ESI-Earn, Save, Invest

MONEY DOES NOT BUY YOU HAPPINESS BUT IT SURE MAKES UNHAPPINESS MORE TOLLERABLE

Below is a paper I have written as a guide for people developing their understanding of wealth and wealth creation principles. I have intentionally kept it as simple as possible and have recommended further reading at the bottom but these key principles are a great place to start.

I hope you enjoy and importantly, learn from my ESI process.

WEALTH

- **What is it?**

WEALTH what is it? When I finished high school I did not know what I wanted to do but I was sure of one thing I didn't want to spend the rest of my life having to do things I did not want to do! I wanted freedom and that to me was what wealth was. For a short time I did desire the symbols of wealth such as cars but I was lucky enough to realize pretty quickly that those things were taking me further away from my dream of a free life full of choice.

My dream was to have as much flexibility and freedom as possible. I did not want to do a job I disliked nor work for someone I did not like and respect.

So it's important to know what wealth is and particularly what wealth is, to you. If we have a clear picture of what our independent life looks like its easier to achieve it…if we have a destination and some discipline there is a fair chance of getting there. If we have no destination we will get wherever society takes us. If you don't choose a future it will be chosen for you.

So what I learnt was that to be wealthy, one must own financial assets that pay you. Not financial liabilities such as cars, boats, planes and fancy clothes that cost you. Those things are traps that stop you getting wealthy.

There is an enormous illusion in society that *STUFF* is how someone's wealth is measured. This is totally false. Wealth is measured by financial assets…shares, cash, property, a business, gold etc. STUFF is a way to show off one's wealth and there is nothing wrong with that but don't mistake a fancy car for wealth!

- **Who wants it and why?**

This is a good point for individuals to reflect on what wealth is to them, and why they want it. There should be integrity behind a desire to achieve. Ideally a desire to achieve is driven by passion rather than fear, greed, jealousy, envy and so on. There are many emotions that drive human endeavour. What ever yours may be, it's a big step ahead to at least understand your internal motivations.

I strongly suggest some self-reflection in order to clarify what you want and why you want it.

- **Who has planned for it and how?**

Start out by being honest with yourself. Do you have a wealth creation plan? If so you can start with that, if not, start from scratch.

As a very simple example of a strategy that most of us use every day to minimise risk and achieve outcomes lets consider driving a car:

Driving a motorcar is a potentially very dangerous activity, evidenced by the death toll on our roads. However, most of us drive a car every day and think little about the potential risk…why is that. Simply put we execute a risk management system that is designed to minimise risk and achieve our goals (get us to our destination). The following steps define this strategy:
1) Use a road safe vehicle.
2) Posses the skills to operate the vehicle
3) Understand the local road rules.
4) Stay within the designated safety driven laws such as speed etc.
If we stick to these rules the vast majority of the time we will achieve our goals safely.
I would like to see every individual have a simple wealth creation strategy as simple and effective as that we employ for driving.

- If you don't understand basic principles of money and have a strategy to manage your financial affairs then you are likely to spend much of your life worrying about money and failing to achieve your dreams and goals.
- Objectives of this paper are to introduce you to the basic principles of achieving financial freedom and help you get started on the road to developing a plan to manage your financial affairs to achieve your goals and minimize stress.

THE BATTLEFIELD WE LIVE ON

We are incredibly lucky to be born in Australia; indeed the odds are about 1 in 300. There is ample opportunity to get wealthy and live the life you choose in this country.

WHY then do we live in a time when 2/3 of people retiring are doing so poor? They are reliant upon their government to look after them. Most of these people have worked for 40 odd years for someone else and have nothing to show for it.

Why do we live in a time when 30,000 Australians per year are filing for bankruptcy and 10,000 more are only just avoiding it by entering into debt repayment agreements? Why do we live in a time when half of marriages fail and the most common reason for arguments and relationship turmoil is money?

