bond prices and yields

A Bond can be bought and sold at any time. Its face value or **nominal value**, will remain the same, but the price at which it can be bought and sold will vary with market demand.

Essentially the issuer of a Bond agrees to pay a fixed interest rate on the money borrowed. That fixed interest rate is known as the **coupon** and is paid either annually or bi-annually.

The word *coupon* dates from the era when interest payments on a bond were redeemed by actually detaching a coupon from the Bond certificate.

The coupon quoted on each Bond represents the level of income paid as a percentage of its fixed face value. If the price of the Bond rises above this fixed face value, the running yield will be lower than the coupon. Similarly, if the price falls, the running yield will be higher than the coupon.

The current running yield provides investors with an indication of the level of income that a Bond is generating. Prices and yield affect the amount of income an investor receives from a bond.

Investment

Major Asset Classes - in detail

Factors affecting Bond prices and yields

The demand for Bonds is influenced by changes in inflation and interest rates or the issuing company's performance. If interest rates fall then a bond with a higher fixed rate of interest will look attractive. Demand for the Bond will increase and therefore the price will rise.

With **Corporate Bonds**, a company's performance can affect its Bond price. If a company improves its performance and looks more likely to honour its debt, its Bond could be assigned a higher credit rating. This will make it more attractive to buyers and its price could rise.

The credit rating also affects its yield. Corporate Bonds that have a lower credit rating offer higher incomes to compensate investors for the extra risk.

Bonds can provide a reliable fixed income and return your original investment at maturity. However; the market price of a Bond will fluctuate during the course of its life, reflecting shifting market expectations for the future course of interest rates. The further away a Bond is from its maturity date, the more volatile its price will be. It is growth, inflation and interest rate expectations that drive Bond prices, not a change in interest rates.

Maturities

Bonds are issued with a fixed life span, which is called its **maturity**. The date when a Bond ends its life is termed the **redemption date**. Bonds with less than 5 years left to maturity are referred to as **Short Dated Bonds**. Bonds with 5-15 years left are **Medium Dated**. Those with over 15 years left to maturity are called **Long Dated Bonds**.

Investment

Major Asset Classes - in detail

Main types of bonds

1) Government backed securities

These are also known as **Treasury Bonds** (or GILTS in the UK) and are the safest type of Bond, because they are debt instruments backed by the Government.

2) Index Linked Bonds

These are also issued by the Government. The interest payments and the amount repaid at maturity are adjusted in line with inflation. In a low inflation environment, index linked Bonds are not as attractive as conventional Treasuries, but when inflation is on the rise they can be a good buy.

3) Corporate Bonds

These are debt instruments issued by large companies with a good credit track record. These are known as **investment grade bonds**.

4) High Yield Bonds

These are issued by companies that have a lesser known track record and need to tempt investors with higher rates to compensate for the increased risk of default.

Bond ratings range from AAA to D, and act like corporate score cards to help investors gauge risk. Bonds rated BBB or higher by Standard & Poor's are termed **investment grade** and are regarded as the safest Bonds for those requiring income. Bonds rated BB+ or lower are referred to as **high yield** or **junk bonds**.

Standard & Poor's, Moody's and Fitch are the three main agencies that give corporate Bonds their credit ratings.

Bond funds

Bonds can be bought directly from issuers (e.g.GE Microsoft, Exxon). However, most investors opt for a **Bond Unit Trust Fund**.

Bond Mutual Funds offer a spread of different bonds managed by a professional fund manager. Because Bonds are traded on the open market, the income you receive from these funds will vary. The value of your capital can also fluctuate.

What affects the underlying capital of an investment in a Bond Fund?

The capital value of a Bond investment will increase in value if the price of the Bonds in the portfolio rises.

There are several factors, which can cause price fluctuations, which are either economic influences or relate to the type of Bonds held in the fund portfolio:

If inflation is high, the fixed income paid by Bonds will not be able to keep up, so investors will tend to shun them. Bond prices generally fall when inflation is rising and increase when inflation is falling.

Low interest rates make cash investments less attractive. Bonds that pay a higher interest rate than Banks become more attractive; so prices rise. The reverse occurs when interest rates rise.

Investment

Major Asset Classes - in detail

When are Bonds appropriate?

Bonds should be part of any well-balanced portfolio. However, the percentage you hold in Bonds will depend on your risk profile, your age and the amount of income you require. Bonds can be especially useful if you are nearing retirement and want to protect your investments from falls in the Stock market. They can provide a steady stream of income, with less volatility than stocks.

Unlike cash, actively managed Bond funds can offer the potential for real growth, and therefore a rising income over time.

Bonds are low risk but not risk free, unless you buy them on their first day of issue and hold them to maturity.

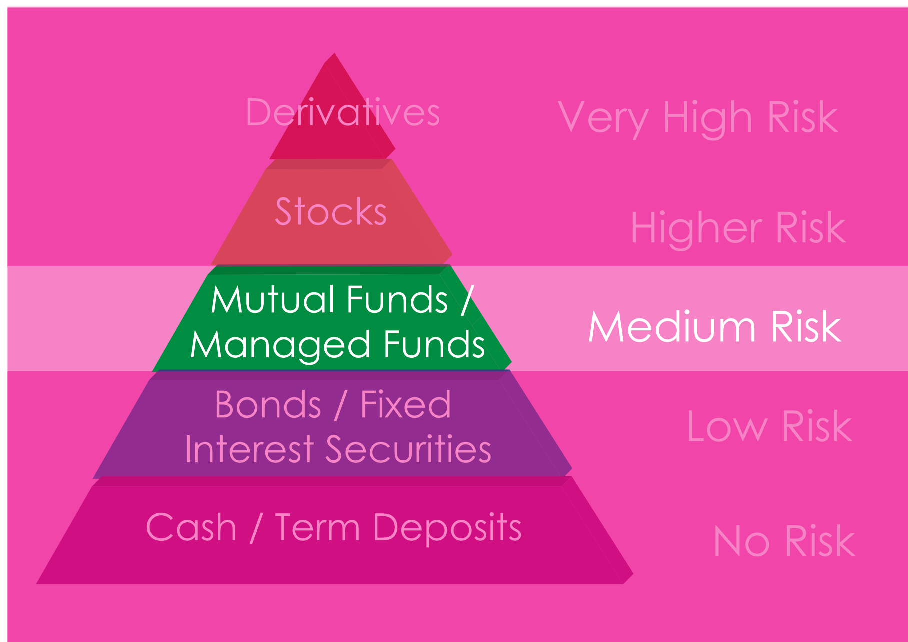
Investment

Major Asset Classes - in detail

Real estate investment

Real estate has a valid place in any diversified portfolio. There are two main ways to gain exposure to the real estate market:

- Directly, by purchasing an investment real estate, and
- Indirectly, by investing via a real estate fund or trust.



Investment

Major Asset Classes - in detail

Direct Investment: purchasing an investment real estate

Like buying a home to live in, buying a real estate to rent out, and selling for a profit eventually, the idea of an investment real estate is an easy concept to grasp. It is not as abstract as the concept of bonds, stocks or derivatives.

It is a simple idea to grasp, and I am sure this has helped explain it's great popularity as an investment.

Data compiled over the years has shown residential real estate as a steady performer over time. However, you must be aware that growth in real estate prices does not occur smoothly over time.

However, residential real estate investment is not this straightforward. Direct investment in real estate normally requires greater care, is more complex and has more pitfalls than any of the other main asset classes.

At the time of writing this e-book we are experiencing a slump in house prices. A relatively common pattern includes a price surge for a couple of years, followed by a price fall. This is then followed by a period of stagnation and/or modest price growth lasting 4-5 years.

The general consensus in real estate circles is that residential real estate works in 7-8 year cycles. So, as with most of the other asset classes, **real estate investment should be viewed as a longer-term investment.**

Investment in real estate is different from other asset classes. With stocks and Bonds you pay your money and then sit back and wait for the investment to start producing gains and/or income. With real estate it is a different story. You hand over money, and then you hand over some more and some more. Just like your main home, a real estate investment requires ongoing expenses.

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Major Asset Classes - in detail

There are substantial transaction costs associated with buying and selling residential real estate. These transaction costs can run into thousands, and so must be factored into the equation. The rental you charge tenants should more than cover these ongoing expenses. For most real estate investors, however, the biggest cost is interest on the loan.

Generally speaking in the initial years net rentals will not cover your interest costs. There can also be times when your real estate may be vacant and not producing steady income. This is something you must be aware of.

For this reason, it is very important that your other sources of income are secure. It is a good idea to produce a cash flow analysis on the real estate before you buy it. A personal computer spread sheet is ideal for this. The cash flow analysis will indicate when you can expect to move into a cash surplus, as the income you receive via your rental outweighs your expenses.

With a cash flow analysis you will be going into the purchase with a clear picture of expenditure versus income. You will also be able to rationally answer the question "can I afford to fund this investment?" Your earnings projections will help to illustrate just how important capital growth (the increase in value of the real estate is) is to the viability of a real estate investment.

Successful real estate investment is absolutely dependent on good rates of capital growth.

Investment

Major Asset Classes - in detail

The impact of gearing

Most people will buy an investment real estate with borrowed funds. There is nothing wrong with that. However, it is important to realise that this is **gearing**.

Gearing is the act of borrowing money to invest. It enables you to increase your stake in an asset over and above what you could afford out of your own savings. This in turn increases the amount of return you will receive on that said investment. This may be a positive or negative return. The more you borrow, the higher your risk.

You should exercise great caution when borrowing to devote to an investment real estate. You must be sure that the asset will show positive returns. If your investment real estate fails to do this you will simply magnify your losses.

Location, location, location

It is well known that location is the all-important factor when buying real estate. In the past decade a trend has shown areas close to city centres are showing stronger price growth, as opposed to properties further out.

In many cities the oldest, closest and mostly run-down suburbs have been put through a process of renovation. This process is known as **gentrification**, which involves transforming low-value areas to high-value ones. Urban renewal of this type tends to spread out in concentric circles from the centre of the city.

In general it is best to buy a real estate that:

- Is close to the city centre
- Is in an area where gentrification is underway or is likely to be soon
- Is aesthetically pleasing or at least has potential to be
- Has a unique or rare positive characteristic.

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Major Asset Classes - in detail

If your foresight is good and you buy into an area, just before gentrification takes off, your real estate will show very good capital returns. But be aware of the risks.

Some areas take a long time before they become popular and in some areas it may not happen at all. These include places where there has been haphazard industrial development, often accompanied by high levels of air and noise pollution. You find such areas in all cities.

The longer a real estate sits around effectively doing nothing, the less money you are making. And if you have borrowed to buy you will actually be losing money while the real estate stagnates.

So what sort of individual real estate is likely to produce the best investment returns, both in terms of capital (price) and income (rental) growth?

An answer begins to emerge if you look at the changing demographic patterns and use this as the basis for your real estate decisions.

Consider this:

The largest demographic grouping, the post-war baby boomers (born between 1945 and the early 6os), are now moving into middle and older age.

Due to a number of factors the aging baby boomers will remain the largest demographic grouping for many years.

In the developed countries, this means that, overall the population is aging, and older people have different housing requirements to younger people.

Increasingly, baby boomers will sell their large suburban houses and move to smaller dwellings such as townhouses closer to the city or to coastal retirement enclaves.

Without a family to feed, these baby boomers or 'empty nesters' will have few or no debts and possibly a pension pay-out. Many will be able to afford to move more or less where they please.

Often, the dwellings baby boomers will move into will be:

- low-maintenance (little or no gardens),
- made of good quality materials,
- Well appointed and well positioned.

Bay boomers will want:

- as few stairs as possible,
- good security,
- ample parking and storage,
- proximity to all amenities, and
- preferably a level stroll to shops and transport.

They will also prefer localities that are attractive, as well as clean, quiet and safe.

So if you want to buy an investment residential real estate, then buy something that fits these parameters, and you will not go far wrong.

Capital Gains Tax (CGT)

The impact of Capital Gains Tax (CGT) on your overall real estate investment returns can be very significant. It is vital you understand the effect and operation of Capital Gains Tax before you invest.

