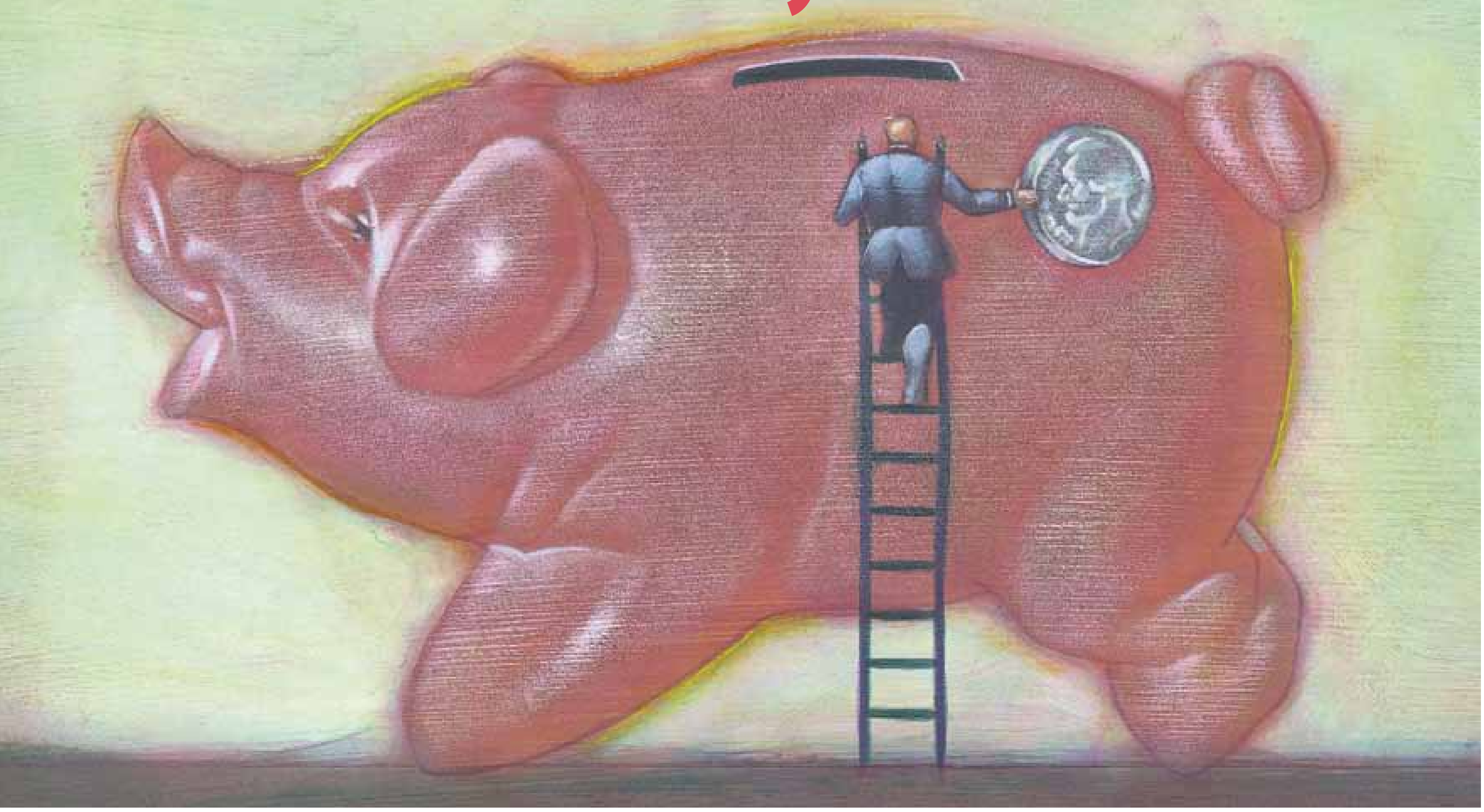
Fighting fear and financial illiteracy



Outside of property, New Zealanders have a globally dismal record when it comes to savings and personal investment. **Craig Sisterson** takes a look at ways to make our money work better for us, both now and into the future