WHY?

The majority of these people have jobs! Why are they in so much financial trouble?

I will provide a view below but it's worth reflecting on this reality in your life and that of the people you know. Can you start to see the behaviour and challenges that lead to this phenomenon where so many people are making more money than ever and yet failing to turn any of it into long term wealth. What do you think?

THE ERA OF MODERN SLAVERY

WE LIVE IN AN INSIDIOUS PERIOD OF MODERN SLAVERY THAT IS PERPETUATED BY ITS VICTIM'S ENTHUSIASTIC PARTICIPATION

Most Australians can get a job and we have amongst the highest paid people in the world, particularly at the lower levels. WHY THEN are so many people in financial difficulty?

The simple answer is debt!

Many years ago a man came to see me and a guy I worked with, for financial advice. He earn't a good living but had borrowed to buy two luxury cars, two properties and had accumulated a solid credit card debt by regularly spending more than he earn't. He was incredibly stressed out when he realized one day that he could not fund his debt repayments. He had played musical chairs for too long. After some hard medicine style advice from us, he resumed his denial by taking the family on a credit-funded holiday.

He did not come back to us but I heard that the resultant carnage was incredibly painful and cost him far more than money.

FACT - You cannot spend more than you make for a prolonged period of time without going broke.

For many years I worked with the late Rene Rivkin. One day he was making fun of my financial frugality. I tried to explain that I wanted to be rich and the only way to do that was to save and invest. He had a theory about life that you maximize pleasure and minimize pain and I wont go into all the details but the short of it was he could not control his spending, he was a compulsive consumer who owned 100 cars at one stage, which put enormous pressure on his financial position. Spending all your money just doesn't work because one day it will rain and with Rene it poured. In the end he took his own life, he lost his reputation and his assets leaving behind a real mess. **The great tragedy was it was totally avoidable. He knew how to make money he just could not control his spending he was an addict.**

THE SLAVES ARE WILLING

Our economy may not look like a slave system but the average person works and gets paid in wealth-accumulating currency IE MONEY. That money reimburses them for their efforts and allows them to purchase needs which, is primarily food, cloths, transport, shelter and a few other requirements.

BUT the strong or smart have always enslaved the weak. In the past they have used chains, guns, class systems, laws, religion whatever.

Today they use consumerism and the greatest enslavement tool of all is consumer debt.

What better way to enslave someone than by selling them a car (for example) they can't afford and then lending them the money to buy it. The car starts falling in value immediately. In 5 years the buyer has paid (say) 30% more for the car than the purchase price and its worth less than half that. So a $50k spend has cost $65k, and they have worn $25k in depreciation and paid $15k in interest. If they sell the car and recoup $25k, assuming they have not actually repaid any of the original capital, they still owe $25k. OUCH! The moment that person decided to borrow money to buy something they could not afford they voluntarily made themselves a slave to the lender and compromised their financial position for years if not forever.

Borrowing money to buy a depreciating asset is a financial sin.

Some things like cars cost money, that's a fact but there are (financially) smart and dumb ways to get around.

SO WHO IS THE BAD GUY?

The MAN (for want of a better term) prays on all of us. He knows that buying something nice makes us feel good for a short time and we want to feel good today more than we want to feel safe tomorrow. It works just like a drug. **Consumerism is the greatest addiction in the world today** and the average person's biggest risk to achieving financial freedom.

If you want to see this drug in action go to your local shopping centre on a Saturday morning and you will see Australians participating in their favourite pastime which unfortunately involves surrendering their wealth in exchange for a short term fix that ultimately leaves the consumer wanting more. With the advent of online shopping, there are even more ways the MAN has found to liberate us from our hard earned.

There is an evil in this system that we must first understand before we can overcome. What stops people from being wealthy is (usually) not a failure to make enough money, it's the inability to hang on to it and convert it into assets.

Those who get this game and play it right get rich those who don't get poor.

