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# Investing

**Making money work for us**

Putting money back into our pockets

Let's start with the basics

Key questions to ask ourselves

# Quick concepts

## What are returns?

Returns are what we get back in our pocket from investing. These can come from either the change in the value of our investment over time or any income received (e.g. interest or dividends from shares).

## What is risk?

Risk is the chance that we might not reach our goals by investing. An investment may not be as good as we expected or were promised, which means we might not get some or all of our money back, and might not get any income (e.g. from interest).

Risk is also partly about volatility – the ups and downs in value that typically happen with investments. For example, if we invest for short periods of time in a volatile investment like shares, there is a high risk that the investment will be in a down phase when we want to get our money out. Yet over the long term, we have time to ride out the ups and downs and get better results overall.

## What is inflation?

Inflation is the rate at which the prices of goods and services increase over time.

The effect of this is to reduce the buying power of our money. For example, if we put $1,000 under our mattress today, it would only have the spending power of around $800 in 10 years' time (if inflation was 2% each year).

Investing your money is a way to stay ahead of inflation and cope with prices rising in the future.

# Putting money back into our pockets

**Investing is all about making our money work for us. That may sound odd, since it's usually the other way around – we usually work for money.**

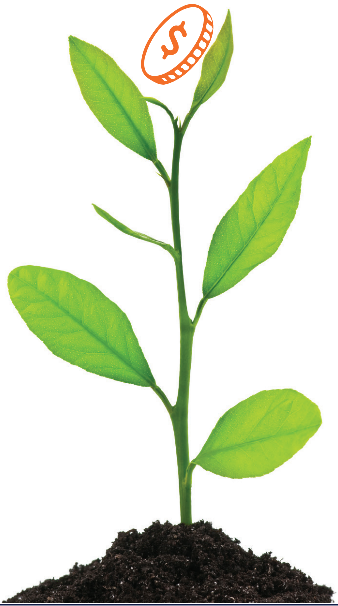
Yet if we have a bank deposit or are in KiwiSaver, we're already investors, since our money is earning us even more money through interest.

We become investors when our money goes into things that can put cash back into our pockets (a return) instead of just draining them like most things we buy. That's what an asset is – something we own that can either give us an income or grow in value so we can sell it for more later on (or both!).

By investing, we're aiming to earn an after-tax return that's greater than any fees and taxes we'll pay, and inflation. Otherwise, our money isn't truly growing and we're rolling backwards instead of getting ahead.

Investing always involves some degree of risk. The higher the returns we chase, the higher risks we take. We all need to be wary of offers promising high returns that don't seem to have any risk! Those are typically scams and therefore the most risky of all.

Try the **investor profiler** on **sorted.org.nz**.



# Let’s start with the basics

**To be successful investors, there are some fundamentals that we can rely on. We’ll need to:**

## Be clear and realistic about what we want to achieve

Let’s think about the financial goals we have, like saving for a car, buying a house or saving for retirement. What goal will investing help us achieve? (For more on setting goals, go to **sorted.org.nz** or see Sorted’s goals booklet.)

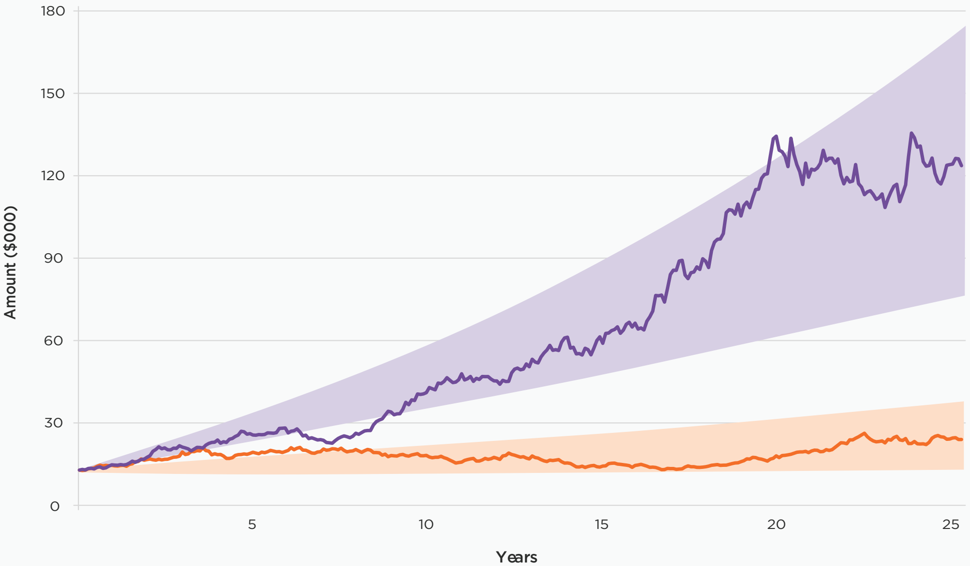
We’ll need to invest in a way that helps us reach those goals. What we are investing for and when we are going to want our money should guide how we invest.