Generally people are scared of investing, says experienced investment manager Christopher Swasbrook, Managing Director of Elevation Capital Management Ltd. The recent negative press about KiwiSaver, coupled with months of dire financial news thanks to the recession, has merely exacerbated New Zealander's long-held distrust and malaise when it comes to personal investment. "People are scared, they don't know where to turn," says Swasbrook. "Financial planners have done them a huge injustice. Finance companies have obviously been a disaster. Other than going to the bank, and putting [their money] on term deposit, they really don't know where to turn."

But simply putting your money in the bank isn't a good answer, says David McEwen, Managing Director of Investment Research Group, a leading provider of investment information and publisher of *New Zealand Investor* magazine. "If you put your money in the bank, yes, your capital is safe, but after tax and inflation, you'll be lucky to make any money at all. You're just holding your ground. If you want to do better than that, you've got to put your money in something else. And that's where [financial] education comes in."

In a 21 February article in the *Sunday Star-Times*, AXA Chief Executive Ralph Stewart said the majority of New Zealanders' savings were in simple bank deposits, in contrast to the rest of the world, where "as confidence and knowledge of savings has grown so has the diversity and depth of savings" ("NZ investment scene a history of 'betrayal'"). And unfortunately our overall lack of savings, and that over-reliance on bank savings (when people save at all), not only hamstrings the financial security and wealth creation of individual New Zealanders but also the wider economy, and country, as a whole.

As a comparison, our cousins across the Tasman have weathered the recession relatively well, not only because of their "incredibly lucky" mineral wealth that allows them to "hitch their wagon to the main global growth engine" of China, says Swasbrook, but because of the "very deep pools of capital" available, created by a better savings culture. "That's why I think KiwiSaver is such a wonderful scheme... You look at what a profound effect compulsory super has had on the Australian economy, and Keating had to drag them kicking and screaming to it," adds Swasbrook, who was a partner at Goldman Sachs JB Were prior to setting up Elevation Capital. McEwen also thinks highly of KiwiSaver. "That's something everybody should be in. It's not every day the Government just gives you $1,000 [to kick-start your investing]."

Getting started

Many people are highly intelligent and very skilled at their jobs, but still neglect saving to build wealth or save for their retirement, because they don't feel very confident about their ability to do that, says McEwen. There are plenty of stories of white-collar workers "slowly going broke on $1 million a year", because despite their high incomes, they are still spending more than they earn, and not investing any of their income for their future.

"The easiest way for somebody who is absolutely, totally, new to investing is to go through a management fund," says McEwen. "And there are lots – unit trusts, for example, are one way to drip feed money in. And a lot of people think 'Well, I'll wait until I've got a spare hundred thou, and then I'll invest that', but life doesn't work like that, not very often anyway. It's better to have some kind of drip-feed, every week, or every [pay], for savings or investment."

Both Swasbrook and McEwen say that investing can be for anyone and everyone. It's about developing an investing habit, regardless of the scale of your contributions. Whether a new graduate, or a more senior professional, simply putting aside even a small percentage of your income regularly, will add up over time, and put you in a far better financial position down the track.

"There's a saying I really like, which is 'pay yourself first'," says McEwen. "Everyone has bills to pay, and so on. But if you get a pay packet and you put some away for yourself into investments, then you're going to get it compounding over time... Then you've got gains on top of gains on top of gains." It's just saving small amounts often, says Swasbrook. "The power of compounding is not something New Zealanders understand very well."

Look long, look wide

The power of compounding is one of the big reasons why people should take a long-term view of investing. "People need to understand that they don't need to take a lot of risk to get good returns over time," says Swasbrook. The greater the time frame you are prepared to invest for, the more compounding comes into play (assuming you reinvest returns), and the better your wealth-building possibilities, even with very conservative strategies.

