MODULE 3: FINANCIAL LITERACY TOOLKIT

Superannuation & Investment Basics

DELIVERED BY RIDHWAN HANNAN, PARTNER,
HANNAN ACCOUNTING
ARISE EMPLOYMENT READY PROGRAM

What is superannuation?

Superannuation (super) is a great way to save money while we work because money is put into the fund every month. Most of the time, money in super can't be paid out until after you retire. This gives people money to live on when they get old. Because of their superannuation, some people may also get a government pension, too.

The purpose of superannuation is to save money for your retirement.

In most cases as soon as you start work you join a super fund because by law the superannuation guarantee makes it compulsory for an employer to contribute a proportion of an employee's salary to superannuation.

What is the current rate of superannuation?

- The current superannuation rate is 9.5%.

How does super work?

The employer's contributions are compulsory contributions. Voluntary or noncompulsory contributions can also be made to a super fund account.

Super works in the following way:

1. For example, if you earn $25,000 p.a., your employer must pay $2,375 (9.5%) into your super fund.
2. The super fund invests the money and any earnings on investments are added to your super account (increasing the amount you have put away).
3. The super fund takes out fees and charges each year from your super account (reducing the amount you have put away).
4. You may make some voluntary contributions to your super fund (further increasing the balance).
5. When you retire, usually at age 60 (this is called your preservation age), you can have the super money that you saved during your working life as well as any investment earnings.

How does super work?

Accessing your superannuation early usually means you must pay more tax than if you left it in your fund until you reach your preservation age.

For example the money will be taxed when withdrawn from the fund, will be classified as income for taxation purposes in that financial year, and will also need to be considered if you are receiving Centrelink payments.

Contact a financial counsellor if you are considering making an application to access your superannuation early. A person can make voluntary contributions to their super fund when they are unemployed and/or when they are working.

They can also receive voluntary contributions from another person. For example, a husband can contribute to his wife's super fund. A self-employed person can choose whether to have superannuation.

Consolidating your super

What issues occur for super when a person changes a job?

- No longer being able to contribute to the previous super fund.
- Different fees and charges are applicable to a new fund.

It can be simpler and cheaper to keep all super in one fund or at least, as few as possible. However before changing funds and/or consolidating super into one fund, it is important to check the costs involved in doing so (for example termination fees) and the changes to insurance cover as the fees and charges associated with superannuation funds can have significant impact on the final superannuation payout figure.

Tax incentives and super

Because the government is keen for people to save via super, a range of government incentives is available to encourage people to invest in superannuation.

1. Tax payable on super investments
2. Government co-contribution scheme
3. Low-income superannuation contribution
4. Tax offset for contributions for a spouse
5. Tax on non-compulsory contributions
6. First Home Super Saver Scheme (FHSS)

Your final super balance will depend on:
- How much you and your employers have contributed.
- How long you have been contributing.
- What investment earnings your super investment has made.
- The amount of tax paid.

Super & Investment strategy

Superannuation funds usually offer a range of investment options. These will be more or less suitable for each person depending on whether they are seeking a short or long-term investment, the degree of risk they are willing to take, and the return they are seeking on their money.

The four common investment options:

- Growth – Generally invests heavily in shares or property. Aims for a high return and therefore risks-high losses.
- Balanced – Generally invests moderately in shares or property and the rest in fixed-term interest or cash (which offers low returns because money can be readily withdrawn). Aims for reasonable returns with less risk than the 'Growth option'.
- Capital stable – Generally invests moderately heavily in fixed-term interest or cash and a small proportion in shares and property. Aims to reduce the risk for a lower return.
- Capital guaranteed – Generally invests 100% in Australian deposit-taking institutions or in 'capital guaranteed' life insurance policies. Your investment and return are guaranteed. This option offers the lowest return, historically only slightly better than inflation.

Investments

Describe what you understand by the term 'investments'

- Savings
- Superannuation
- Term deposits
- Shares

Why do people decide to invest their money instead of spending it?

- Saving for retirement
- Buying a house
- Leaving an inheritance

While saving is about accumulating a certain amount of money for a certain goal, investing is more about 'building wealth'.

Many people assume you must be wealthy before you can invest, but actually, it's the other way around: investing can help to build wealth.

Some people avoid investing because they fear the risk involved, but by understanding the basics of investing you can be better positioned to make your money grow. Professional advice is available to assist individuals to identify investments suited to their personal needs.

Investment and Asset Classes

1. Cash – includes assets that can readily be converted to cash with a lower risk of capital loss. Cash usually means notes but also includes short-term interest-bearing deposits such as term deposits, savings accounts, and cash-managed accounts.

2. Fixed interest (bonds) – includes securities and bonds issued by companies or governments. They earn asset interest over a fixed period of time. Cash and fixed-interest options are sometimes called 'Defensive investments' because they are investments that produce income, but (usually) the original investment does not increase in value. They typically involve less risk to initial capital than other types of investment and therefore generally produce lower returns.

3. Property – includes houses and units, commercial properties, industrial properties, rural properties, and vacant land. All have the potential for long-term capital gain (their value should increase over time) and except for some vacant land, they can generally provide some income from rent. Property investment can be a 'direct' investment where the investor buys and manages the property or 'indirect' through a property trust. Property trusts allow people to pool their money for investment in a spread of properties. The minimum investment can be as little as $1,000 to $5,000 depending on the trust. Property trusts can be listed on the stock exchange.

4. Shares – (also called 'equities') means buying a small part of a public company. Shareholders are usually entitled to a share in the company profits in the form of dividends and any capital growth. Dividends are usually paid twice a year and can be paid directly into an investor's bank account or sometimes the investor can choose to 'reinvest' the dividend back into the company to buy more shares. Shares can be bought 'directly' by an investor or 'indirectly' through a managed fund that holds shares in a selection of companies.

Investment Factors

A range of factors needs to be considered when selecting a personal investment strategy. With so many options available it is important to remember that what is good for one person may not be suitable for another.

Personal circumstance, timeframe, and risk are three critical factors that need to be considered when making investment decisions. This is a similar set of considerations that financial planners take when discussing investment options with clients.

Personal circumstance considers how much you can afford to invest. All it takes to start investing is a small amount from each payday. A large lump sum is not a prerequisite for investing.

Time is one of the keys to successful investing. Short-term ups and downs in the market tend to average out over longer time periods. Longer-term investments can also benefit from compounding interest to increase the investment value.

Risk considers what degree of risk you are comfortable with. All investment has some degree of risk. Generally, if the return expected is above average, the risk involved is above average. Investment risk is normally described in terms of low, medium, and high.