Quest ADVISORY GROUP

Don't short-change your medium-term goals

When it comes to setting financial priorities, medium-term goals often suffer from middle child syndrome, not taken as seriously as the oldest or indulged as much as the youngest.

The serious long-term goal of saving for retirement gets lots of attention, and rightly so. It's super important. And next year's trip to Bali will be so much fun, even if it does drain all your savings.

It's little wonder there never seems to be enough money left over to save for those in-between things you hope achieve in the not-too-distant future. Things such as your children's education, a home deposit, renovations or a new car.

Yet those medium-term goals – for spending approximately three to 10 years away - are just as important to the life you want to create for yourself and your family. So how can you make sure you've got them covered?

Getting started

The first step is to find time to think about your medium-term goals. Write them down with an estimate of what each will cost, your time frame and how much you need to save each month to achieve them. The more specific you can be the better.

These goals will differ depending on where you are in life, but whether you are 25 and saving a home deposit or 55 and wanting to buy a boat, you need a plan. Otherwise you might be tempted to use high interest loans and credit cards or simply borrow more than you can afford.

Next comes the reality check. To work out whether your medium-term goals are achievable, you need to take stock of your current financial situation. Tally your income and expenditure to calculate how much you can afford to save and invest each month. There are plenty of free apps and online calculators that will help you do this.

Also look at what you owe. If you have any high interest debt, such as an outstanding credit card balance, you might consider paying this off first as the interest rate is likely to be higher than the return you could earn on your savings.

Weighing risk and reward

Setting an investment time frame is important because it has a bearing on how much risk you can afford to take. That's because the longer your investment horizon the more time to ride out short-term market fluctuations.

Say you are saving for a holiday next year. You can't afford to risk losing money in a sharemarket correction, so you park your savings in the bank. The interest rate may be low, but your capital is guaranteed.

With medium-term goals you can afford to take a little more risk for a higher rate of return. For example, over the five years to June 2018, Australian shares returned 10.3 per cent a year on average, listed property 12 per cent and Australian bonds 4.4 per cent. Over the same period cash returned 2.2 per cent a year, barely above inflation of 1.9 per cent.[i]

Of course, the exact return you earn on your investments will change from year to year but historically shares and property do better over the medium to long term than cash or bonds.

Even so, the last thing you want is for your investment to fall 10 per cent just before you need to spend the money. One way to avoid this is to spread your savings across a range of investments and asset classes, reducing the risk of a large or untimely loss in any one of them.

Finding a home for your savings

Unlike long-term savings which are locked away in superannuation until you retire, you want your medium-term savings to be accessible. And unlike a bank savings account, you want an investment that will grow in value.

Alternatives you may wish to explore include managed funds and ETFs (exchange-traded funds). These options allow you to diversify your investments across the full range of asset classes and can be bought and sold whenever you want.

Some managed funds allow you to get started with a small initial investment and then make regular weekly or monthly contributions. Depending on how comfortable you are with risk, you could choose a 'balanced' fund with up to 70 per cent invested in shares and property and the rest in fixed interest and cash, a high growth fund with a larger allocation to shares and property, or a conservative fund weighted towards bonds and cash.

Another approach might be to set up a direct debit from your pay into a dedicated savings account and every time your balance reaches, say, $5000 invest in an ETF. Some of the new investment apps allow you to make regular contributions into ETFs tailored to your risk profile, from your smartphone.

If you would like us to help create an investment plan that includes all your important life goals, the long, the short and everything in between, give us a call.

i 'Where will your goals take you?' Vanguard 2018 Index Chart, https://static.vgcontent.info/crp/intl/auw/docs/resources/2018-index-chart-brochure.pdf?20180913%7C160622

Case study

A 5-year home run

Tom and Jess, both 26, want to save a deposit of $80,000 to buy their first home in five years' time. They already have $10,000 in a joint savings account and decide to invest this in a managed fund.

They are comfortable with a relatively high level of risk without being too aggressive. So they select a diversified fund with 70 per cent in shares and property and the remainder in fixed interest and cash, with expectations of earning an average return of 6-7 per cent a year.

After drawing up a budget, they are confident they can afford to contribute an additional $220 a week ($110 each) into the fund which would see them reach their target.

This case study is fictional in nature and is not a reliable guide to future returns.

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