Capital Gains Tax is complicated and varies from country to country. All potential real estate investors should check out the implications of Capital Gains Tax with an accountant before making any purchase.

Investment

Major Asset Classes - in detail

What will diminish your Real Estate investment return?

These factors will reduce your real estate investment returns:

- Buying real estate in a poor location
- Buying real estate in an area showing below average growth
- Buying real estate in poor structural condition with high maintenance costs
- Buying real estate with no aesthetic appeal or no potential
- Buying at the top of the market
- Paying too much
- Selling at the bottom of the market
- Overcapitalising
- Inadequate maintenance
- Bad tenants
- Excessive vacancy
- Being a bad landlady
- Inadequate planning for capital gains, land and provisional taxes rising
- Interest rates
- General economic malaise with low rates of growth
- Nearby construction of a major road or factory
- Inadequate insurance to cover any real estate damage such as fire, or to cover

- Any claims for damages brought by tenants or neighbours for which you may be legally liable.
- Ineligibility for depreciation allowances (i.e.: the real estate doesn't qualify for depreciation deductions.
- Poor record keeping, poor bookkeeping and poor overall control of costs

What will enhance your investment return?

These factors will increase your return:

- Buying a real estate with good position in a strongly performing area
- Buying an aesthetically pleasing real estate or with potential
- Buying a real estate with appeal to aging baby boomers
- Buying a real estate that has a unique, positive feature
- Buying a real estate in good structural order
- Buying at or near the bottom of the market
- Paying a fair price
- Selling at the top or near the top of the market
- A real estate rezoning in your favour. For example, permission to subdivide a large block of land into two separate blocks, or to convert an old block of flats to fashionable units
- Low maintenance and other running costs

Good tenants on long-term leases

- Low vacancy
- Being a good landlady
- An appropriate degree of sympathetic renovation
- Low interest rates
- A healthy economy with strong rates of growth
- Proper maintenance
- Adequate insurance cover
- Sufficient planning for taxes
- Eligibility for depreciation allowances
- Good records, good bookkeeping, good accountancy and good overall control of costs.

Commercial Real Estate

This is a major investment sector and has been the source of extraordinary wealth for some people. But for the small investor it is not a traditional area of direct investment.

That's not because it's a second-rate investment. It's because commercial real estate is too specialised, too expensive and often too difficult an area of investment for most people. If you thought residential real estate investment sounded involved it's nothing compared with commercial!

Indirect investment: Real Estate Mutual Funds

For many small investors a less expensive and hassle free way of gaining exposure to the real estate market is to buy indirectly via a **real estate trust**.

When you buy into a mutual fund, you effectively become a part owner of the underlying assets held by the fund. These would typically include shopping malls, office blocks, industrial properties, residential estates, hotels and apartment buildings.

A minimum investment of around $1,000 is all that is required, so it is a lot less expensive than buying directly into an investment real estate. Also the units or stocks you hold in the fund can be sold on the stock market quickly. The investment is much more 'liquid' than if you have it directly invested in bricks and mortar.

What are Real Estate Investment Trusts (REITs)?

Real Estate Investment Trusts, or REITs, are big business in the U.S.A, where there are over 300 publicly traded on the stock exchange. They have assets in excess of $300 Billion!

REITs are listed companies that own and manage real estate, including apartment buildings, offices, shopping centres, industrial buildings, and hotels.

These trust funds invest primarily in stocks of REIT stocks. Unlike corporations, REITs don't have to pay income taxes, if they meet certain Internal Revenue Code requirements. To qualify, a REIT must distribute at least 90% of its taxable income to its stockholders and receive at least 75% of its gross income from rents or mortgage interest.

Investment

Major Asset Classes - in detail

The benefits of real estate funds

Funds that invest in listed real estate offer investors an opportunity to gain exposure to the real estate market with greater liquidity and diversification than direct ownership of real estate. **Real Estate Index Funds** can be an excellent way to achieve diversification within the real estate sector.

Owning real estate *directly* can be costly. It requires ongoing management and maintenance, and it can be difficult to convert the real estate into cash when needed.

Real estate funds tend to offer higher dividend yields than other types of stock funds. But keep in mind that real estate fund prices will fluctuate, like any stock fund. During periods of high interest rates, real estate funds may lose their appeal to investors who could obtain higher yields from other income-producing investments; such as long-term bond funds.

It is important to remember that, as with any investment in real estate, a real estate fund's performance depends on several factors. These include its ability to find tenants for its properties, to renew leases, and to finance real estate purchases and renovations.

The risks with real estate funds

Real estate industry risk: The chance that real estate stock prices will decline because of adverse developments affecting the real estate industry and real real estate values.

In general, real estate values can be affected by a variety of factors, including supply and demand for properties, the economic health of the country or of different regions, and the strength of specific industries that rent properties.

Investment style risk: The chance that returns from real estate funds (which typically invest in small- or mid-capitalization stocks) could under perform compared to the stock market.

Interest rate risk: The chance that fluctuating interest rates may affect real estate values or make real estate funds less attractive than other income-producing investments.

Who should invest in real estate funds?

Real estate funds received a lot of attention in the years between 2000-2002. This is particularly due to the fact that they had outperformed the stock markets during that time and their yields were higher than those of many bond funds.

Be warned - it is not always a good idea to chase the ‘best-performing’ market sector or asset class. Chances are that you will buy right before the sector or asset class begins to drop. Unfortunately, there will be many women sitting on losses from real estate funds over the last year.

Real estate funds are generally appropriate if you are seeking to add real estate exposure to your long-term mix of stock, bond, and money market funds.

Real estate funds have a unique nature and can add diversification to an investment portfolio. As real estate is not so linked to the stock market, it often can move in the opposite direction. So if the stock market is down the real estate market could be going up. At the moment however, both are down!

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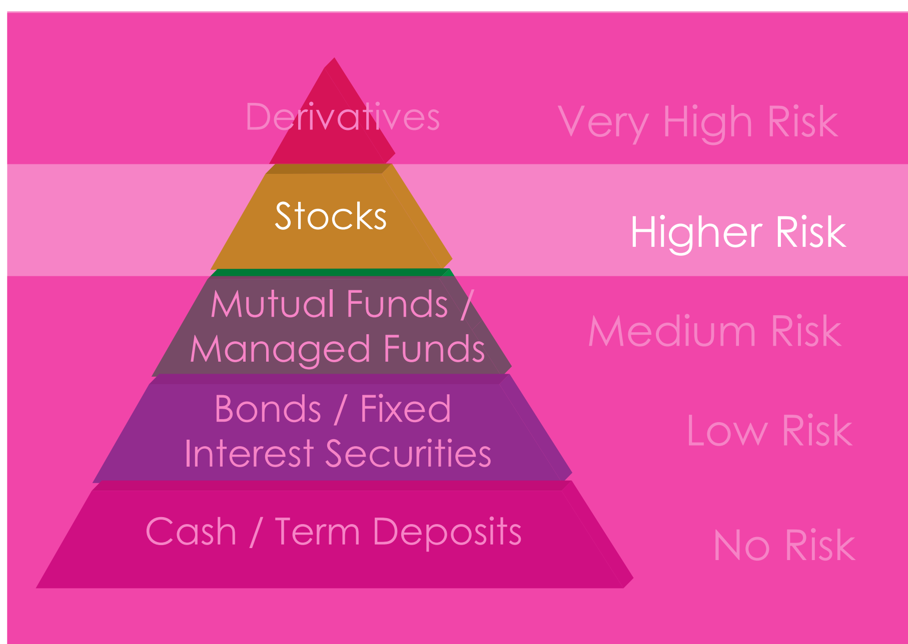
Major Asset Classes - in detail

Stocks

If you are interested in saving for the long term, and want the potential of higher returns, then you should look at investing in **stocks**.



What is a stock?

A stock is a part-ownership of a company listed on the stock market. So when you buy stock you become a part owner (or **stock-holder**) of that company. You take **equity** in it; which is why stocks are also known as **equities**.

Stocks are issued by companies to raise money. When you buy stocks in a company you stock in its profits by means of **dividend distributions**. A **dividend** is a term to describe the payment made by a company to its stockholders.

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Major Asset Classes - in detail

If the company doesn't make a profit you won't receive dividends. As an owner, you are also entitled to a stock of the company's assets if that company goes bankrupt. You are also invited to stockholders' meetings.

Ordinary stocks are the most popular. These are issued by thousands of companies around the world. Ordinary stocks entitle you to any dividends that may be paid and to participate in rights and bonus issues.

Preference stocks

Preference stocks differ from ordinary stocks in that they normally pay a *fixed dividend*. This can work to your advantage if the company is performing badly and paying little or no dividend to ordinary stockholders. On the other hand when the company is doing well, a fixed dividend will be a disadvantage to you.

In the event of a company going bankrupt, preference stockholders are paid out before ordinary stockholders.

There are many types of preference stocks and because of their relative sophistication; they are not usually the first choice for novice investors.

Returns from stocks come in two forms: **dividends** and **capital gains**.

Dividends

As a stockholder, you receive a dividend (an income stream),which is paid either bi-annually or annually. The amount of your **dividend** will depend on how many stocks you hold and what proportion of the company's profits the directors choose to distribute to stockholders. Companies are not obliged to pay dividends although most leading companies do. Many companies make it their policy to grow their dividends on an annual basis.

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Major Asset Classes - in detail

In a rational market, dividends offer investors the promise of a regular payment as reward for holding the company's stock. For years the dividend payout was key when considering **stocks** or **equities**.

In recent times dividends were pushed aside in favour of a rather less reliable promise of greater **capital appreciation**. Thankfully common sense has prevailed and investors are once more demanding regular dividends.

But is the smartest move simply to seek out the highest-yielding stocks? Absolutely not! In situations where dividends are set by an income-based formula and not a board (such as trusts), these yields can fluctuate wildly. As such what you see is not necessarily what you get.

Be warned!
High dividend payers do not always equal better stocks

For example:

Imagine you have purchased 100 company stocks (at $10 per stock), and this company pays a 15% dividend.

The equation to calculate dividend is:

(Number of Stocks)*(X %)*(Market Price or Par Value) = Total Dividends.

Therefore you would receive:

(100)*(15%)*($10) =$150. On an investment of $1,000

The stock price needs only to fall to $8.50 before the dividend is neutralized by **capital loss**. (I.e. amount by which the purchase price outweighs the selling price)

You would still receive your dividends of $150 BUT your stocks would only now be worth $850

If a company is paying a big yield/dividend relative to their peer group, there is often something amiss.

Be suspicious - companies with very high yields are being discounted by the market for something!

Reasons behind this can include:

- A loss of confidence in the future of the company (i.e.: WorldCom, before it went bankrupt, offered a dividend yield in excess of 60%!)
- The dividend is itself at risk (AMP recently reduced its dividend due to the adverse effects of the credit crisis on its business).
- The payout ratio (dividend as a function of net income) is too high
- The company has experienced a high-risk event such as a lawsuit, loss of contract, or loss of prime customer.

Generally the big blue chip companies will pay a moderate dividend as well as giving you the potential for capital gains.

Capital gains

Another return from stocks you can receive is **capital gains**. Capital gains is the amount by which a stock's selling price exceeds its original purchase price.

As you may know stocks are traded on the stock market and can both fall and rise in value. So if you buy stocks and then later sell them at a higher price, you have made a profit. That profit is **capital gains**.

Some degree of **capital growth** can also occur through **rights issues;** although this does involve investing more money. A rights issue is when a company invites its stockholders to purchase new stocks at a discount to the current market price.

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Major Asset Classes - in detail

Why do stocks fall and rise in value?

Many factors influence the price of individual stocks. For example, the stock market is generally influenced by 'big-picture' factors such as the state of the economy, inflation and interest rates. If the economy is doing well, and people believe companies quoted on the stock market will deliver bigger profits and bigger dividends, then usually the stock market will rise

On the other hand, if factors such as the credit crunch are forcing the economy into recession, then stock markets can fall. This is why we are seeing increased volatility in the stock market at the moment.