OK SO THERE IS YOUR CONTEXT BUT THERE IS A SOLUTION AND IT IS ESI!!!

FIRSTLY: CHOOSE TO BE WEALTHY AND MAKE IT A GOAL

If you don't choose your own future someone else will do it for you.

Then build your strategy from the steps below:

1) Maximise your **Earnings**

2) **Save** as much as possible

3) **Invest** your savings with the lowest risk and highest return that you can.

ESI!

STEP 1, Earn.

I am not going to tell you how to do your job better, that's a job for your boss, coach or mentor. However, I will leave you with a number of points that I believe will help maximize your income no matter what you do:

> **Never compromise your integrity.**
> I have a saying that the pain of losing money when trading is much greater than the pleasure of making and this goes for a reputation as well. I have never seen anything more painful than the reputational assassination of Rene Rivkin which, ultimately led to his suicide. I was reminded of this situation again when I watched the third installment of the popular underbelly series. During the Wood Royal commission into NSW police corruption, more than 10 police took their own lives. I also watched Lance Armstrong admit to being a drug cheat and lose everything.

As an employer, I looked for one over riding trait in my team members and that was integrity. People with integrity are punctual, reliable, honest and put in (work hard). They bring a positive energy to the work place that affects others in a positive way.

Warren Buffett suggests that before you make a decision you use the media test. If what you decide, was scrutinized by a smart and objective journalist, how would it look on the front page of the newspaper and all over the web tomorrow?

It takes a lifetime to earn a reputation for integrity and a minute to lose it. I can't put a monetary value on maintaining your integrity because I believe it's too valuable for that. I can't guarantee every other person I do business with will value integrity as I do, it can be a very amoral world. However, I strongly believe it is a smart financial decision and it leads to your internal bank account going up too. Self-respect is as important as dollars in the bank. At least it is to me.

Learn to think like an owner.

If you watch a boss in the work place, very often you will see that they have an attention to every detail in the business. If they see something that needs doing they either just do it or ask someone else to do it. They take a holistic approach to their enterprise with an attitude that *everything matters.* A boss will pick up a piece of rubbish outside the office because they know it all matters.

I remember visiting Gerry Harvey once and hearing the stories of his frugality but it's true. He uses the back of used envelopes as note paper, he had an old desk and wasted no money on things he did not consider important.

Owners see how everything affects the health of a business.

I run my own business and the most valued team members were not the smartest or even the hardest working. They were the ones that thought about the business as a whole. It seems to me that many employees today spend too much time thinking about themselves and their own interests. This does not make them more productive or more valuable to their employers. Of course, ask to be paid a fair wage for what you are worth but it's up to you to increase that price **through** your actions and attitudes. The more valuable you are to a business the better you will be paid and the safer your position.

Think like an owner and make yourself invaluable and ideally indispensable.

Discuss actions and attitudes that reflect an owner-thinking attitude.

Do something you like

It's my experience the most productive, successful and happy people in any field of endevour, love it and don't just do it for money. Do you think Tiger Woods, Steve Jobs or Madonna did it for the money? Passion is the most productive driving force. Warren Buffett (one of the world's richest men) often says he would do his job even if he didn't get paid.

Find a job/field you like.

Work for someone you respect

Working for someone you respect will lead to a more interesting and motivating environment at work. Your efforts at work are helping your boss and the organization you work for, if you respect that organization you will be happier and more productive. Most humans long for relevance and a sense of belonging and to feel their efforts matter and are appreciated and that they are part of something bigger than themselves.

If you don't think I am right, find someone who hates their job and their boss and see how happy and productive they are… NOT.

Keep learning and believe in yourself.

We are all a work in progress, the day we stop growing is the day we start dying. While nature has dealt us a certain hand (we can't all be Jonny Depp, Roger Federer or Bill Gates), we have an enormous amount of potential to grow and improve both as wealth generators and as people and I strongly believe that life's journey is one of self-discovery and improvement.