For example, saving to buy a car in two years’ time requires a completely different investment strategy than saving for retirement in 30 years. To save for the car we’d invest in bank deposits that return interest, but to save for retirement we would probably be better off with a KiwiSaver fund that has a mix of shares, property and bonds.

## Understand how investments grow and compound over time

Starting investing early helps. The more time we have, the more the value of our investments can ‘compound up’ – when returns are reinvested and earn even more.

Regularly adding to our investments can greatly improve our results. If we regularly reinvest our returns or constantly drip feed more money into our fund, we’ll see the highest growth.




**Contributing regularly harnesses the market.** The above example shows the vast difference between leaving $10,000 in the share market over 25 years (which here in orange results in just $21,17) and instead adding $50 each week to that $10,000 (the blue line, which here grows to $121,100). Typical results would fall within the shaded areas – orange results would be between $10,080 and $34,730; blue between $74,160 and $170,930. (These figures have been adjusted for fees, taxes and inflation.)

# More basics

## To be successful we'll need to:

### Find the right balance between risk and return

The greater the returns we chase, the more risk we have to be ready to take on.

In the short term, higher-risk investments tend to be more of a roller coaster. Yet over the long term, they typically come out with better results.

A great place to start is to find out what type of investor we are. This is based on the time period we're investing for, our attitude towards risk, and how well we can handle any ups and downs or possible losses.

### Find the right mix of investments

Once we know what type of investor we are, we'll need to find a mix of investments to match (experts call this 'asset allocation'). The four main kinds of investments are cash, bonds, property or shares.

For each investor type, there are typical mixes of these four kinds in the profiler results. Specific mixes of investments lead to specific results, and the profiler also gives an idea of what we can expect.

**Sorted's**
investor profiler
can help

**Online tools at sorted.org.nz**

## Research, compare and review our choices

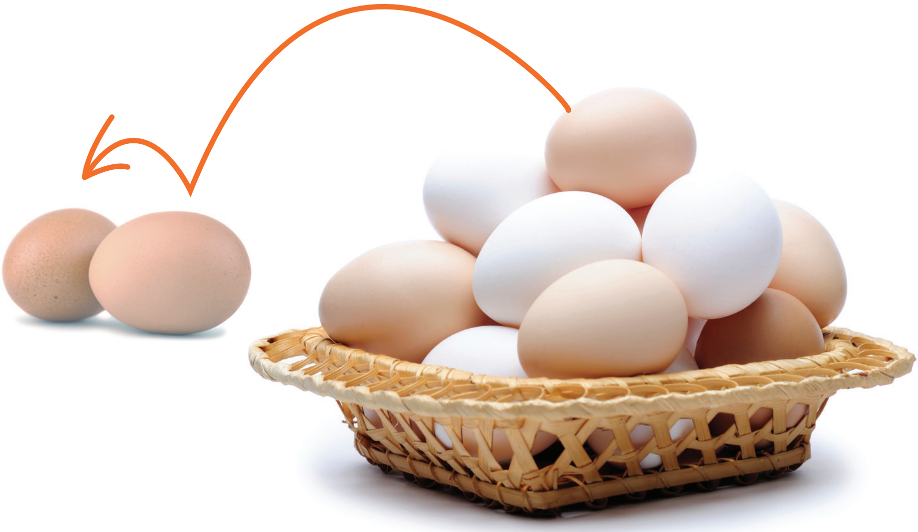
When it comes to selecting the individual investments within our mix, we all need to do our homework, or get a professional to do it for us. Or both!

There are so many choices to make – such as whether to invest in professionally managed funds such as KiwiSaver or to take more of a DIY (do-it-yourself) direct approach.

## Avoid putting all our eggs in one basket

A good way to reduce the risks we take is to spread our money in different kinds of investments (what experts call 'diversifying').

So if we are investing in shares, for example, instead of buying part of just one company (a 'share'), we should buy shares in different companies, a variety of industries and different countries. Some investments may do badly, others will do well.



# Key questions to ask ourselves

## How long are we investing for?

How soon we'll need our money back is one of the most important things to guide our investment choices. (Experts call this our 'time horizon'.)

