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Jim Fenwicke, Fenwicke Financial Services

Launching Fenwicke Financial Services in April 2009, Fenwicke has held several senior roles within the financial services industry including chief operating officer for Equity Products Australia and head trader for the offshore banking unit for Equity Markets Group at Macquarie Bank.

Fenwicke provides holistic advice and specialises in budgeting, saving and wealth creation strategies, life insurance, investment planning, superannuation and tax, retirement and aged care. He also won the 2011 FPA Associate Financial Planner National Best Practice Award.

GEARING VS SAVINGS STRATEGIES

Jim Fenwicke

Newly-married couple, Tim and Kate, had begun a life together and decided that before they tried for a family, they would need to get their finances on track before life got in the way.

Keen to ensure that they saved surplus income in preparation for buying their first home, Tim and Kate wanted to increase their investment knowledge and experience and make sure their super was invested sensibly. Being in their late 20's, they also had not considered their own retirement or estate planning.

Meeting with Jim Fenwicke, financial adviser from Fenwicke Financial Services, they initially told him that all that they wanted was to make good decisions now that would pay off for their future.

"When Tim and Kate met with me the first time, they appeared young, energetic and motivated. They had well-paying jobs and thought now was the time for smart planning for future life-stage and lifestyle events," said Fenwicke.

Talking with them, the couple said they wanted to capture their savings and move them towards buying their first home.

"They wanted to know they were adequately insured should any misfortune strike. What's more, they wanted to prepare for starting a family as well as being able to assist extended families when they can.

"Tim and Kate also stipulated that that they wanted to maintain their lifestyle, include some overseas travel and be in a position for Tim to follow his business ideas if they decided to go down this path."

Tim had some income protection insurance while Kate had none. A comprehensive risk plan was recommended in separate Statement of Advice.

Creating cash

While establishing their financial goals, Fenwicke decided the first issue to focus on was the couple's cash savings.

"I wanted to set up an effective cashflow management strategy to optimise their financial resources and income position. This was a multistep system including preparing a monthly budget, opening a new high interest savings account and linking this new account with investment accounts to allow for regular contributions.

"We set $15,000 as the goal figure as a cash reserve for unforeseen circumstances."

This system suited their needs as their surplus monthly cash of $5,000 will not be left sitting in a low interest rate environment while using Tim and Kate's credit cards to pay for bills and living expenses would allow them to take advantage of interest free periods.

"This strategy ensures that any surplus income, plus your cash reserve and other funds, are invested in a high interest earning account with no risk."

Commencing a savings plan straight away, the couple began contributing surplus income of $5,000 per month to a high interest savings account in Kate's name.

"As their account balance accumulates short-term term deposits could be used to maximise yield. Based on our projections, they should be able to save 26.5% of the property value and purchase costs ($850,000 plus $50,000) in around 4 years or $225,000 + $50,000= $275,000."

The only drawback was that the returns may be low compared to other asset classes but the couple agreed that they would prefer a safer, secure savings vehicle. See table 1 for estimated projection.

Assets and liabilities		
Assets	**Owner**	**Value**
Life Style / Motor Vehicle	Kate	$10,000
Life Style / Household Contents	Tim & Kate	$20,000
Liquid Assets / Cash on Hand	Tim	$17,000
Superannuation / AMP Flexible Lifetime Super	Tim	$43,750
Superannuation / Virgin Money Super	Kate	$17,200
Total		$107,950
Total Net Worth		$107,950

Income	Owner	Amount
Employment Income (includes $12k bonus)	Tim	$112,600
Employment Income	Kate	$73,000
Total Income	$185,600	

Expense	Owner	Amount
Income Tax	Tim	$31,300
Income Tax	Kate	$16,550
Living Expenses	Tim & Kate	$41,000
Other Expenditure	Tim & Kate	$14,000
Rent	Tim & Kate	$22,440
Total Expense		$125,290
Estimated Cash Surplus/Deficit		$60,310

Changing gears

As an alternative to the savings proposal, Fenwicke also recommended an instalment gearing plan using $5,000 of their own capital and borrowing $5,000 from a margin lending provider. The total amount invested each month will be $10,000. These funds will be invested into a diversified portfolio of managed funds.

"We expect the interest repayments to be met from the distributions and dividends from the investment portfolio. However timing of these payments may cause a drawdown on Tim and Kate's cash reserve over some periods. Ongoing contributions can be reduced in the future if further personal cashflow is required."

According to Fenwicke, this approach suited Tim and Kate as it would accelerate their wealth accumulation process while also using the dollar cost averaging strategy to help reduce timing risk.

"I also spoke to them about the benefits of investing in assets outside of superannuation, essentially providing them with an investment portfolio they can access at any

Table 1: Consolidated cashflow projection: an estimated income, expenses, tax & overall cashflow after implementing recommendations