When I first started public speaking, it scared me (it's often considered the most common fear in society) but I stuck it out and found that I loved it and was quite good at it. Avoid comfortable situations; growth comes from embracing what is uncomfortable.

Give some thought to how you can improve yours skills.

***Develop success from failures. Discouragement and failure are two of the surest stepping stones to success.'* –** Dale Carnegie

THE CLOSER YOU ARE THE HOTTER IT IS

I am going to add one more point here that was the key reason I ended up in the stock market. It's easier to make money where there is plenty of it than where there is a shortage.

When a good manager teams up with a bad business it is the business's reputation that will prevail. Some industries are more profitable than others and people in those industries make more money than those in less profitable industries. A secretary working for a billionaire will almost always get paid more than a nurse working for a cash-strapped public hospital. Money moves via osmosis, if there is plenty around, everyone gets some. The closer to the source you are, the easier it is.

It is worth pointing out that by and large the wealthiest people in our society own businesses. If you have the inclination to own your own business, and you are successful, it is a very effective way to achieve financial success.

Having said that I don't believe you should ever do anything just for money…it kills the soul.

To summarise my first step towards wealth: Maximise your earnings by taking your career seriously. Work for someone you respect, learn to think like an owner, never compromise your integrity and keep investing in yourself.

"Wisdom is knowing what to do next, skill is knowing how to do it, and virtue is doing it" – David Starr Jordan

STEP 2 SAVING

AUSTRALIA'S LOST SKILL

Making money in Australia for most people is relatively easy. It's easy to get a job and most of us are relatively well paid, so the question must be why are so many of us consistently broke?

The answer is simple, as I said earlier, the smartest in our society spend their time and effort trying to remove us from our wealth; some via fraud but more commonly via consumerism. ***The Man*** **knows how we tick. He spends every waking moment of every day coming up with strategies that will convince us to part with our wealth in exchange for making us feel good for a short time.** Once he has us hooked he knows we will be back when the short term high wears off. It's the same system that drug dealers rely upon.

Even governments struggle to save and are dependant upon us spending to prop up the economy and help them fund their irresponsible deficits.

So it's in almost nobody's interest (except yours) to tell you that saving is perhaps the most important skill or discipline you will ever develop in your lives.

A few years ago my beloved mother and my business partner both died. My mother was a school teacher who never made much money but she was a great saver and developed a good nose for property and was not afraid to borrow money if the right investment opportunity presented itself.

Rene Rivkin on the other hand was a pathological consumer who was good at making money and made a lot of it over the years. He probably made more money in an average year than my Mum made in a lifetime.

However, Rene died by his own hand, depressed and bankrupt and my Mum died with assets of $2m and still loving life. Money does not buy you happiness despite what just about every influence in society would like you to believe.

To be wealthy you need to save. I would target 20-30% of your income. Simple as that, if you can't save you can't be wealthy…period.

3 Rules in learning to save:

1) **Save first!** Have your savings taken out of your pay and allocated to your savings account. Live on the balance and I **mean live on the balance**. This strategy removes the ability for you to actually spend your savings; they are put away where you can't easily get at them. Most people will spend what they earn and living on a bit less will not make you less happy.
2) **Never buy impulsively.** *The man* relies upon you acting impulsively without allowing you the time to consider a decision properly. I suggest you avoid putting yourself in situations where you can be impulsive (if you don't have cash nor a card it's difficult to buy anything). I suggest you save for something you may want. By the time you have saved to buy something you may very well find the desire to buy that thing has passed. How much hard earned wealth have you wasted thru poor spending decisions?

Don't waste your wealth by being impulsive. Spend on things that make your life better in the long run but DON'T waste it.