With investing, short term is up to 4 years, medium term is 4–9 years and long term is more than 10 years (for example, an investment for retirement). It's quite common to have different investments with different durations.

For example, if we're a short-term investor (1–3 years), we'd be better off looking at something more stable that offers consistent returns. If we're investing for the long term (10 years plus), we probably have time to go with the ups and downs of shares and property for the promise of better returns.

## Will we need to get our money out quickly?

How easily we can get our money back when we want it is also quite important. (Experts call this 'liquidity'.)

For example, a bank savings account is highly liquid because we can get to our money easily and probably won't have to pay any penalties for taking it out. Low-liquidity investments include property (because it takes time to sell and is expensive to do so) and superannuation schemes (where our money is locked in until we retire).

## Will we need a steady income from our investments?

If we need regular income from an investment, we're best to put our money where we can have more certainty about the interest it will earn, such as a bank deposit or a bond paying a fixed amount of interest for a set period.

But if we want our money to grow as much as possible, we can consider more risky investments such as shares or property, which potentially offer higher long-term returns but fluctuate in value along the way.

## What are some different kinds of investments?

We need to make sure we understand what options we have, starting with the main kinds of investments and how they work:

**Cash** – investing our money in things like a term deposit from a bank

**Bonds** – lending our money to a government or company and receiving regular interest payments

**Property** – investing in managed funds that hold commercial property or owning rental property (i.e. not the family home)

**Shares** – buying a part of a company (a 'share') and receiving part of the company's profit, either through dividends paid by the company or because the value of the company goes up.

For more on these 'asset classes', see the **investing guides** on **sorted.org.nz**.

## What are the different ways we can invest?

We need to decide whether to invest directly and manage our investments ourselves. It's possible to invest directly through a bank (short-term deposits), sharebroker (shares and bonds), real estate agent (property) or other brokers. Managing all our own investments requires higher levels of research on our part, and we'll need to be well informed.

We can also invest indirectly using managed funds, where our money is pooled with that of other investors and we rely on a professional fund manager to invest for us. There are many different forms of managed funds for different goals – these invest in different types of assets for different objectives – and KiwiSaver is just one example.

**Sorted's**
smart investor
can help

**Online tools at sorted.org.nz**

# More key questions

## What risks are we taking?

No investment or financial institution is entirely risk-free, but the level of risk can vary greatly. If an investment seems too good to be true, it probably is.

The main risk is that our money may not be there when we need it. Our investments could lose value or we may not receive all of our money back.

The more risk we're prepared to take, the higher the returns we should get – but it also means a higher chance of making a loss. Getting the right balance between risk and return is one of the most important parts of investing.

Lower-risk investments like bank deposits are less likely to decrease in value than higher-risk investments like shares. But if we can tolerate higher risk, we'll probably have a better chance of achieving a greater return in the long run.

Some investments like bonds may be given a rating by an independent agency. These ratings are a useful tool as we assess our overall investment risks.

## What costs are there?

Knowing the fees involved with investing is important, since they can eat into the returns we're after. Managed funds usually charge management and administration fees. These can vary a lot.

We also need to know how we'll be taxed on our investments.

Essentially, we need to weigh the fees we are being charged against the likely return we are going to get from our investment. How much seems reasonable to pay?

Fee information can be found in investment statements – clarity of fees is important in judging whether investment is a good one. For estimating the impact of KiwiSaver fees, use Sorted's **KiwiSaver fund finder** tool on **sorted.org.nz.**

## Where can we get advice?

For professional investment advice, you need a financial adviser who specialises in investment, KiwiSaver or planning. A financial adviser is a qualified expert who can:

- Advise you on investment products like KiwiSaver and managed funds
- Draw up a savings and investment plan for you to reach your goals in life, like a home deposit or long-term goals like retirement.

You'll need to check they're licensed as a Financial Advice Provider or working for one. To find out, search their name on the Financial Service Providers Register (FSPR).

It helps to shop around to find the right adviser – they should take the time to understand our financial situations and investment goals, and recommend investments to match.

## How advisers get paid

Most financial advisers are paid by a company (like a KiwiSaver provider) to sell their products, which is common practice. Financial advisers are required to tell you about any commissions or bonuses they get. Feel free to ask.

When they are paid by a company to s ell, the adviser has a conflict of interest. They might, for example, be more focused on selling and less on whether what they're selling is right for you. When there isa conflict though, financial advisers are required to tell you up front and put your interests above theirs.

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## Where to now?

1. Work out our investor type.
2. Learn more about different kinds of investments.
3. Work out what advice we need.

## Next steps:

Try the investor profiler
on **sorted.org.nz**/investor-profiler

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**Notes:**



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