Geo-political events can also impact on stock markets. Adverse events such as economic turmoil or war, can cause a crisis of confidence, leading to sharp stock market decline.

The price of individual company stocks can also be influenced by micro factors such as how the company is faring in the economy, against competitors and its future prospects. If these factors look favourable, investors will want to buy that company's stocks which consequently lead the stock price to increase. Conversely, the more people want to sell a company's stocks, the further that company's stock price will fall.

It is proven that over the long term stocks outperform other classes of financial assets such as deposits and bonds. Over the last 10 years equity (or stock) markets have returned, on average, around 10.7% per annum

Investment

Major Asset Classes - in detail

How to value a company or stock

There is a variety of formulas and tools available for valuing a stock. However, what should be fair value for a company or stock is not always what the market will pay for that stock.

A simple rule of thumb would be to look at the following essential security features to test a likely stock before you buy it:

The P/E ratio

The P/E ratio (price/earnings ratio) is the most widely used comparative measure of the value of a stock. All things being equal, a stock on a ratio of seven is cheaper than one on a ratio of 30. If the stock is already rated on a low P/E, it is less likely to fall than a highly rated stock; particularly if earnings expectations fall only slightly short.

High P/E stocks are frequently decimated for a tiny under-performance in earnings. This is not so with low P/E stocks. As they are already low rated no-one expects too much.

Over the longer term, the case for equities is even more compelling. Annual returns from equities over the past 50 years has convincingly outweighed returns from bonds and cash. Over the long term, stocks can enhance your wealth.

Yield

Yield is the cash dividend income to be expected for holding the stock. The yield can give you some compensation whilst waiting for a value stock to perform. With interest rates at all time lows, most yields are paying as much as, if not more, than money on deposit. This means you get more from dividend yields than interest from bank accounts. Therefore, you have received the dividends, even if the stock price of the company does not increase) And if it does perform then a good yield is a bonus.

High yield is an accurate indicator of value and is used in many mechanical investing strategies. It helps to protect the stock from falls because this will only drive the yield higher; assuming the dividend is secure.

A secure high yield is attractive to income investors.

So remember – seek out companies with no debt or low debt levels.

Market capitalisation

This is another security feature to pay attention to.

Market capitalisation should be over $100m. Companies with smaller capitalisations are less predictable. It is generally harder to find published forecasts for such companies and fewer institutions will take a stake in their stocks.

4 main ways to buy stocks

There are four main ways to buy stocks:

1) Through a Stockbroker

If you want advice on what stocks to buy, you can use a stockbroker. They will recommend stocks that they feel meet your investment objectives. However, charges can be expensive and you will probably need a relatively large lump sum to begin with.

Stockbroker advice tends to take two forms. There is the **discretionary service** where you grant full power to your stockbroker to buy and sell stocks on your behalf. This is after you have laid down your investment requirements. Then there is an **advisory service** where the stockbroker will provide advice on specific stocks but the decision as to whether to buy and sell is left entirely to you.

2) Through a Bank

Your bank may provide a stock-dealing service; although it is unlikely that you will be given investment advice. These services are generally limited and more costly. However, they are convenient for people who only want to make occasional stock transactions.

3) Through an Execution-Only Stockbroker

In this scenario you receive no advice; just the facility to buy and sell stocks. Most of these services are run via the post or telephone and are usually inexpensive.

4) Via the Internet

This is becoming an increasingly popular way to buy and sell stocks. You need to set up an account before trading, but once done costs can be very competitive. In the US , Etrade, Ameritrade, Charles Schwab specialises in internet stock dealing.

Stock indices

Stock exchanges all over the World developed **indices** as a fast way of monitoring particular markets. An **index** reflects a change in the value of a sample selection of stocks in a single market or a sample selection of markets.

On the day an index is created, that particular day is given a **base value** (say 1,000). Any changes in the market direction are measured in relation to that base value.

Each stock exchange has a main index that represents the market as a whole. The most commonly quoted are New York's Dow Jones Industrial Average, London's FTSE 100 index, Tokyo's Nikkei Index, Hong Kong's Hang Seng Index, Australia's ASX index, Germany's DAX index and France's CAC index.

There are countless indices in existence and more are being developed. As long as you know what they are measuring, they are a useful, at a glance tool, to indicate which direction a market is moving in.

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Major Asset Classes - in detail

Managed funds

The term **managed fund** (or investment fund) is a generic term covering a range of related investment products including balanced funds, listed or unlisted real estate trusts, pooled pension trusts, insurance company savings bonds and some annuities. Although all are structured differently and may have varying taxation treatments, they have basic similarities.

A managed fund is a vehicle where the investments of a large number of smaller investors are pooled together and managed as one large investment portfolio by a professional investment manager.

Managed funds can invest in stocks, cash, real estate or fixed interest securities. They can invest in these assets directly or indirectly via other managed funds.

Managed funds can specialise in all sorts of assets; be they domestic or international, from any other region or mix of regions. They can also invest in infrastructure, alternative energy, forest plantations and feature films. In fact, the mix and type of assets you can invest in is limited only by the imagination of those offering them.

Investors in a managed fund are effectively part-owners of the assets held by the fund. Earnings generated by the fund's assets can be distributed as income to investors on a regular basis (monthly, quarterly or six monthly). Alternatively, generated earnings can go towards increasing the capital value of the investors' units. This capital appreciation (designated by an increase in unit price) is realised when the units are sold by the investor.

Most managed funds require minimum initial investments in the fund, minimum additional deposits and minimum balances. As a general guide, an average minimum investment would be around $1,000 (as a lump sum) and $100 per month as a regular premium.

Investment

Major Asset Classes - in detail

If you have read the previous sections on real estate, stocks and fixed interest you'll know that each of these asset classes satisfies certain **investment objectives.** You will also understand that your short, medium and long-term needs and goals should determine what proportion of each you hold in your portfolio. For example:

If long-term capital growth is your goal you should bias or 'weight' your portfolio towards stocks and real estate.

If you need regular income and security you should weight your portfolio towards cash and fixed interest.

If you want both growth and income then you should have an even spread of investments across all these assets.

If it all sounds like too much hard work, don't worry. There is an easy way around the difficulties, namely, investing in professionally managed investment funds. These are called **mutual funds**.

The idea behind **mutual funds** is simple. You employ investment professionals to do some or all of the work involved in creating and managing an investment portfolio for you. They charge a fee for this service but, in return, they save you the time and effort involved in selecting and monitoring stock performance.

Theoretically, investment professionals should also be able to generate better returns than you as they're the professionals with their ‘fingers on the pulse’. Whether managed investments are right for you will depend on the level of control you want over the investment selection process.

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Major Asset Classes - in detail

How much involvement do you want to have in your portfolio's ongoing management?

If you have the confidence and time to manage your own investments and are reluctant to delegate this responsibility, that is fine. That is a perfectly acceptable way of managing your affairs, particularly if you have market experience.

However, if you have limited time, limited investment experience, and limited confidence in your ability, investing through managed funds is a sensible way to go. Managed funds are a popular investment strategy throughout the world, with billions of dollars, pounds and Euros invested in them.

Fund managers and Professional trustees

A fund's investment manager is usually an experienced and reputable investment organisation such as AMP, Tower, Fidelity, or Rothschild.

The fund may also have a **professional trustee**.

Both fund managers and trustees charge investors a fee for their respective services. The role of the fund manager's job is to invest pooled monies in a range of assets. They have the right and responsibility to shift the fund's monies in and out of assets as they see fit and as changing market conditions dictate. The manager's objective is to achieve as high a sustainable return on the investors' pooled monies as possible within certain (usually conservative) risk limits.

The key features of the **trust deed** are included in any managed fund's **prospectus**.

The professional trustee does not get involved in the day-to-day management of the fund. Nor do they select the specific assets that the fund invests in; that is the responsibility of the fund manager. They are more concerned with the legal & compliance side of things.

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Major Asset Classes - in detail

Units

Managed funds are divided up into **units** of equal value. Like an ordinary stock, they give you a part ownership of assets. Although stocks and units are technically quite different, the concept is the same. In fact, some units, those of **listed trusts**, are traded on the Stock Exchange. In certain funds the number of units issued for sale is fixed, whereas in others new units are readily available.

In general, managed funds, such as Retirement savings plansfunds and insurance funds, are nearly always open, meaning you can increase your stake holding in them at any time.

Valuing units

Aside from listed trusts' units, which are priced on the stock market, other managed funds price their units at least weekly. The method of valuation must be done in strict accordance with the rules laid out in the **trust deed** (where one exists). Two values per unit are calculated; a value for buying units and another for selling them. This is commonly known as the **bid/offer spread**.

The difference between the two prices can be as high as 6%. This includes any commissions payable to a licensed adviser.

Liquidity

Liquidity defines the ease with which an asset can be converted into cash. Managed fund units vary significantly in their **liquidity**. For example, you can access your money in cash management funds fairly quickly. Converting units in an insurance bond to cash may take a few days.

Having said this, liquidity issues have occurred with real estate trusts, primarily due to the relative lack of liquidity of their underlying real estate assets. This is particularly relevant at the moment. If a managed fund is unlisted you can normally only buy and redeem units directly from the fund manager.

A new hybrid type of fund is gaining rapid popularity with traders and institutions, although many investors still seem unaware of them. I feel they are well worth taking a look at. They are called **Exchange Traded Funds**.

Exchange Traded Funds (ETFs)

Exchange traded funds (ETFs) are baskets of stocks that trade throughout the day as an individual stock, but allow investors to own a diversified portfolio. They have an advantage over traditional managed funds because investors do not have to wait until the end of the trading day to buy or sell. They are also good value, usually with cheaper management fees than index funds.

ETFs are hybrids that combine the characteristics of unit trusts and individual stocks. They have become a regular tool in the arsenal of traders. ETFs such as 'Spiders', 'Webs', 'Diamonds' and ‘Vipers’ are widely used by traders.

Globally, the amount invested in ETFs has risen to $162.5bn. ETFs are one of the few investments to have grown during the bear market. One exchange traded funds you may be familiar with is the **QQQ**, the NASDAQ 100; during the “dot-com bubble" of the 1990s big profits were made trading the QQQ.

So if you had purchased Q's stocks during the mania of the dot-com bubble, your portfolio would have been 100% ahead of two of the NASDAQ’s most recognised stocks – Dell and Microsoft. Of course, that was during the most furious trading for tech stocks.

Investment

Major Asset Classes - in detail

The sharp increase in the popularity of Exchange traded funds highlights the effect that volatility can have on a worried, but return-hungry investing public.

Instead of taking stock-specific risks you can also use ETFs to get sector or broad market exposure.

Financial institutions are finding more sophisticated uses for ETFs.. Imagine a fund manager wants to purchase financial services stocks, but has concerns about accounting issues. During the bull market, the manager might simply limit herself to buying a stock or two in that industry. But because of the concern around scandals and stock-specific risk the manager is less likely to do that. A simpler and safer way to gain exposure to the industry is through a **sector ETF**.

Exchange traded funds are fast becoming the best way to safely accumulate wealth in today's markets. They allow you to quickly and securely profit from ‘big-picture ideas’ by playing certain market sectors or industries.

The beauty of exchange traded funds is that you gain exposure to whole sectors of the market or industries, without owning the stocks outright. You have access to the diversity of a whole market or industry sector by trading just one exchange traded fund.

To date, there are over 100 different ETF's which focus on ultra-specific market segments. Whether it's the Oil Index, the Dow Jones Utility Average, the Asia 25 Index, the Health Care Sector, the Technology Index, the Gold Index, or even the SmallCap Index, the range of investment vehicles is limitless. New ETFs are coming onto the market regularly.

Take time to find out more about them. They could be just the ticket to add an instant shot of diversification into your portfolio!

Hedge funds

Exchange traded funds offer substantial investing variety in a cost efficient way and are hugely popular with those 'in the know'.

Growth within the hedge fund industry has been staggering. The industry is said to be worth over $300 billion and growing rapidly. Yet there is still a level of mystery surrounding them.

It is hard to define exactly what a hedge fund is, because they can employ just about any variety of investing strategies. They are alternative investment vehicles, which differ from your average unit trust.

