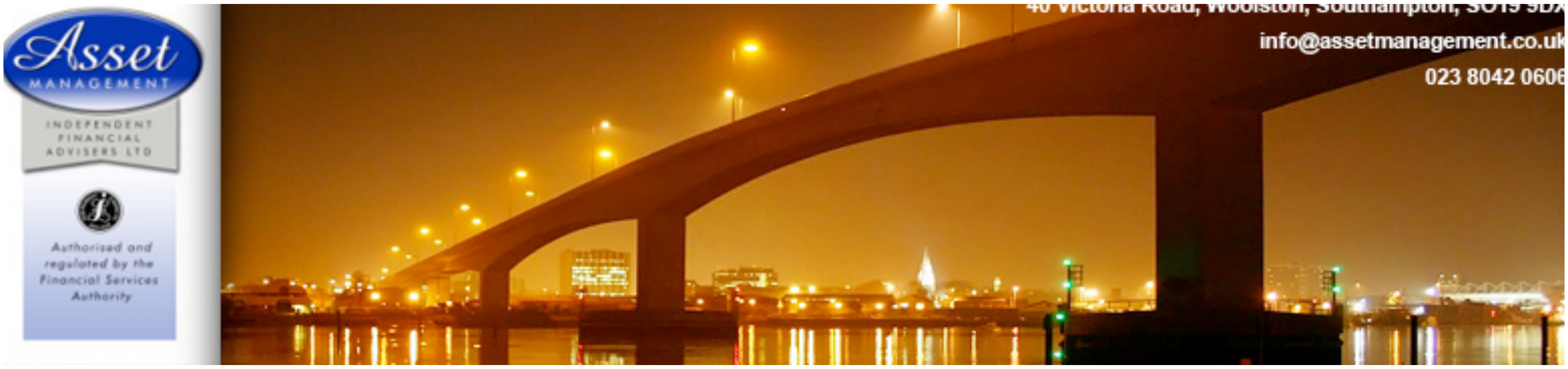

Finance Matters – The Wrap Issue

Last night, my wife and I stared death in the face -- and lived to tell the tale!

Actually, it wasn't quite as dramatic as all that, because we were only confronting the *financial* implications of our inevitable deaths. As a matter of fact, we were completing a questionnaire so that we can have new Wills drawn up (using an expert member of the Society of Trust and Estate Practioners, of course!).

One thing which struck us was how much money had slipped through our fingers during the course of our working lives to date. Alas, I reckon that we've jointly earned perhaps £1.4 million over the past seventeen years, but we've only managed to hold onto a fraction of this sum!

Then again, drawing up a list of all our worldly goods and assets gave us a very clear picture of how much we own -- and how much we need to invest in order to have our first million.

Anyway, later yesterday evening, I explained to a group of students in my local pub that I could take any one of them and make him/her a millionaire before s/he retired. Here's how it can be done:

First, you have to be willing to learn the basics of budgeting and spending, so that you have some spare cash left over to set aside at the end of each month; these fifteen tips will help.

Second, you need to ditch your debts, because there's no point earning, say, 9% a year on your investments while you're paying 20%+ on your credit cards!

Third, you need to build up a cash cushion to fall back on when the chips are down. Personally, I keep about six months' outgoings in a high-interest, instant-access savings account, but anything between three and twelve months' living expenses is fine.

Fourth, you need to take steps to safeguard your future when your plans get blown off course, as they inevitably will. This entails buying some insurance to ward off the impact

of crises and catastrophes -- How To Master Disaster will help you to decide what you need.
Fifth (and this is where the fun finally begins), you need to become an investor. It's up to you to choose what to invest in -- shares, property, antiques, wine or whatever takes your fancy. However, my preference is investing in shares, so I can't and won't tell you how to go about investing in any other assets.

The main reason I invest in shares is that, over time, they tend to beat the returns from other assets, such as property, bonds and cash. Since the Second World War, the UK stock market has produced an average annual return of 11% a year (before taking inflation into account), compared to about 8½% for property, which has been the "in thing" since prices started rising a decade ago.

Another reason why I prefer stock-market investing is that I'm buying stakes in real businesses, so when those businesses do well, so do I, because I'm part-owner of these firms. I also enjoy investing in shares which pay high dividends (the income paid to shareholders), but I reinvest these dividends into yet more shares, in order to add a further boost to my returns.

Lastly, it's simplicity itself to buy and sell shares -- the process takes seconds with an online stockbroker. What's more, fierce rivalry among brokers has markedly reduced dealing costs, bringing low-cost investment to even the humblest investors. Naturally, low charges mean better returns for investors, because less of your money is being gobbled up by transaction fees.

In Ten Ways To Win With Shares, I explained how to invest in the cheapest, simplest stock-market vehicles: index trackers and Exchange Traded Funds (shares which behave like index trackers). Thanks to their ultra-low charges, index-tracking funds beat four out of five fund managers over, say, twenty years. Hence, they are the ideal choice for both beginners and experienced investors -- indeed, about a quarter of City funds are invested in trackers of one form or another.

So, armed with an index tracker, you can easily make a million -- the only question is over what period do you plan to invest? Ten years? Twenty? Forty? The longer you have ahead of you, the more you can make use of the investor's most powerful weapon: time. Over long periods, the effect of compounding (earning interest on interest, and interest on interest on interest, and so on) becomes more and more powerful. Let me show you how compounding works in your favour:
Let's assume that my low-cost index tracker makes, say, 9% a year after charges. In order to make a million within ten years, I'd have to save a whopping £5,234 a month.

Over this decade, my total contributions of £628,080 plus growth of £372,064 would produce a pot worth £1,000,144. Then again, I know almost no-one who can comfortably afford to put aside almost £63,000 a year, so this is a non-starter for most of us!

Let's extend our horizon to twenty years, where annual growth of 9% turns £1,555 a month into £1,000,574. This is made up of contributions of £373,200, plus growth of £627,374, so most of our pot is made up of growth, rather than our own payments. Still, not many people can afford to save almost £18,700 a year, so let's move on again.

Over thirty years, £584 a month becomes £1,001,198, made up of contributions of £210,240 and growth of £790,958. Happily, you can invest £7,000 a year (£583.33 a month) into a tax-free shelter known as a shares maxi-ISA, so this million can be entirely free of tax, which is a plus. Although these figures put us in the realm of everyday reality, let's take one more step.

Over forty years, £236 a month becomes £1,002,917, consisting of contributions of £113,280 and growth of £889,637. As you can see, almost nine-tenths of our final pot (89%) consists of money that our money made for us, rather than money which we paid in. That's why I say that the stock market saves its greatest rewards for the most patient investors!

Alternatively, young people can retire rich by investing, say, a tenth (10%) of their before-tax income throughout their working lives -- increasing this sum every year in line with their rising incomes.

One last thing -- and it's bad news, I'm afraid! The above figures don't take inflation (the tendency for prices to rise over time) into account. With inflation at 3% a year, £1,000,000 forty years from now will be worth under £307,000 in today's money, so you need to understand that a million isn't what is used to be -- and never will be!