The other benefit of long-term thinking, rather than trying to "time the market" by aiming to buy low and sell high in big lump sum amounts, is that it allows you to ride out the fluctuations in the economic cycle. "There is a business cycle, which is generally seven to 10 years," says McEwen. "So if you stick with something long-term, like some people building up assets for retirement for example… if the market does go down for a year or two (as it has been doing now), then that's okay if you're thinking long-term and not taking out money now."

"For most people, they are better to try and take the slow and steady approach, rather than getting up to the plate and trying to knock it out of the park," says Swasbrook. "And that's what they forget, I think, when they try to invest into the share market. They all want to get up to the crease and put the ball over the back fence... slow and steady usually wins the race."

Another way to protect your capital (the amount you invest) is to diversify your investments. It's the old 'don't put all your eggs in one basket' idiom. For McEwen, that's why funds, whether managed or exchange-traded index funds, can be a good option for investors, particularly new ones coming in with smaller amounts. As he sees it, if you have $1,000 to invest, you wouldn't be able to buy a diverse portfolio of shares or other investments directly with that amount. However, $1,000 invested into a fund can mean that you have bought a small share in a wide variety of investments (that the fund chooses to invest in). "But you have to be careful of what funds you go into. There are better ones than others."

Making a choice

So how do you choose the fund, or fund manager, that's right for you as an investor?

"A lot of people make the mistake of looking at short-term track records," says McEwen. Just because someone has perhaps headed a 'funds manager league table' as the best-performing funds manager over the past year or two, doesn't mean they can necessarily be relied upon to do the same in coming years. "It's more important to look at their strategies, and ... one of the things you have to watch out for is managers that have a certain mandate, and then they start drifting away from the mandate by trying riskier things to try to get their results up. That can pose risks." The approach of the funds manager, and how their actions match that purported approach, can be as important as how well their strategy has done in the recent past. "Consistency is very important."

As a funds manager himself, Swasbrook unsurprisingly has a strong opinion on what investors need to look for (and watch out for) when making their choice(s). "Choosing an investment obviously requires a lot of due diligence, but if you are going to say 'Right, I don't have the skill-set or the time, and I want to abdicate that responsibility to someone else' [ie a fund manager], then what's the key thing?"

For Swasbrook, the answer comes in two parts: alignment of interests; and being able to understand what the fund manager is talking about. "The overriding thing, above everything else, is alignment of interests. Is the person I am entrusting my hard-earned capital to invested alongside me? And are they invested alongside me on the same terms?" Swasbrook practises what he preaches; he and his fellow directors all have very considerable investments in Elevation Capital funds. "I think that sends a very strong signal to investors that we believe in what we're doing, and that we manage our money the same way we plan to invest yours."

Swasbrook also believes that potential investors should keep diversity in mind when choosing a fund – not just how diverse the fund's own investment choices are, and how they align with the investor's own strategy, but also that a particular fund itself should only be one part of the investor's portfolio. Not their entire portfolio.

Financial literacy

Both Swasbrook and McEwen are keen for more New Zealanders to become more active, and more educated, investors. For the financial and other benefits of wise investing flow not only to the individual, but the wider economy, and nation, as a whole. Unfortunately, financial literacy is currently poor in New Zealand, says Swasbrook. "If I go back to my education, we were taught nothing with regards to [things like] the stock market. The way I learnt ... is I read magazines and books." So, in the coming year, Swasbrook is taking some steps to help improve New Zealanders' financial literacy. He plans to establish a financial literacy programme which he believes will be innovative, and most importantly "will seek to teach young New Zealander's about asset diversification and the benefits of investing for the long term".

McEwen, of course, provides investors old and new with regular information and education via *New Zealand Investor* magazine. But he also recommends books by the likes of Warren Buffet and Benjamin Graham, for those interested in gaining a better understanding of investing. "It's not as scary as people think to make an investment decision, and it's not as complicated as people think," he says.

Readers wanting to further discuss any matters raised in this article, or personal investing in general, can contact David McEwen on (09) 304 0145, or Chris Swasbrook on (09) 307 6741.