Hedge funds can 'hedge' against downturns in the markets being traded, via flexible investment options such as **short selling**, **leverage**, derivatives such as **puts**, **calls** and **futures**.

Alternative investments such as hedge funds can offer the following benefits to your overall portfolio:

- A diversification away from long-only investment.
- Relatively low correlation to the movement of equity and bond markets.
- Significant capital protection in bear markets.
- Out-performance of markets over time but with significantly reduced volatility.

Faced with the huge diversity and lack of information about these funds, mainstream investors have tended to shy away from hedge funds. This is probably not a bad thing, as many have collapsed in the last few months.

Investment

Major Asset Classes - in detail

Derivatives

A **derivative** is a generic term for futures, options and swaps. They are all instruments derived from conventional direct dealings in stocks, currencies and commodities. Trade in derivatives increased substantially during the 1990's. Many banks and fund managers use them as a hedge against security price changes and currency fluctuations.

These instruments are complex and generally not universally understood.

In this guide we will only touch on the topic of derivatives. However, if you feel that they may be right for you, then I suggest you **download our free Derivative module** from our website or take a specialised course on the subject before investing.

Investment

Major Asset Classes - in detail

Options

Options are suitable for experienced investors who want to invest on an advanced level. Options can be high risk, and you can quickly lose a lot of money. It's extremely important to thoroughly understand the subject of options before getting started. Stop now, if you are trading and don't thoroughly understand options. Thoroughly study options before you get involved.

A very general definition of an option is as follows:

An option is a legal financial contract. It gives the holder the right, but not the obligation to acquire or to sell a predetermined number of stock or futures contracts, in a particular asset, at a fixed price, on or before a specified date.

Options can be traded on such things as stocks, stock indices, treasury issues and currencies. You have options (on the underlying financial instrument), which are made possible through a financial contract.

These are complex contracts. If you want to learn more about them, **download our free Derivatives module** from the website.

Investment

Major Asset Classes - in detail

Contracts for Difference (CFDs)

Contracts for Difference are the fastest growing tool for trading in stocks, foreign exchange, and commodities such as oil and gold.

A CFD is an agreement between two parties to exchange the price difference of a financial instrument. The profit and loss is determined by the difference in the entry and exit price of the underlying instrument from when the contract is opened and closed.

Contracts for difference have been used by professional investors for over twenty years and first emerged in the **over-the-counter** (OTC) or **equity swap** market. Equity swaps were used by institutions to cost effectively hedge their equity exposure.

CFDs have become one of the most popular derivative products in recent years. Its popularity has been fueled by the advantages it can offer retail clients.

Advantages of Contracts for Difference

Leverage: CFDs offer you full exposure to a stock for a fraction of the price of the underlying instrument. They require only a small initial margin as a trading deposit.
However leverage, often involves more risk than a direct investment in the underlying instrument. It is important that you understand that leverage can work against you, as well as for you. Using leverage magnifies both your trading profits *and* losses.

Profit from a rising or falling market, by taking long or short positions over selected stocks, indices, foreign currency pairs and commodities.

Contracts for Difference can be used to go ‘short’. This means that you can sell stocks you don’t actually own. With a ‘short’ position, you'll receive the full benefit of any fall in the stock price.

Low transaction costs: CFD providers pass on volume discounts allowing you to benefit through lower transaction costs. CFDs are a competitive and liquid financial instrument.

Hedging: CFDs allow you to employ more advanced strategies such as hedging your existing stock portfolio.

Simplicity: CFDs mirror the price of the underlying instrument. You can hold a position as long as you like. Unlike options trading, there's no expiry date, no time decay, and you'll never have to take delivery of the underlying securities. You can trade them online or over the phone.

CFDs also give you the transparency of a regulated market such as with:

Dividends and Corporate actions: When you take a long position CFD, you can enjoy the same dividends and capital growth as ordinary stockholders, but with an outlay of approximately 5% of the cost of the stocks.

The Two CFD models

There are two different CFD models: **Direct Market Access** (DMA) and **Market Making**.

The difference between these models relates to the way in which the prices are derived and the orders placed between yourself and the CFD provider.

Direct Market Access (DMA)

Direct Market Access is a system of trading where your **CFD** order is placed directly into the real underlying market. This allows you more control and easier access to liquidity

Direct Market Access results in real time execution, true market prices, participation in the order book and opening and closing phases of the market.

Transparency is a key ingredient of the DMA CFD market. All CFD orders are transacted in the underlying cash market, ensuring complete pricing transparency. All trades are executed on a strict price/ time priority.

Price/time priority means the first person to enter the best price is traded against first. The result is everyone in the central market order book are treated fairly and consistently, no matter what size trader you are. All market information reflects the cash market. This DMA system of CFD trading is essentially the same as trading stocks using leverage.

Market Maker model

Some CFD providers use a **market maker** (MM) model. Here you trade on synthetic prices that can potentially differ from the real prices of the underlying stocks.

Market makers base their prices on those offered in the physical market. Yet as a middle man they have the flexibility to adjust prices in their favour and as they see fit. This can cause slippage and result in a significant cost of trading.

A market maker will often quote that they 'mirror the price', rather than actually matching the price; resulting in orders being filled at lower prices. Market makers do not hedge 100% of their CFD positions and make money when you lose money.

When trading through a market maker your orders are at the discretion of a dealer. Your CFD order is not placed directly on the market, so trading can be slower, especially in fast moving markets.

Investment

Major Asset Classes - in detail

Versatile powerful products

Contracts for Difference (CFDs) are versatile and powerful products that can enable you to make effective use of your capital. They present a flexible and low cost alternative to traditional stock trading.

It is important to establish a trading plan that covers entry and exit criteria. If your trading is to be a success you must adopt thorough risk and money management procedures.

CFDs are simpler and more versatile than other derivatives such as options, futures contracts and installment warrants. However, to be a success at CFD trading you will need to remain aware of multiple information streams. Spend plenty of time trialing the various systems available; this will help ensure that you are using a suitable system for your trading style.

CFDs won't suit everyone. As a highly leveraged class of financial product, they are risky. Only experienced investors with a high tolerance for risk should use CFDs.

Free insider's guide to CFD's

To gain a detailed understanding of CFDs it is important to be familiar with all the key features of the product. **Download our free Derivatives module** from the website to get all the details you will need to trade CFD's.

Investment

Investing Philosophies

There is an assortment of weird and wonderful investing philosophies; appealing to a myriad of investor types. Each philosophy and accompanying strategy can have their uses. In fact they can be combined to create a portfolio perfectly customised to your own personality.

A full discussion regarding investing strategies and philosophies would take up a whole bookshelf! Below is a brief overview of some of the better-known philosophies.

Index investing

Index investing could be seen as the bottom of the investment ladder. It is an ideal strategy for women who don't have the time or interest to do their own stock research.

When investing in index products such as **index tracking funds**, **unit trusts** or **exchange traded funds**, you simply follow your chosen market up or down.

Index investing has low on going costs. As far as time or research is concerned it can offer good long term performance for very little effort.

Mechanical investing

Mechanical investing is the next rung up on the ladder of investing. These are strategies that determine which stocks to buy and sell, based on historically back tested returns.

However, mechanical investing does require more time and effort than index investing. Mechanical strategies come in many shapes and sizes. My advice is to select a strategy that suits you, and rigidly commit to that strategy for a set period of time.

Generally speaking, mechanical strategies will involve choosing a limited basket of stocks (typically 5). This requires up front time and commitment, but you need not get involved with financial or business analysis.

Investment

Investing Philosophies

Value investing

Value investing is a widely talked about strategy/philosophy. The famous investor, businessman, and philanthropist Warren Buffett created his fortune entirely through value investing.

Buffett simply bought stocks in ordinary businesses, such as Gillette, Walt Disney and Coca Cola. He made great picks steadily and consistently and focused on what he knew to be rational. As a result, Buffett amassed a $30 Billion fortune!

Buffett selects outstanding companies that he can hold, allowing his returns to compound year after year. In essence, his wealth grows at an exponential rate. What's more Buffett's approach enables him to do less and achieve more!

Over a 47 year period, Buffett's investment company, Berkshire Hathaway, has achieved returns of 214,433%. Whereas the Wall Street market index (S&P500) made returns of 3,663%. The difference in results is an astonishing 210,770%!

As the name implies, value investing places major emphasis on valuing companies to identify which are compelling long term investments. Usually investments are made when the price-to-value equation makes the investment a high percentage bet. That rarely happens in today's efficient markets. As such, a value investor will often possess a concentrated portfolio containing only a few stocks.

Warren Buffett has been known to hold as few as 3 stocks in his portfolio. Value investment will appeal to quantitative investors; those confident in assessing the true quality and value of a company.

Investment

Investing Philosophies

Growth and Value. What is the difference? Which is better?

As you learn more about investment you may come across the terms **growth** or **value**. These are the two philosophies/strategies that you hear most about.

It is illogical to make an artificial distinction between growth and value stocks. We should be looking for **quality stocks selling at good prices**.

However, these two categories will crop up frequently in investing literature, so it's best to understand the terminology.

Growth investors opt for companies that are fast growing. They focus on companies that have a greater potential for *growth* in their stock price. Value investors centre on purchasing stocks that seem good *value* in relation to its company's basic worth.

Growth investors

Growth investors focus on companies with high P/E ratios. Theoretically growth stocks increase faster than the market average. They usually don't pay dividends because they need their cash to increase. Growth stock prices can fluctuate wildly. Investors with aggressive risk profiles favour growth stocks. Examples of growth stocks include Google and eBay.

Value investors

Value investors focus on companies with low P/E ratios. To understand the difference more clearly we need to consider price earnings ratios. The P/E ratio is the ratio of the current price of a stock divided by its **earnings per stock** (EPS). Some companies don't have P/E ratios because their earnings are negative. Others have extremely high ratios because they have extremely small earning per stock (EPS).

Explaining the P/E ratio

Imagine the price of a stock is $20 and the EPS is $2.
Then its P/E ratio would 10.
Because 20 divided by 2 = 10.

If the EPS is $0.20, then the P/E ratio would be 100.
Because 20 divided 0.2 = 100.

So the formula for calculating the P/E ratio is:

$$\text{P/E ratio} = \frac{\text{Market Value per stock}}{\text{Earnings per stock (EPS)}}$$

The average P/E ratios for stocks in the S&P 500 index were approximately 22. In the U.K FTSE and Australian ASX, the average was around 16. After the recent market declines, the P/E ratios for each market are now much lower.

Some investors select stocks with high PE ratios; say above 20. They believe that the earnings in these companies will grow and that, because of this, it is easier to find stocks in this section that are under priced. These are the **growth investors**.

The value investor will focus on stocks with lower PE ratios because they believe that it is easier to find hidden value in this section.

A value investor will systematically search for stocks that are mis-priced by the market in terms of their earnings potential. Amongst other things, this mis-pricing is reflected in the relationship between the current P/E ratio and the future growth of its earnings. However, it is not easy to find such companies in today's markets.

The single best gauge for an investor's success is the quality of company she invests in. Factors such as entry point, technical analysis and ratios, are useless if the company you are investing in is of poor quality.

Investment

Investing Philosophies

'Core and satellite' holdings

'Core and satellite' holdings is a strategy fast gaining favour with many investors in Europe. The basic principle is that you hold the *core* of your portfolio (70-80%) in **index tracking funds** or stocks, run by a computer. Here the aim is to keep costs to a minimum and shadow your chosen markets or sectors. It is not to outperform the market.

The remaining 20-30% of your portfolio can then be invested with specialist fund managers. The purpose being to invest in emerging markets or small companies or into themed investment sectors such as real estate, technology, commodities or biotech. This 20-30% of your portfolio are your **satellite holdings**.

The advantage of using such a split model is that it gives you a clear benchmark; the performance of the *core* against which to judge the performance of your *satellite* holdings. If the satellite holdings consistently under perform the index tracking core holdings, then you may want to rearrange your portfolio.