Date	1 Jul 11	1 Jul 12	1 Jul 13	1 Jul 14	1 Jul 15	1 Jul 16
Age - Tim	30.81	31.81	32.81	33.81	34.81	35.81
Age - Kate	28.78	29.78	30.78	31.78	32.78	33.78
Inflow						
Earned Income						
Tim	112,600	115,978	119,469	123,072	126,788	130,616
Kate	73,000	75,190	77,453	79,789	82,198	84,680
Investment						
Income Paid						
> Bank Account	2,726	6,303	10,117	14,134	672	672
Capital Proceeds						
> Bank Account	0	0	0	0	275,000	0
Financing						
Proceeds from Borrowings	0	0	0	0	625,000	0
Total Inflow	188,326	197,471	207,039	216,995	1,109,658	215,968
Outflow						
Expenditure						
Lifestyle Expenses	41,000	42,230	43,501	44,813	46,166	47,560
Additional Discretionary Spending	14,000	14,420	14,854	15,302	15,764	16,240
Rent	22,450	23,124	23,819	24,538	0	0
Home Purchase Expenses	0	0	0	0	50,000	0
Taxation						
Tim	31,677	32,602	33,945	35,333	36,763	38,237
Kate	17,532	19,325	21,665	24,110	19,855	20,811
Investment						
Capital Investment						
> Bank Account	60,000	60,000	60,000	60,000	0	0
> Principle Residence	0	0	0	0	850,000	0
Financing						
Home Mortgage	0	0	0	0	53,336	53,336
Total Outflow	186,659	191,700	197,784	204,096	1,071,885	176,184
Net Cashflow						
Total Inflow	188,326	197,471	207,039	216,995	1,109,658	215,968
Total Outflow	186,659	191,700	197,784	204,096	1,071,885	176,184
Net Cashflow	1,667	5,771	9,255	12,899	37,773	39,784
Surplus						
Allocated to/from Assets						
> Bank Account	-1,667	-5,771	-9,255	-12,899	0	0
Allocated to/from Debt						
> Home Mortgage	0	0	0	0	-37,773	-39,784

Table 2: Capital projection of gearing strategy

Date	1 Jul 11	1 Jul 12	1 Jul 13	1 Jul 14	1 Jul 15	1 Jul 16
Age - Tim	30.81	31.81	32.81	33.81	34.81	35.81
Age - Kate	28.78	29.78	30.78	31.78	32.78	33.78
Net Assets						
Tim						
Total Investments (incl Super)	43,750	56,140	69,771	84,752	101,196	119,227
Total Liabilities	0	0	0	0	0	0
Net Assets	43,750	56,140	69,771	84,752	101,196	119,227
Net Assets (PV)	43,750	54,505	65,760	77,540	89,872	102,782
Kate						
Total Investments (incl Super)	34,200	103,022	176,685	254,631	62,090	72,593
Total Liabilities	0	0	0	0	0	
Net Assets	34,200	103,022	176,685	254,631	62,090	72,593
Net Assets (PV)	34,200	100,021	166,526	232,965	55,142	62,580
Joint						
Total Investments	0	0	0	0	0	0
Total Liabilities	0	0	0	0	625,000	578,765
Net Assets	0	0	0	0	-625,000	-578,765
Net Assets (PV)	0	0	0	0	-555,062	-498,936
Total						
Total Investments (incl Super)	77,950	159,162	246,456	339,382	163,285	191,819
Total Liabilities	0	0	0	0	625,000	578,765
Net Assets	77,950	159,162	246,456	339,382	-461,715	-386,946
Net Assets (PV)	77,950	154,526	232,286	310,505	-410,049	-333,574

time. Not too mention they can claim the interest on the margin loan as a personal tax deduction."

Based on this strategy, Tim and Kate's net capital position after four years is projected to be $320,000 less $20,000 CGT = $300,000 in today's dollars as a result of implementing this strategy.

For this to work, the couple also needed put in place income protection prior to commencing this strategy.

The risks and implications of this strategy was a point that Tim and Kate wanted to talk through as they were cautious about investing and what the dangers were.

"I explained to them that while they had greater opportunity for capital gains, they also had greater exposure to capital loss and needed to ensure that if interest rates rise, they could continue to service the loan," said Fenwicke.

"But by investing on a regular basis and drawing down smaller loan amounts, I told them they can reduce the risk of margin calls."

If there is a market downturn, Fenwicke did warn the couple that they may be subject to a margin call.

"If this occurs I told them the margin facility provider would contact them and they will be required to repay part of the loan so that the loan balance is restored or lodge additional investments acceptable to the lender to increase the loan limit. Of course, they could also sell part of the portfolio and use the proceeds to repay part of the loan."

See table 2 above for capital projection of gearing strategy.

Super start

Looking at the couple's superannuation, Fenwicke recommended they transfer the administration of their two different superannuation accounts to one wholesale account.

"We completed a comparison of their existing superannuation account and found that by transferring each superannuation account into the new wholesale super account, the combined administration fees will drop by $500 per annum."

Fenwicke also advised Tim and Kate that a more focused investment strategy may result in a higher return on superannuation.

"There were some risks with this approach of course, such as confirming their employers can direct your superannuation guarantee (SG) contributions to the recommended fund, but the main concerns whether either Tim or Kate needed to lodge a notice of deductibility form prior to rolling the contributions over to the new fund to be eligible to claim a tax deduction for contributions.

"They also needed to complete an insurance application for cover being taken out through the recommended superannuation fund."

Future foresight

After completing an assessment of their investment profile, Fenwicke suggested a growth profile for a long term strategic asset allocation target.

"We recommended a portfolio based on an active approach, which is appropriate given their desire to maximise returns in accordance with their stated risk profile."

Fenwicke also recommended Tim and Kate seek professional legal advice to prepare their Wills and the appointment of a Power of Attorney.

"In addition, we recommended they complete a binding death nomination to each other as beneficiary for superannuation accounts using a qualified estate planning specialist."

Advice structure

After explaining to Tim and Kate the difference between advice fees and product costs, which are paid from the investment balance to the product provider to manage and administer investments, Fenwicke charged them an initial advice fee of $2,640.

"This covers the cost of our meetings, analysis, research and modelling, together with the preparation and presentation of this Statement of Advice. This fee will be covered by any up front insurance brokerage paid as a result of putting policies in place."

Tim and Kate will also pay an ongoing advice fee of $2,640 for the management and review of their investment plan.

"Our ongoing advice will cost $220 per month, direct debited." **FS**