Examples of the long-term impact of poor spending habits :

a) A smoking habit costing $10 a day compounds (at 5% p/a) to $136,000 over 20years.

b) Eating out at $200 p/w compounds (at 5% p/a) to $390,000 over 20 years.

c) How about wasting $100 a week during your 40years of working? It's worth $700,000 when you retire (5% annual compound interest).

3) **Never ever borrow to buy** anything that is not a low risk, appreciating investment. Debt is the ultimate tool of enslavery as I mentioned earlier. There is no better way of taking away a person's freedom than lending them money and having them working hard for you as you charge them interest on the loan.

There are 3 types of debt:

a) Bad debt used to buy a depreciating asset.

b) OK debt used to buy a depreciating asset that can be used to make money (such as a tradesmen might use) and

c) Good debt is used to buy good quality, long-term appreciating assets at acceptable prices.

OK so that's saving and for most working Australians this is the most important step in getting wealthy.

Simple summary:

Save 20-30% of your income and lock it away so you can't get at it.

STEP 3 INVESTING

The magic of compound interest

NEXT once you have saved and accumulated a stake: you move to investing but in this day and age even if you don't save a stake, you are an investor by way of your superannuation so understanding the basics is critical for your long time health.

Investing is the process of putting savings to work. The objective is to preserve capital, maximize growth while minimizing risk.

Warren Buffett says: Rule number 1 is don't lose money, rule number 2 is don't forget rule number 1. And that should always be our first rule when investing. If you lose 50% of your capital, you have to double the remainder to get back to where you started, so it's much, much easier to just not lose it in the first place.

Warren calls compound interest the 8th wonder of the world: So what is it and how does it work?

Simply put when you reinvest your investment income back into your investment it accelerates the growth rate.

$100 invested at 10% grows at 10% in year 1, 11% in year 2, 12.1% in year 3, 13.3% in year 4 and so on. That $100 will double every 7 years.

There are three major asset classes for investing:

1) Cash and bonds
2) Shares/businesses
3) Property

While investing is my passion and there are hundreds of books written on the subject, I'm going to just try to provide a simple introduction here. While I have many, many investing rules, I will endeavour to leave you with three that I hope will help guide you in the future no matter what you invest in:

Starting with a summary:

> Make the effort to develop a simple investment strategy that works for you, which, you can understand and operate. If that means putting the money in the bank on Term Deposit then that is fine. If it means buying apartments within walking distance of Bondi Beach on a gross yield of 5% or higher, then that's fine too but develop a strategy and stick to what you know and understand.

KEY PRINCIPLES

1) **Never commit your money to an investment you don't understand**…ever.

Many years ago my Mum came to me saying her accountant whom she new through church had talked her into an investment that was going to double her money. She showed me the piece of paper, which, I could not understand. I put it to some more senior people I worked with, and they said it did not make sense. It of course, turned out to be a fraud. She was robbed of $40k. **Never underestimate money's ability to corrupt, it can make good people do bad things and bad people do outrageous things.**

2) **Keep it simple**. It's amazing how we humans seem to make things more complicated than they need to be. How often do we hear coaches of professional sports teams talk about the need to bring things back to the basics and just focus on getting those things right?

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3) **Buy in gloom and sell in boom**. While I have so many investment rules, most are about not losing money rather than making it. This one is both, most stock market investors lose money buy buying into booms and selling into busts. The right thing to do is to buy when markets are down and sell when they are up. As simple as it sounds, most do the opposite. Don't get influenced by the herd.

4) **Never underestimate the impact of structural incentivisation**. Greed is incredibly influential; people will do what is in their best interests.

Many years ago Xerox brought out a new photocopier, it was better than its predecessor but it did not sell. Despite attractive pricing and better functionality, the company was not selling them. They asked the customers about the new products but could not understand why they were not selling until someone realised the salesmen got paid more to sell the old models than the new ones.