Investment Strategies

Common Pitfalls

Being overly aggressive

Some investors delight in risk. They may concentrate their holdings in one high-flying sector, such as biotech or semi conductors. The danger here is that if the market falls the drop can be significant and the recovery may be long.

Tip: Make sure you're properly diversified and your investments are in line with your overall goals.

Chasing performance

A common mistake, is jumping into last year's top performing fund or asset sector. If you invest after a terrific run-up, you may be arriving just in time for the fall.

Whichever mix of investing strategies you use, the key to successful investing boils down to doing a few basic things right and avoiding the most common pitfalls.

Not expecting years with losses

Your portfolio will fluctuate in market value over time. Remember your objectives and time horizons. If you're invested for the long-term, don't be overly concerned about short-term losses on your investments. Any equity investment will experience volatility in the short-term.

Not thinking in portfolio terms

Choose your portfolio carefully, monitor it regularly and review and rebalance when necessary. Don't evaluate your individual fund investments in isolation. Focus on your overall portfolio.

Ignoring costs

Cost can eat into the return of your portfolio. Keep an eye on the running costs of your portfolio. Wherever possible go for no-load funds and discounted dealing charges.

Investment Strategies

Common Pitfalls

Timing the market

Which area of the market will perform best this year or next year, is anybody's guess. Yet many investors try to be "market timers". They try to predict where the best returns will be and move their money there. Inevitably, marketing-timing leads to more bad decisions than good ones.

The vast majority of investors don't know when to sell.

Exit Strategy

One strategy that an investor cannot afford to ignore is an exit strategy.

HOW AN "EXIT STRATEGY" CAN SAVE YOUR NEST EGG

100 years ago, Charles Dow said that one of the oldest rules in the book was to "cut your losers and let your winners ride." Yet so many investors do the opposite.

When an investor sees a 20% profit, she takes it. However, if that same investor sees a 20% loss, she lets it ride, hoping it will come back. Over the last year, instead of coming back, many 20% losses turned into 40% losses, then 60%, 80%, and beyond.

Having a few big winners that offset small losses will make you money. If you have no big winners, you'll never create wealth. If your winners and losers are the same size, you'll probably break even. But if you take profits at 20%, and leave your losers to continually fall, you will ultimately lose money in stocks.

Investment

Reasons to Sell

There are only **two** reasons to sell an investment: If the reason why you invested is no longer there, or if you've reached your pre-defined "point of maximum pain". Both concepts are simple. But most people don't follow either.

Let's look at each:

Your reason for being there is gone...

Say you bought a speculative biotech stock because its wonder drug was going to be approved by the FDA. But it was never approved. This is the time to sell.

Imagine you bought because you liked the top CEO of a company and now they have left. Now it's time to sell.

Say you bought stocks simply because they were cheap, and now they are really expensive. Why would you still hold on to them?

Why did you buy?

There is generally a main reason why you bought into an investment. Try and remember what it was and then ask yourself if that reason is still there. You may be surprised to find how many investments you're still holding that you shouldn't be.

Investment

The "Stop Loss" Strategy

The "Stop Loss" Strategy or point of 'Maximum Pain'

The best rule of thumb I've found is to use a 25% trailing stop. That way, you'll never have a catastrophic loss.

The concept of a **stop loss** is simple. If a stock or fund you own falls by 25%, you get out, and stop your pain.

The concept of a **trailing stop** is also simple. As the stock or fund rises, you raise your stop point. So, if you bought a stock at $5, and it goes to $10, then your new stop is $7.50. If it rises to $20 without falling by 25%, then your new stop is $15.

The biggest blow to any portfolio is a catastrophic loss. If a stock falls 90%, it has to rise by 900% to get you back to where you originally were! No one wants to be in this position.

Some may say that a 25% stop loss is ridiculous. What is the significance of 25%? The purpose of a 25% trailing stop is to convey discipline and avoid a catastrophic loss. This forced discipline also helps us to limit our losses and let our winners ride.

The 25% trailing stop strategy is the longest standing technique for making money.. Without an exit strategy you will always be giving back your gains.

A 25% trailing stop strategy is a simple example of an exit strategy and you can customise the percentage to what suits you. 25% is a rough rule of thumb. The goal is to sell when you should, instead of indefinitely holding and hoping.

Consider this:

During the tech boom of 1999, JDS Uniphase's stocks rose 1,200% before they fell by 25%.

If you sold using a 25% stop loss you would have taken a profit of 900%! Today the stock is lower than where it began.

But, if you held onto that stock you would have lost your profit and some of your initial investment. It is a dreadful feeling to lose money on something that was once up 1,200%!

Investment

The "Stop Loss" Strategy

A defined exit strategy is vital. You'll know when to get out systematically, instead of by the 'seat of your pants'. The seat-of-your-pants method is probably the most common exit strategy, even among experienced investors. There is a mass of research about stocks and stocks, but little about *when* to sell them.

If you commit to an exit strategy, you will be amazed at the change in your life. You will be able to sleep soundly at night. You won't worry about your nest egg. This is because you have considered your worst case scenario and have the strategies in place to cope. The uncertainty of when to sell will be gone.

Never allow yourself to have a catastrophic loss.

Before buying or selling another stock, take a quick inventory of your current portfolio. Do you have a proper exit strategy in place for each of your investments? Do you know what the worst case scenario is for each investment?

If you answered "no" to any of these questions, take action immediately, and put an exit strategy/stop loss strategy in place.

Like many of us, you will have to build your fortune from scratch. Regular saving is the basis behind establishing wealth. It is your route to financial security.

Many women find it hard to save. On a worldwide basis saving levels are at historic lows. The trouble is that it saving is not as much fun as spending! Saving requires discipline.

Just remember, your journey to financial freedom begins with a single step.

Investment

Establishing Saving Habits

The first step to building a fortune is to develop strict saving habits. This means setting a **budget**. Establishing a budget allows you to monitor exactly where your income goes and how much you can 'pay yourself' as part of your new saving regime.

The next step is to create a **financial plan**. Write down what your goals are (to build a fortune in the long term) and how you plan to achieve them.

Your investment options may seem endless. There are numerous companies listed on various Stock Exchanges; companies offering prospectuses through thousands of investment managers.

Do not be daunted. Keep things simple.

It can be tempting to abandon any attempts to save or invest money. The stock markets have been through a stormy time, interest rates are the lowest they have been for 40 years. It seems safer to sit tight and wait for things to pick up again. After all, if you buy into stocks or managed funds now, what happens if the market falls further?

Sitting tight is the wrong attitude. If you sit on the sidelines, or abandon thoughts of saving until things pick up, you might well miss the next upturn, and miss the opportunity to get in on the ground floor.

I know many women who procrastinate for so long that they never get started. Just as you should be smart with your investments, you should also make every dollar of savings work as hard as it can.

Investment

Establishing Saving Habits

Saving options

When it comes to maximising your money there are plenty of savings options better than an everyday bank account. Long-term savings shouldn't be kept in ordinary savings accounts or term deposits. For most people regular contributions to a managed fund, will give much better returns.

A **cash management trust** is the most disastrous place for women to leave their long-term savings. Instead, these savings should be channeled into a **managed fund** that invests in a range of asset classes and is managed by a professional.

Managed funds are less effective as a short-term investing strategy. This is due to their volatility and associated fees. However, over the longer term, fees and the extra risk associated with them become less significant.

An efficient way to save money is to set up a managed fund and regularly drip feed a portion of your salary into it . Most managers accept $50 - $100 a month, which shouldn't be beyond the reach of most of us.

Today, savings plans are very flexible.

To cater for unexpected expenses, most savings will accommodate your varying circumstances. Just as an unexpected windfall can be deposited into the account at any time, you can also stop or change your monthly contributions without penalty.

However, you should not exploit this flexibility by aiming to time the market. A stop-start savings strategy that attempts to pick market lows to boost returns is bound to fail. Market timing is difficult to achieve and is fraught with risk.

Investment

Establishing Saving Habits

Dollar cost averaging

The best approach is to keep it simple. Experts recommend the well-proven investment strategy of **dollar cost averaging**. Regular saving is all about controlling risk. It makes use of dollar cost averaging and will work in your favour. For example:

Say you invest a fixed amount at regular monthly intervals into stocks with a randomly fluctuating price. As such your money buys more stocks in the months when the price is low and fewer when the price is high.

The result is that your average cost basis per stock is *below* the average price of all those fluctuations.

So in reality you have bought more when the prices were down and less when they were up; without having to worry about the daily market. This is the big advantages of investing regularly.

Remember, you must invest the same amount of money in the market at the same time, over a reasonable period for it to work effectively.

Imagine the following scenario:

Paula invests a lump sum payment of $1200 once a year into an equities fund.

Wendy contributes $100 a month into the same fund.

Over 15 years, Wendy's monthly contributions leave her $8,079 better off because she adopted a regular savings strategy.

Wendy did not try to time the markets and benefited from dollar cost averaging. She effectively smoothed out, daily market price fluctuations by periodically investing into the market

Even modest savings are enough to get you started. But, if you can only put away a small amount each month, consider buying a **managed fund** such as a **unit trust** rather than stocks.

Investment

Establishing Saving Habits

Diversity

A novice investor with few other investments should consider a managed fund because they offer diversity. Look out for managed funds that invest across different asset classes, such as international and domestic stocks, real estate securities, fixed interest and cash. Diversifying will reduce your downside risk.

Many investment houses offer a range of suitable risk graded managed funds; which can be a sensible starting point when building your savings.

Investors seeking more diversification within a single fund should consider investing across a range of fund managers. Then you also get manager diversification. **An automatic savings regime is a convenient, simple and effective strategy for wealth accumulation.**

A parallel savings plan

Financial advisers stress the importance of having a parallel savings plan to run alongside your Retirement savingsplan. Likewise, home-owners who channel every cent into mortgage repayments are advised to put some money into a separate savings plan. It is just plain old diversification.

How much do I need to save?

This is like asking,' how long is a piece of string'?!

Most financial advisers will say "Pay yourself first and then try to save a minimum of 10% of your salary". My advice is to *save what you can comfortably afford.* There is no point aiming for a set percentage of salary, if this leaves you short of money at the end of each month.

Investment

Establishing Saving Habits

A more conservative saving regime is often the most successful. Many people set unrealistic goals, which is often why they unwind their savings plan early. They try to do too much too quickly.

Little things in life add up.

I am an advocate for small but regular savings. Small amounts saved over long periods can grow into large, impressive numbers.

If you save just $1 per day from age 18 to age 65 you could accumulate around $500,000.

If you save $2 per day for the same period the figure would be $1 Million, (assuming 10%p.a growth).

This method of accumulating large sums of money is easy and relatively painless. It illustrates just how powerful a long-term savings regime can be. Many of you reading this guide will not be 18. However, do not think it's too late to start saving; start now!

If you are 40 and you save $5 per day until you are 65, you can accumulate a tidy sum of over $200,000! The power of compound interest (growth on top of growth) works just as well for a 40 year old as it does for the 18 year old. You just have to save that bit more.

Think about dieting. It won't make any difference to your weight if you eat ten pies in one day. But if you eat ten pies every day for a year you will notice a big difference! The same rule applies to saving money.

A solid savings strategy can make you a millionaire.

If you can save $50 a week into a good equity unit trust, growing at 12% a year for 35 years, you will accumulate $1.4 million. You have a much better chance of achieving this than winning the Lottery!

Investment

DRIPS

DRIPS (Direct Investing Plans or Dividend Reinvestment Plans)

If you have experience and knowledge of stock investing, then you can benefit from dollar cost averaging and achieve the same results by using DRIPS

Through DRIPS, you can buy stocks of a company directly from the company and bypass brokers (and broker commissions!). DRIPS have grown in popularity in recent years, and hundreds of major corporations now offer them.

With traditional DRIPS, the company expects you to already own at least one stock of its stock registered in your name before you enroll. If you're not already a stockholder, you'll have to buy at least one stock through a brokerage, paying the commission.

In addition, you'll have to specify that you want the stock(s) registered in your name, not the brokerage's name, as is typically done. Then you can open a DRIPS account with the company and buy additional stocks directly through the company (or its agent).

