Planning in Perth, explains the strategies for 30-year-olds; Jonathan Philpot, from HLB Mann Judd, gives advice for 40-year-olds; Suzanne Haddan, from BFG Financial Services, covers 50-year-olds; and Michelle Smith, from Mercer Financial Advice, looks at 60-year-olds. The younger you start building wealth outside super, the more scope you have for benefiting from the power of compound interest. And there are important tax-effective strategies for later in life too.

The four financial planners were unanimous that the top priority should be paying off the mortgage. Once it is down to 50%, it is time to consider whether to use the equity to gear up to buy an investment property or a share or managed fund portfolio.

Biti likes insurance bonds for high-net-worth earners who are on the top marginal tax rate of 49% (at July 1, including Medicare levy) because these bonds will have a tax rate of 30%, providing a saving of 19%.

The top priority should be paying off the mortgage

"There are some inefficiencies because they are taxed under the company tax law and they don't get any discounts for capital gains." She recommends them for part of cash reserves.

Family trusts suit people with higher levels of wealth and are popular with those who run businesses. But many of the tax benefits have diminished, says Biti. Family trusts are more an estate-planning vehicle.

Biti says negative gearing is increasingly popular with young people aged 25 to 35 who can't save enough to buy their property of choice but want to get into the market. It provides disciplined saving and gives them the opportunity to get started.

It is important for couples to even up their super balances by adding to the partner with a lower amount. Biti says couples need to have common goals about how they manage the household budget.

**The examples that follow are all hypothetical.*

THE 30s

OUR COUPLE: Tim and Rebecca are 30-year-olds earning $65,000 and $35,000 a year respectively. They have one child, Abbey, and hold $35,161 in superannuation.

If Tim and Rebecca both work until 60 with their salaries rising 2% each year, their superannuation guarantee (SG) payments will total $457,800 in 30 years, based on current legislated contribution levels

Working 30-year-olds such as Tim and Rebecca who have a view to retire at 60 are in a fortunate position. The super system, if respected and given the appropriate attention of investors, will provide a more than adequate retirement bucket. Tim and Rebecca will receive employer SG payments of about $457,800 over the next 30 years. When combined with their current balance of $35,161 and annual growth of 8%pa, this should give a superannuation balance of about $1.4 million at 60.

Even better, they could build on this position with some careful money management starting now. The key will be to eliminate their non-deductible debt first and this could be achieved when they are 41½ years old if they put all cash flow surplus into their home loan. I have estimated that their salaries will increase by 2%pa and their bills are around $40,000pa, with living expenses also increasing by 2%pa. They upgrade their car every 10 years and spend $1000pa on whitegoods and furniture plus $3000 on travel. They pay Abbey's fees for six years at a mid-tier high school and stay in their current home, valued at $400,000 with a mortgage of $300,000.

Once the home loan is gone they have these options for their surplus money:

- Park cash flow surplus in cash at 3%pa and they would have about $900,000 in cash outside super by 60. With cash and super combined of $2.3 million (now invested at lower risk to earn 6%pa), they could support a lifestyle of $70,000pa in today's dollars which would last beyond their life expectancy.
- Invest surplus cash in diversified portfolio targeting 8%pa growth and Tim and Rebecca would have $1.4 million in the portfolio at 60 plus super of $1.4 million. This would support a $95,000pa lifestyle in today's dollars throughout retirement and leave a significant inheritance for Abbey. At 55, Tim and Rebecca's assets outside super are $830,000, so this offers an early retirement option or protects them if the preservation age is pushed beyond 60. This portfolio is best in joint names as most growth would be capital in nature and they would benefit from sharing the capital gains tax impact in the future. They could consider an investment bond structure, which saves around $100,000 tax over 18 years of investment to 60, but the costs are higher, so this should be considered along with the extra complexity of staying within contribution limits to achieve the tax concessions available.
- Borrow 100% for an investment property in Tim's name worth around $400,000 in today's dollars and rented for $300 a week, paying off the loan by 58. As Tim and Rebecca only have rent from the property and can't easily access the equity in retirement, they have to draw further from super, which runs out in their early 70s. So the property will need to be sold at some point to support retirement. Also there is the challenge of picking a good property that yields at least 5%pa capital growth to compare favourably with other options. You only get one chance to buy the right property – compared with holding thousands of investments in a diversified portfolio of equities and bonds.
- Contribute pre-tax super up to the contribution caps without reducing Rebecca's income below the tax-free threshold, so personally contributing around $1 million between ages 42 and 60 and saving about $450,000 in income tax. The super balance would be a huge $3.3 million. This would easily support a lifestyle of $95,000pa in retirement. However, they face legislative risk – almost 100% of their wealth is held in super and the government could push out the preservation age, requiring them to work longer. But significant changes are unlikely to occur overnight so Tim and Rebecca could revise their strategy along the way and build further wealth outside super. Salary sacrificing is a flexible strategy that can stop and start in line with changes throughout life.
- I would favour a pre-tax contribution of $10,000pa to Tim's super from now and not wait until the debt is repaid, then split the super 50% with Rebecca, building more equal balances over time, which will help protect against legislative risk. The tax savings will amount to around $2000pa. The cash flow surplus can be diverted to paying off the home loan by age 45. Then, subject to what we know about the preservation age, start maximising Tim's super contribution until 60 and maintain a splitting strategy. This leaves funds of around $20,000pa available to contribute to a diversified portfolio, building a balance of $285,000 by 60 and super of $2.9 million. They don't need this much super at 60, so the strategy could be amended along the way to build further assets outside super. An earlier retirement could also be planned.

The key for 30-year-olds to obtain financial independence and retirement security is to develop their plan early and set realistic lifestyle goals. Compound interest and time are their biggest assets but some people will not even achieve the $1.4 million super balance from SG contributions alone – as they will mismanage their super, either through non-engagement and hence inappropriate asset allocation or through overengagement and taking too much risk, trying to time markets or not diversifying enough. Or they may tackle an SMSF structure with high costs and not achieve steady long-term returns.

BY PIPPA ELLIOTT
Director and financial planner at Momentum Planning (CFP) with 17 years' experience in financial services.

TOP TIPS

Before thinking about wealth creation, ask yourself if your best investment could be to invest in human capital – yourself. Would extra study allow you to move into a higher-paying career? What you earn will have the biggest impact on your wealth generation over time – not what you invest in.

With this done, if choosing to build wealth outside super, focus on the reduction of debt on your home as your first priority.

Ensure your strategy is well diversified and offers the flexibility to change it if your circumstances change. Property is not that flexible, so don't overextend yourself or do this too early – make sure that you will have plenty of surplus cash flow after any property purchase or you may have to sell when you don't want to. Make sure you have income protection insurance.

Focus on after-tax returns (not headline returns) and compare your options fairly. The performance of two stocks over the past five years compared with that of a portfolio of 500 stocks is not apples v apples, as there is a much higher stock-specific risk with the two-stock holding.

You can't control what markets do; you can only control how much exposure you have to markets and they will always be volatile. Just because you have time on your side, this does not mean you should take more risk in the belief that you have time to recover if things go wrong. That is flawed thinking.

If you take less risk, you increase the probability of achieving the return you're targeting and you won't need "knockout" returns to succeed. If you see a high return being offered, look for the associated risk – it will be there somewhere.

Investing should not be your form of entertainment – find another hobby! Sound investing is structured, methodical and disciplined and it's effective. Finally, advice is valuable but if you seek it, research it well and know that if you pay peanuts, you'll likely get monkeys.

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