In another case, (I think it was) DHL has this enormous hub, where all the packages for its delivery system are sent to each night. These millions of packages need to be sorted and resent out in order for parcels to be delivered to their ultimate destinations. In an effort to make the process faster, the company tried multiple strategies to speed up the sorting system at the hub. Nothing seemed to work until someone suggested that all employees got paid per shift not per hour. That meant that as soon as the job was done, employees could go home. Guess what, productivity skyrocketed.

Never underestimate a financial structure's ability to influence people's behaviour.

Who has heard of the GFC? Well the primary cause was flawed structural incentivisation. The people who were selling home loans to home buyers were not in any way responsible for the loans being repaid, so they got paid as soon as the loan was written. They did not care if the borrower could repay or not. Next the investment bank got paid to package up the loans and sell them. They had no incentive for the investments to do well. So they were incentivized to put together as many mortgage backed bonds as they could and sell them as fast as they could by saying anything. The investor's situation was not considered as part of the equation, these people were getting rich by doing something, that's all they could see.

Finally the investors were being driven by greed and not rational decision making although many were completely misled but that's another story.

Investing is a series of decisions you make with your head not your heart. As Warren Buffett says, buy stocks like you buy groceries not like you buy perfume.

PSYCHOLOGY

Money is an incredibly emotional issue for most people. If you don't understand your emotions around money, it's unlikely you will ever develop an appropriate system to help you attain financial freedom.

This is a process of self-discovery and examination. Try to step back and look at your self and your actions objectively in regards to what you do with money.

There is a legendary trader called Ed Sakota who once said that everyone gets what they want from trading. I think money is the same. Be very clear what you are trying to get from spending your money. Understanding this driver is a great piece of knowledge to help your investing success.

SUMMARY

Getting wealthy is ESI.

First decide what wealth is to you, formulate a plan around the 3 components:

Step 1 maximise your **earnings**

Step 2 have a **savings** plan.

Step 3 **invest** your capital sensibly

And the OUTCOME will be financial freedom barring some left field influence but I will guarantee that if there is some huge left field influence those with savings will be in much better shape to survive than those with debt.

Good luck!

FINAL PICTURE

Governments in the western world will increasingly struggle to fund traditional pensions. As populations age, costs will explode and taxes from a shrinking work force will not keep up. We must look after ourselves.

Right now: 2/3 of retirees are retiring broke. That means they are full recipients of the old age pension.

More than 1/3 of older Australians are planning to stay in the work place till at least 70 years old. Is this by choice?

The average super balance for workers aged between 55 and 64 is $71k. I estimate the balance would need to be more than 10 times that (around $1m) to be secure in retirement.

McKinsey Global Institute survey found that average total debt (private and public sector combined) in 10 mature economies rose from 200% of GDP in 1995 to 300% in 2008.

In the 1950s US household debt was close to zero, in 2013 it was about $13 trillion. Household debt as a % of household income has exploded from 68% in 1980 to 112% in 2011.

This trend reflects the addiction to spending in the modern society and is the measure of the extent of modern slavery as I have defined it.

The short-term nature of our electoral cycle supports short term over spending by governments too without an equal consideration for the long-term ramifications. The majority of people I have spoken to, do not trust politicians nor believe the Govt is good at financial management yet entrust their future to Governments via pensions without adequately preparing for the potential risks that come with an unpredictable future.

Government debt has reached such a scale that Government debt default appears inevitable in some countries but there is no easy way out of a large debt burden, the future will suffer no matter what strategy is pursued. The outcome of this trend is innately unpredictable. People should prepare for the potential negative changes to the world we live and work in.

Recommended reading for an introduction to wealth creation principles:

1) The Richest Man in Babylon by George S. Clason
2) The wealthy Barber by David Chilton
3) Rich dad Poor Dad by Robert Kyosaki
4) The Millionaire Next Door by William D. Danko

This is a list of books I have enjoyed and learnt from over the decades and are easy and entertaining to read. There are many others that may be as good; I have simply chosen a selection I have found memorable.