Investment

DRIPS

Direct Stock Purchase plans (DSPs)

A new variety of DRIPS is **direct stock purchase plans** or DSPs. These operate in the same way as DRIPS except you are not required to have owned stocks before enrolling. You can buy your very first stocks through the company.

DRIPS allow you to gradually build a sizable position in a company by regularly contributing small sums of money.

For example:

If a company is trading at $6 per stock and you send in a $60 contribution, you will get ten stocks.

If next month stocks are at $5 and you send in $20, you will get four stocks. When the price is low, you get more stocks, and vice versa.

Take some time to learn more about DRIPS. For the experienced investor they are an excellent way of using the dollar cost averaging principle. Small amounts invested regularly over time, can build up a sizeable stock portfolio.

Investment

Encourage Saving Habits

Encourage your children

To adopt a disciplined saving attitude early in life will eliminate the stress and anxiety that many suffer, in the run up to their retirement.

If you can **encourage your children to get into a saving habit early**, then in most cases they will follow that routine for life. Children do not need to be bamboozled with the technicalities of investing. A simple saving routine is all that is required. If it is fun, then, all the better.

Two-Box system

One simple saving routine is the **Two-Box System** established by Justin Ford. By using this system you can ensure your children learn the fundamentals of wealth building. What's more they can become wealthy at a relatively early age. If you have children or grandchildren take a look at it:

The Two-Box System Explained...

Exactly how do you start your child on their 'march to millions?' Strangely enough, it all begins with two ordinary shoeboxes. One box is marked 'savings box', and the other is marked 'spending box.'.

Each time your child receives money, be it pocket money, birthday money etc, half of it goes into one box... and half into the other.

The 'spending box' contains money your child can spend on anything they want and you allow. Such as toys, sweets, books, movies etc.

The 'savings box' is money your child can not touch. This is money is allocated to long-term investments that, over time, will grow into hundreds of thousands of dollars.

It Really Works!

Investment

Encourage Saving Habits

The Two-Box System is not a great sacrifice for kids. On the contrary, the habit is a simple technique. It may well inspire your children to enjoy what they do have without becoming spoiled, or contracting the dreaded 'Gimme Disease'.

Your child can count out the permanent savings with you once or twice a year and you can invest it for them. The temporary savings can be spent on whatever they want. These saving habits will become second nature to them, which is the whole point!

But what happens when the kids grow up?

At an appropriate time your child will gain control over their investment accounts. But what's to prevent them from squandering the wealth they've accumulated, you ask? Nothing can stop them from squandering, but as they have created wealth themselves, through their own discipline, they are less likely to do so. Hopefully they will know that wealth is not an 'easy-come' proposition.

In other words, your child's financial character has been moulded from the very beginning. Going on a spending spree would feel 'unnatural' to them.

With such disciplinary traits in place there is a stronger possibility that your child will have a good savings and work ethic. And they'll have you to thank for it.

As you can see, you don't have to win the lottery to gain wealth. You can systematically create your own financial security, by saving little and often, and letting compound interest work its magic.

Tax Issues

Tax Issues

Tax is an intimidating subject. Detailed discussion on Tax issues is beyond the scope of this guide. However, you do need to be aware of any Tax liabilities you may have. I can only scratch the surface of an area of personal finance which is too complex by far.

'In this world nothing is certain but death and taxes.'

Benjamin Franklin

It's certainly true that you can't escape from one, but what about the other? Well you can avoid tax legitimately to varying degrees. There are a number of ways to reduce your tax bill, which you should take advantage of if you can. These are common to most tax regimes.

You should try to avoid tax where possible as distinct from evading tax, which is illegal as well as unproductive. Never participate in any investment simply because it will reduce your tax bill. Only invest in what you believe will increase your wealth. If they happen to come with a tax rebate then all the better.

No one has ever become rich by building up tax deductions!

Taxes relevant to investors are **income tax**, **provisional tax** (applicable in some countries) and **capital gains tax**.

Personal income tax

Income is more than just a salary or wage. It includes returns from investments such as interest from deposits or bonds, rental income and dividends from stocks. This investment income, in addition to your income from paid employment is taxable at your personal income tax rate.

Tax Issues

Capital Gains Tax

This tax is payable on any capital gain made after the disposal of non-exempt assets. A capital gain is the difference between the cost of the asset and the amount you receive when you sell it (assuming this is for a profit). Capital Gains Tax can apply whether you acquired the asset by purchase, inheritance,construction or you received it as a gift.

In the United States, individuals and corporations pay income tax on the net total of all their capital gains just as they do on other sorts of income.

The amount an investor is taxed depends on both his or her tax bracket, and the amount of time the investment was held before being sold. Short-term capital gains are taxed at the investor's ordinary income tax rate, and are defined as investments held for a year or less before being sold. Long-term capital gains, which apply to assets held for more than one year, are taxed at a lower rate than short-term gains. In 2003, this rate was reduced to 15%,and to 5% for individuals in the lowest two income tax brackets. These reduced tax rates were passed with a sunset provision and are effective through to 2011; if they are not extended before that time, they will expire and revert to the rates in effect before 2003, which were generally 20%.

The reduced 15% tax rate on eligible dividends and capital gains, previously scheduled to expire in 2008, was extended through 2010 as a result of the Tax Reconciliation Act signed into law by President George W. Bush on May 17, 2006. As a result: In 2008, 2009, and 2010, the tax rate on eligible dividends and long term capital gains is 0% for those in the 10% and 15% income tax brackets. Capital Gains are subject to tax at the marginal rate of income tax (for individuals) or of corporation tax (for companies).

In most jurisdictions your main residence is exempt from capital gains tax. It is a confusing tax and is best dealt with by an accountant. Be aware of it and do not go along blindly ignoring it.

Tax Issues

Tax Saving Tips

There are a number of tax saving tips relevant to most tax jurisdictions. Even if you only act on a handful of those listed, you will be on your way to improving your personal finance affairs.

Tip 1

Keep proper tax records. These include your working papers and relevant documents such as savings certificates, tax credit forms, dividend payment records. Remember, you can be fined by the tax man for not keeping proper records.

Tip 2

Don't be late sending in your tax return. You risk a fine for being late.

Tip 3

Don't forget that you can send in your tax return over the Internet. This is a convenient method for busy women.

Tip 4

Don't be frightened to check documents the taxman sends you such as a notice of coding or a tax calculation. Remember, taxmen make mistakes too.

Tip 5

Don't be a shrinking violet. If you think you are being asked to pay too much tax on account, ask to pay less.

Tip 6

If you're feeling charitable, be tax-efficient. Consider making donations to charities.

Tax Issues

Tax Saving Tips

Tip 7

If married, ensure your finances are organised so that investment income is paid to the partner who pays less tax.

Tip 8

Keep good records of your business expenses so you can substantiate any claims.

Tip 9

The government provides numerous tax incentives for you to save longer –term. Contributions to a qualifying pensions fund are very tax efficient. Take advantage of these tax shelters (i.e.: Kiwi Saver account in NZ).

Tip 10

If you are a non-taxpayer, ensure you receive interest from your savings free of tax.

Tip 11

Make a will.

Tip 12

Don't forget that you can make a number of gifts which will reduce any future liability to Estate Inheritance tax.

Tax Issues

Tax Saving Tips

Doing Your Own Tax Return

If you work for a company and have no rental income or capital gains liabilities then you should be able to save money by doing your own tax return.

However, in my experience DIY tax returns can be a false economy, if you have complex finances, enlist an accountant.

Employing a competent accountant to do your tax returns will save you time, hassle and in most cases you will pay less tax.

If you keep on top of your tax liabilities as you go, you should have no problems. When you ignore your tax and let it build up, then it can be a daunting task.

If in doubt, always seek professional help.

Planning for Retirement

Planning for Retirement

Planning for an active, rewarding retirement

Many of our grandmothers and great grandmothers saw the institution of marriage as their pension. Many of our grandmothers were heavily reliant on a state pension. Thankfully this is rarely the case today. However, there are still a worrying number of elderly women living on or near the poverty line.

Women still tend to have much less income in retirement than men. This is mainly due to the fact that women on average earn less than men, we tend to have more breaks in our careers and we live to older ages. On average we live 7 years longer than men.

In the U.S.A alone, women-owned businesses now number 7.7 million, employ over 15 million workers and generate nearly $1.4 trillion in sales! These are staggering figures. Yet, women still earn only about 76% of what men earn. Lower wages translate into lower retirement benefits, as well as smaller state pension benefits.

It is generally recognised in the countries that provide state pensions, that due to demographic changes these benefits will dwindle as the years go on. With life expectancies continuing to increase, so does the need for income above and beyond 401K plans, IRA's and social security.

The burden of funding for retirement is falling more and more to the individual.

Planning for Retirement

It is clear that many women need to look to additional sources to help build their retirement nest eggs.

You do not need to understand everything about retirement plans. Hundreds of choices and changing legislation make it hard to keep up to date.

You do not need to get embroiled in understanding all the ins and outs of the legislation, in order to plan your retirement. The rules vary from country to country, but the fundamentals are the same regardless of where you live. The main elements are common to most countries, where they can be divided into 3 key parts:

Planning for Retirement

State Pensions

With the burden of funding for state pensions ever increasing, most people are now aware that they can not rely solely on the state to provide a comfortable retirement.

Social Security is neutral with respect to gender. Individuals with identical earnings histories are treated the same in terms of benefits.

But, women still receive lower pension benefits due to their relatively lower earnings.

With longer life expectancies than men, elderly women tend to live more years in retirement and have a greater chance of exhausting other sources of income. They benefit from Social Security's cost-of-living protections because benefits are annually adjusted for inflation.

Women represent 57 % of all Social Security beneficiaries age 62 and older and approximately 70 % of beneficiaries age 85 and older.

The Social Security system is progressive in that lower-wage earners receive a higher percentage benefit than higher-wage earners do.

The system returns a greater percentage of pre-retirement earnings to a lower-wage worker than to a higher-wage worker. Women who are low-wage workers receive back more benefits in relation to past earnings than do high-wage earners.

The amount for 2009 for a person retiring at full retirement age (66) is $2,323. This is based on earnings at the maximum taxable amount for every year after age 21. Since President Obama came to power, roughly 50 million individuals will get around 5.8% more in 2009, the largest increase in more than a quarter century.

Planning for Retirement

State Pensions

In 2007, the average annual Social Security income received by women 65 years and older was $10,685, compared to $14,055 for men.

In 2007, 47% of all elderly unmarried females receiving Social Security benefits relied on Social Security for 90% or more of their income!

These are hardly amounts that are going to allow you to live the high life in retirement! Obviously in order to live comfortably in retirement you can not rely on state benefits alone.

Elderly women are less likely than elderly men to have significant income from pensions other than Social Security.

Planning for Retirement

Company Schemes

If you work for a company, there is a good chance that it will run a retirement plan.

The employer sponsored retirement plans are given numbers- 401(k) or 403(b).

Participation in employer-sponsored retirement plans is increasing for women in today's workforce. Over 52% of women employed full-time, now participate in an employer-sponsored plan.

If you are eligible to join any of these schemes, then in most cases, you should do so.

Contributions you make to a 401(k) can reduce your federal income tax burden and the contribution limits are higher than those of an IRA.

The 401k plan has gained steadily in popularity. Total assets in 401k plans passed traditional pension funds in 1996.

An estimated $1 trillion dollars are invested in the plans. Studies show that 70% of companies with 100 or more employees offer a 401(k) plan.

The 401(k) works pretty simply. The employer will select a plan administrator. A number of investment options will be made available within the plan.

Typically the options will include a guaranteed vehicle (certificates of deposit), a few mutual funds, and the employer's own stock (if it's publicly traded).

The employee will be allowed to contribute a portion of their wages into the plan. There will be a maximum percentage.

Planning for Retirement

Company Schemes

One of the big advantages to the plan is that the amount you contribute reduces your taxable income. So if you earned $50,000 last year and contributed $1,000, your taxable income is $49,000.

You won't pay taxes on the 401 (k) money until you withdraw it. Then any withdrawal is added to your ordinary income.

If you take money out before age 59 1/2, you'll also face a 10% penalty except for certain loan options.

But, by delaying taxes on your contribution, it's like giving yourself a pay raise. For someone making $50,000 per year, a 2% contribution could save you $280 in taxes.

The tax benefit also has a hidden effect. Since taxes aren't deducted before you make your investment, you have a full $1 that begins to earn money right away. That's a big difference.

For example:

If you had paid 28% in taxes only 72 cents would have been invested. And that 72 cents would need to earn nearly a 40% return before it would become $1 once again. Even in good markets that takes a couple of years.

And that's only the beginning of the good investment news. Some companies offer to match a portion of your contribution.

For every $1 you contribute they'll add 25 or even 50 cents. Thats definitely a bonus worth having. That would equate to a 25% or 50% return on your money before the investment does anything. So even if the investment choices offered by your company are not your favorites, it really doesn't matter.

Planning for Retirement

Company Schemes

Within the choices available there are a couple of things that you can do to make the most of your investment. Since the funds are meant for retirement you'll be taking a longer view with the investments. That means you can afford to take more risk than you could if you expected to use the money in a year or two.

The second suggestion comes as a caution.

Don't voluntarily buy company stock. If the company goes through hard times, not only will your investment be hurt, but you could also lose your job at the same time. Remember what happened to Enron!

Finally, remember that it's money that you don't see. You don't need to work hard at saving. It's safely put away before you'd have a chance to spend it.

Overall, a 401k plan is an excellent way to save. The company may be controlling your investment options, but, generally, that's a concession worth living with for the benefits of a 401k plan.

For most women, the company scheme will be the best way of boosting your income in retirement.

Planning for Retirement

Company Schemes

Company sponsored schemes tend to fall into two categories:

Defined benefits/final salary schemes

This type of scheme is typically offered by public sector employers and some larger private companies. With this type of scheme your pension is calculated by a formula, as a proportion of your final salary and is dependent upon the number of years you have worked for the company.

The advantages of this type of scheme is that there are certainties:

- You know that if you work for so many years, you will be entitled to a certain level of pension.
- You do not have to worry about stock market movements, because you will obtain the promised pension irrespective of how well the pension fund is invested.
- You will generally have to pay a percentage of your salary into the scheme (typically 5%), which is taken from your gross salary. In return your employer will bear all the investment risk.

Take time to read your company scheme booklet which will outline the maximum retirement benefits payable and any entitlements to a tax free lump sum, life cover etc…

The bad news with this type of scheme is that for many women they are unable to build up enough years of service to get adequate benefits in retirement. The costs of running a defined benefits scheme have blown out of all proportion in the last decade, because retirees are living to older ages. The last stock market down turn, exposed huge funding black holes at major companies such as IBM , G.E, ICI and British Airways.

Because of the increased funding costs, many companies are changing from defined benefit schemes to defined contribution schemes.

Planning for Retirement

Company Schemes

Defined contribution schemes/money purchase schemes/accumulation schemes

With this type of scheme, your final benefits will be determined by the amount of money paid in by you and your employer and the investment earnings of the fund. The performance of the underlying fund is critical to what you end up getting. It is therefore very important that you take an interest in the investment funds on offer and select funds appropriate to your risk profile and time horizon.

This type of scheme is becoming increasingly common, they are easier to understand and more flexible than defined benefits schemes, however, your end benefits are less predictable. What you get out will largely depend on investment performance.

Another unpredictable factor is when your retirement fund is turned into pension income. At retirement your fund will be used to purchase an annuity, which will pay you a lifetime regular income. Annuity rates vary from year to year, according to factors such as interest rates and the fixed interest market.

As you can see with this type of scheme, you have to take much more responsibility than with a defined benefits scheme.

Planning for Retirement

Individual Retirement Accounts

If you don't have access to a company sponsored scheme, then there are a number of personal retirement savings vehicles available.

Don't be put off by all the jargon surrounding these plans. They are basically just tax efficient long-term savings plans.

If you work for yourself, make sure you contribute to a retirement plan so that you will have something to show for your hard work.

What plan should you chose, and how much can you contribute? Here are some of your options:

> Women make good entrepreneurs because they are able to juggle lots of tasks and respond to a myriad of demands.

IRAs

The easiest plan is to establish an Individual Retirement Account, but you can contribute only $2,000 a year. An IRA might be a good choice if you're just starting out and can afford only minimal contributions. Regular IRAs are tax-deductible, but if you are in a low tax bracket, consider a non-deductible Roth IRA that will grow tax-free instead. While Roth IRA contributions are not deductible, qualified distributions are received free from federal income taxes.

SEP-IRAs

If you want to contribute more than $2,000 to an IRA, the SEP-IRA (Simplified Employer Pension) will let you put 13.04% of your net business income into the plan, up to $30,000. There is a down side, in that you will have to cover all employees over 21 years of age who have been working for you for the past three years. That can get expensive!

SEP-IRAs are more popular among self-employed business owners with no employees.

Planning for Retirement

Individual Retirement Accounts

SIMPLEs

This plan also requires that you cover employees, but to a lesser extent. This Savings Incentive Match Plan for Employees operates like a simplified 401(k) salary deferral plan, with an employer match. It requires you to contribute only 3% of your employees' wages, and it covers employees who have earned at least $5,000 in two prior years and are expected to earn $5,000 this year.

You can put in up to $6,000 for yourself. Your employees can make tax-deductible contributions to the plan as well.

KEOGHs

A Keogh plan is the Rolls Royce of entrepreneur retirement plans. But be aware, significant red tape is involved. With a Keogh, you can tailor the plan to allow hefty contributions for yourself, while requiring much smaller contributions for your employees.

With a defined benefit Keogh, you can contribute 100% of your salary, up to a maximum of $170,000.

The down side is, that they require the services of an actuary, and you must file a Form 5500 tax report with the IRS on a regular basis.

If you are an employee and your business is a sideline, you should contribute the maximum possible amount to your work 401(k) or 403(b) plan before investing in a self-employed plan. The advantage here is that your employer may match your contributions. The contributions to the 401(k) plan are by payroll deductions and most 401(k) plans allow you to borrow from the plan for education, hardship or general purposes.

Planning for Retirement

Individual Retirement Accounts

You can set up any of these plans through most financial institutions, brokerage houses and mutual fund companies.

All personal retirement plans work on the same principles as defined contribution/money purchase/accumulation schemes. Your contributions are invested in your selected assets or funds to build up a pot that on retirement can be used to buy a lifetime income. The final benefits you derive from a personal plan will depend upon the amount of contributions you have made, the charges for running the plan, the performance of your selected investments and the annuity rates at the time you convert your fund into a regular income stream.

With any personal retirement plan you have to be disciplined about making adequate contributions and be proactive in keeping your investment decisions in line with your risk profile.

If the current financial debates tell us anything, it is this: the only funding you can count on is that which you do yourself.

For many women who are self employed or only working on an erratic or casual basis, these plans offer a tax efficient way of saving long term.

Planning for Retirement

Maximize Your Savings

There are a number of factors that will help you maximize your retirement savings:

Start young

It is hard to think about abstract subjects like retirement when you are in your 20's and 30's, but the sooner you start saving the better. If you get into the discipline of saving regularly when you are young, this will become a habit that you will continue throughout your life. If you start saving, then have a few years out of the workforce to have children or study, this is far better than not starting until you have returned to the workforce.

The secret to making a better financial future for yourself, is planning and waiting. It may not sound exciting, but you stand to gain some of the biggest paybacks you'll ever experience, from the retirement fund you have accumulated over the years.

Contribute your own money to retirement savings

Many women rely only on their employer's contributions into their retirement plan. This is better than nothing, but your eventual pot of money will be considerably boosted if you contribute your own money over and above what is being funded by your employer. In most countries there are Tax incentives for doing this - either in the form of Tax deductions or Tax rebates. So, this is a tax efficient way of saving.

Make the best of the investment options

Many women do not take enough interest in their retirement savings, until they approach retirement. By then it is often too late to make any significant difference to the size of your pot. Because retirement savings are tied up and out of our reach for a long time, this doesn't mean that you cannot have control over how the money is invested.

Planning for Retirement

Maximize Your Savings

Your retirement plan may well be your biggest asset after your home. It is therefore very important to be proactive. The investment return you get on your savings will dictate the type of lifestyle you will have in retirement. Many retirement plans offer a choice of investment options. Make sure you make use of this facility.

You should now be familiar with the various asset classes, and this will stand you in good stead, when choosing how best to invest your retirement savings. The various alternatives may range from conservative to aggressive, where the approach you choose will impact greatly on the returns you receive.

As with any investment, there is a trade-off between risk and reward (investment performance). You should already know what your risk tolerance and time horizon is. Women tend to be more conservative investors than men. But, being overly conservative over long periods of time can have a devastating impact on the growth of your retirement pot.

Your first impulse may be to protect the value of your savings by picking a relatively conservative investment. However, if you consider that you may well have to live off your retirement fund for another 20-30 years after you retire, a less conservative investment mix, such as shares, listed property and bonds will have a better chance of outpacing inflation and providing a higher return.

Be proactive and regularly review how your retirement funds are growing. As with any other investment, you may wish to change your asset allocation from time to time.

Invest in assets that are appropriate for your risk tolerance and time horizon.

Planning for Retirement

Maximize Your Savings

Consolidate your retirement funds

As you move from one employer to another, you will have preserved benefits accrued in various funds. In most cases it is more cost effective and easy to keep track of, if you roll over all these preserved benefits into one plan. But be aware of any exit fees that may be payable, before you rollover benefits.

Be realistic

I have yet to meet the woman that says she has too much money in retirement! Be realistic about how much you will need, in order to live an active comfortable retirement. Remember you will have more time to spend money when you are retired.

How much should you be saving?

This will vary dramatically from individual to individual. Some women will be able to live well off a modest amount, whilst others will never seem to have quite enough! There are all sorts of formulas that you can use. But realistically it all boils down to what you can afford to save. Save consistently over a long period of time. Top up your regular savings with lump sums as and when you can.

The earlier you start contributing to your retirement savings, the greater the compounding effect on your investment long-term. You can earn interest on your interest, or growth on growth. Your retirement savings will grow exponentially over long periods of time.

The following example illustrates the point:

Consider Sarah and Mary, both 65 years old. They worked for the same company for 35 years and both invested in the same retirement fund.

Planning for Retirement

Maximize Your Savings

Sarah started investing at age 30. She invested $1,000 each year for ten years and earned 8% per year. Then she stopped contributing, but her investment continued to earn an 8% annual return. At the end of the period her $10,000 investment was worth $107,148.

Mary didn't start saving until age 40 and then invested $1,000 each year for 25 years. She also earned 8% per year. At the end of the period, her $25,000 investment was worth $78,954.

As you can see, although Sarah contributed to her investment for 15 fewer years than Mary and invested $15,000 less, she accumulated $28,194 more than Mary, simply because she started investing ten years earlier.

Earning interest on interest is a very effective and simple way of increasing your retirement pot. One simple compounding rule can take years of worry about retirement off your mind, provide a clear goal in your financial life, and set you on course for later years.

The rule: Your money will double every seven years if it compounds at the stock market's average rate of return of nearly 11% annualised over it's lifetime. Compounding is definitely your friend when it comes to long- term savings!

Planning for Retirement

Retirement Strategies

Your retirement strategy will change, as you get closer to retirement. Consider these strategies from age 20 to age 65.

Age 20's

The carefree years

1.Have fun

2.Go to college/university

3.Retirement is a long way off

4.Get into the discipline of regular saving

Age 30-35

Life Is good.

1. Ideal time to fund a retirement account

2. Concentrate on paying off school/university loans as soon as possible.

3. Buy a home: pay it off; do not get involved in the refinancing game!

4. Your car should be paid off and well maintained.

5. Your debt-free thinking should be sinking in.

Age 40-45

Getting Serious about retirement funding.

1. If you haven't started a retirement account, START NOW!

2. Your career is moving.

3. Return to studying? - do it now, ONLY if it is affordable.

4. Help your kids? This is your last chance.

Planning for Retirement

Retirement Strategies

5. Health insurance benefits in check

6. Savings are geared up, paying off your home.

Age 50-55

The Plot Thickens

1. Aggressively fund your retirement account

2. Review your social security benefits.

3. Research health care possibilities before age 65.

4. Your house should be at least half paid off, no loans.

5. Fund a supplemental retirement and a savings account.

Age 65

Enjoy your leisure time.

1. Stay debt-free

2. Enjoy your travel

3. Have fun with your grandchildren

4. Avoid the scam artist

5. Try some new crafts

6. Review your investments regularly

Planning for Retirement

Living in Retirement

For most women, living well in retirement means living in comfort and security. It means being able to manage your money in your own time, without any worry or inconvenience.

The difficult thing about managing your money in retirement is making sure it doesn't run out before you do! There are 4 main variables to consider:

1. How much money do you have? If you have already retired you won't have much control over this factor.

2. What rate of return will you get? Most retired women will want to have their money in pretty safe investments. This means that in most cases you may have to accept somewhat lower returns than you did when you had a higher risk profile. But safer investments are prudent at this stage because you can't afford to lose any of your capital at this time of life.

3. How much do you need to live on? This might require some careful budgeting. It is the one variable that you have the most control over. If you set a realistic budget in the early days of your retirement, you shouldn't need to scrimp and save later on.

4. How long will it need to last? This of course is the great unknown. But as a woman this issue is far more critical for you than it is for men. Over the next 40 years, the number of women aged over 85 is expected to triple or quadruple in the developed countries. 75% of these women will be single, divorced or widowed!

Planning for Retirement:

Living in Retirement

Investing when you are retired usually has two purposes:

- To provide you with a regular reliable income
- To generate some capital growth, so that your money is protected against inflation and does not run out before you do.

Make certain you don't outlive your assets!

In recent years the concept of funding retirement out of capital is becoming more acceptable. For many decades the idea that you should always preserve your capital has been hallowed, but today people are less likely to excessively moderate their life style in retirement simply to pass on capital to their children. There is a growing acceptance that you will indeed erode some of your capital before you die.

Once you reach retirement and you wish to start taking your income, there are a number of steps you will need to take:

1. You should obtain details of the retirement fund you have built up, from your retirement plan provider. This will explain any tax free cash entitlement you are eligible for and the annuity options you have.
2. Now is the time for careful consideration. Do you need the tax free cash or do you use the whole of your pot to convert to lifetime income?
3. Then you need to go about getting the best annuity deal. This is critical because it will determine how much income you receive for the rest of your life. There is often a big difference between the best and worst annuity rates available.
4. If in doubt get professional advice.

Planning for Retirement:

What are Annuities?

In simple terms, an annuity is a contract between you and an insurance company. In exchange for getting your hard-earned cash today, the insurance company agrees to pay you an income for a specified period or for your life. Those payments may start at some date in the future or they may start on the day you buy the contract. If the payments are delayed until the future, you have what's called a deferred annuity. If the payments start immediately, you have an immediate annuity.

When you reach retirement most people will be buying an immediate annuity. You pay for an immediate annuity with a lump sum of cash on the day you buy it. In exchange for your lump sum, you will receive a regular income stream. The amount of income you get depends upon your age, sex and interest rates at the time the annuity is bought. Unfortunately, because women live longer than men, the annuity rates we get are not as favorable as for men. In a low interest rate environment, such as we have today, annuity rates are less attractive than when interest rates are high.

There are term certain annuities or lifetime annuities. If you opt for a traditional lifetime annuity, you would want to be in good health and have longevity in your family genes, because if you die soon after buying the annuity the annuity dies with you! A term certain annuity is where payments are guaranteed for a fixed term – typically 10 years. If you die within this period your beneficiaries will continue to receive the income payments until the end of the term.

Planning for Retirement:

What are Annuities?

In the past there were few choices when it came to annuities. But today as people are living longer there is the need for some potential for capital growth. Hence annuities come in a number of varieties:

Fixed Annuities

As the name implies, a fixed annuity provides a locked-in, guaranteed rate of return on the investment and a fixed, stable income in its payout phase. A fixed annuity thus provides a steady retirement income - but this steady return can and will be eroded by inflation. Options are available (at a price), to have your annuity payments increase by 3% to 5% each year should you so desire. If you select the indexed option, your income payments would initially be lower than a fixed payment, but over the years the payments will steadily increase at the specified rate. For those expecting to live many years, the added cost of this feature might be worth the price.

Variable Annuities

Probably the most popular form of annuity these days, a variable annuity or allocated annuity, allows the purchaser to decide how to invest the money within a range of mutual fund/ insurance fund options offered by the insurance company. They will typically offer a selection of stock, bond, and money market sub-accounts. Thus, like a mutual fund/ insurance fund and unlike the fixed annuity, the returns of the variable annuity are not stable, and will vary along with the markets.

While this variability does carry downside risk, it nevertheless affords the annuity buyer the ability to participate in the potentially greater returns of the stock market. As the stock market rises, so does income derived from an investment in an equity sub-account. Conversely, as the market declines, so will income.

The advantage of this type of annuity is that, over the long-term, a variable annuity invested in an equity sub-account should provide a much better opportunity for inflation -protected income than a fixed annuity.

Planning for Retirement:
What are Annuities?

Equity-index Annuity

A recent innovation in the insurance industry, an equity-index annuity is a form of a fixed annuity contract tied to a stock index that provides the opportunity to earn returns better than those in a traditional fixed annuity, but less than those of a direct investment in the market itself. In this contract, the insurance company invests in a mix of bonds and stock options designed to give a targeted participation rate on the return of a particular index (e.g., the S&P 500 Index).

While the purchaser has no choice in the investment itself, she is able to participate to a degree in stock market gains during a rising market. If stocks fall, then the contract guarantees a minimum return, typically 3%. Because of that guarantee, the equity-index annuity has less downward volatility than the variable annuity.

Phased retirement and income drawdown

These are both ways of controlling the income you obtain from your retirement/pension fund while leaving the fund fully invested. In most cases this facility is only available for individual retirement plans.

As you can see there are a lot of decisions to be made once you get to retirement. Annuities are a complex subject and there are various tax implications (depending on where you live) that should be fully explored before you make any firm decisions. This is a time when it may well pay you to take professional advice from a specialist in this area.

Planning for Retirement:
Inheritance Tax Planning

Statistics show that women live longer than men. As such, married women tend to inherit the family assets. Therefore, they often have to make provision for mitigating estate/inheritance tax.

When a loved partner dies, women's worlds can go haywire. Many have no idea where their partner's financial papers were kept. Worse still, if they died intestate (meaning they didn't have a will), then sorting out their estate can be a nightmare.

No one wants to think about losing a partner and many of us dodge the discussion of death. The simple task of writing a will is often avoided.

If you are not prepared, the onslaught of paperwork that will hit you after your partner’s death may be overwhelming. It is traumatic even when you are prepared.

A helpful to-do list:

- Get a grip on your assets. Gather copies of your joint tax records for the past five years, records of both you and your partner's retirement plans. Collate all insurance, bank and brokerage accounts, including the deed to your house. Bundle documents in one big file that you can keep in a safe, but accessible, place.

- Obtain death certificates. You'll need to make multiple copies of your partner's death certificate to send to credit card companies, your mortgage lender, and insurers to verify the death.

- File a claim for benefits. Notify your partner's employer. Enquire about any benefits owed to you, such as pension income, life insurance and health insurance coverage. Enquire about employee benefits (the human resource department can direct you). You may need to talk to more than one employer if your partner retained benefits in previous employer’s plans. Find out about settlement options. Some plans ask you to choose between a lump sum payment and annuitised payments. Annuitised payments are made monthly or annually.

Planning for Retirement:
Inheritance Tax Planning

- File insurance claims. Alert your partner's life insurance company and file a claim. Your insurance agent or broker should have all the policy information you will need and be able to help you obtain the necessary forms.
- Notify government offices. Centrelink will need to be informed. You should also contact your Roads & Traffic Authority, to change their car registration to your name.
- Contact financial services providers. Any joint accounts should be transferred to an account in your name. (You will need a copy of the death certificate to do this.) In many cases, you can re-negotiate the terms of any outstanding loans with your bank. If your partner had a brokerage account, ask their stock broker to give you a value on their account at the time of your partner’s death.
- Update your insurance policies. If your partner worked for a company, check what cover they had. Also update any life or disability insurance policies.
- Most financial advisers recommend that you refrain from investing any lump sum insurance or pension payout for at least six months, post your partner's death. Put any cash into a high interest bank or building society account, until you are able to make informed decisions on longer term investments.

- Compile a budget that works. Decide how best to allocate your new income. Take into account the current and future needs of you and your family.

- Calculate your total assets (including your investment accounts, income, and life insurance payouts). Now, subtract what you owe on your mortgage, credit cards, outstanding loans and any tax liabilities. Ascertain much income do you have and how much you spend each month. Determine which bills *must* be paid and which are optional; such as a gym membership. Once this is done then you have your budget priorities in place.

- Take it slow. After you have sorted the 'must-do list', take a break. Don't feel pressured to make big financial decisions. Once you feel ready to take action, consult a financial adviser to help you develop a short-term and long-term investment plan.

What is inheritance tax?

The estate tax in the United States is a tax imposed on the transfer of the "taxable estate" of a deceased person, whether such property is transferred via a will or according to the state laws of intestacy. The estate tax is one part of the Unified Gift and Estate Tax system in the United States. The other part of the system, the gift tax, imposes a tax on transfers of property during a person's life; the gift tax prevents avoidance of the estate tax should a person want to give away her estate just before dying.

Estate taxes are very complex. Consult a specialist who can give you expert advice.

In addition to the federal government, many states also impose an estate tax, with the state version called either an estate tax or an inheritance tax.

Since the 1990s, the term "death tax" has been widely used by those who want to eliminate the estate tax.

If an asset is left to a spouse or a charitable organization, the tax usually does not apply. The tax is imposed on other transfers of property made as an incident of the death of the owner, such as a transfer of property from an intestate estate or trust, or the payment of certain life insurance benefits or financial account sums to beneficiaries.

Planning for Retirement:
Reducing Tax Liabilities

Make a will

It is amazing how many people do not make a will. If you die intestate (without a will) it can cause a lot of anguish for the family. Without a will your estate can be disposed of in a way you would not have wished.

Anyone with an estate, a spouse or partner, children, or a family must make a will. What's more it needs to be clear, current and valid.

Use Trusts

It is possible to use certain trusts to minimize inheritance tax. The principle is, that your assets are put into trust for the benefit of your children or grandchildren. This then reduces the number of assets that will be liable for inheritance tax.

A **power of attorney** can also be useful. This gives someone you trust the ability to act on your behalf. By nominating a person you trust can alleviate situation where you may be incapacitated and unable to sign documents.

Please note: The use of trusts and power of attorney should only be considered after taking expert advice.

There are many legitimate ways of reducing your inheritance tax liability. If you put the effort into an effective estate planning strategy your beneficiaries should not have to pay unnecessary tax.

Further Reading

Further Reading

Although the guide should arm you with sufficient information to tackle the personal finance market with comfort, it cannot provide you with specific advice. Nor can it keep you abreast of all the latest products available in your home country. To fill this gap, you need to refer to regular personal finance publications and websites, of which there many.

Here follows some useful starting points:

Websites

www.pinkinvestments.org

www.bloomberg.com

www.ft.com

www.money.com

Further Reading

Publications

Australia/New Zealand:

Business Review Weekly

Australian Financial Review

The Bulletin

Personal Investor

Smart Investor

U.K:

Money management.

What investment

Investors chronicle

Stocks

Moneyweek

U.S.A:

Business week

Harvard business review

Kiplinger's Personal Finance

Barrons

Bloomberg money

The Economist

Forbes magazine

Many of the above magazines are available worldwide and are printed in many different languages. Most will also have an associated website. There are many more available, as you will find when you start browsing in the money/business section of your local newsagent.

References

The Financial literacy Foundation, 2008, *Financial literacy: Women understanding money,* Canberra, Commonwealth of Australia.