ISSUE 10 | VOLUME 10 | May 31, 2020

YAMAN Coach

EMPOWERING YOU

Debt is not Death

by Coach Rose D. Gases, RFP®

DEBT.

A four-letter word which associates to evil, fright, panic, alarm and even a curse. Many debt-laden individuals and societies incontestably define it is the worst innovation of the humankind. Yet some people resolved this financial enigma in their favor.

They call it 'leverage.' Leverage is using other people's money, time, and effort with the goal of multiplying the potential returns to one's own pursuit in spite of the risk of losing a good portion of capital.

Take the case of a company that plans to build a new plant with state-of-the-art facilities. They can either raise funds through raising new capital or contracting debt. In turn, debt can be contracted through loans and issuing bonds to the public. The finance department will come up with the cost-benefit analysis for the appropriate financing mix.

Or take the case of an events planner who uses his credit card to purchase a high-grade digital camera and drone that his team can use on their e-sessions (engagement sessions). The advanced camera allows the events planner to take excellent videos of current clients that he can use, with expert editing, to further promote his services on social media.

Or take the case of an IT programmer who is looking for other ways to augment her income. She thought of using her skill in developing websites for her small business owner friends. Having no laptop of her own, she buckled down to churn the numbers to see if she could quickly recover the cost of buying a new laptop through a credit card with various pricing strategies. She decided that she would have a 3 month payback period. She would later find out that her financial projections panned out. Now she is using her extra income to create more projects where she can earn more.

Or take the case of this individual who owns a vacant lot near a bus terminal. He knows the real estate industry well and his lot is on a high foot traffic street. He concludes that his vacant lot is a perfect spot for entrepreneurs who need space to capture the foot traffic market. He plans to take out a bank loan to help in the construction of a commercial building for lease.

Debt is not bad. In the book, "Pwede Na! The Complete Guide to Personal Finance", debt is only death for those who abuse it. In the previous examples, debt was not used for mere consumption but as an aid to the business equity to acquire earning assets. Please note that for each venture, financing was not sourced purely from debt as each business already had capital invested. And before the debts were contracted, a thorough study was conducted foreach possible venture.

To sum things up, leveraging was the strategy that dispelled debt as being evil, frightful, panic- and alarm-causing, and even a curse. This is what is called GOOD DEBT.

Credit is a tool that can work wonders for a good and responsible borrower provided proper consideration is given to interest cost, financing mix and other attendant risks.

Now, should you use leveraging for investing in financial securities? This is called margin and will be a topic of future articles by other **YAMAN** Coaches.

.

Coach Rose is a Registered Financial Planner with an AB Mass Communication degree cum laude from Adamson University. She may be reached at rose@personalfinance.ph.

Retirement Planning 101 (part 2)

by Coach John Hero A. Salvador, RFP

I have mentioned the importance of knowing the time horizon, specifying two concepts on time horizon which are important to retirement planning –years to go before retirement and length of retirement (before the retiree moves on to the next life).

The number of years leading up to retirement heavily impacts the savings and types of investments a person who is preparing for retirement can get into while the length of retirement provides the idea on the total cost of retirement.

We have heard the notion that the earlier one starts preparing for retirement, the better. This is due to the ability of investment returns compounding for a longer period of time (and can translate to lower periodic investments).

As an illustration, suppose a starting investment of Php100,000.00 with a 6% p.a. return. After 10, 15, and 20 years, the future value of that starting investment would approximately be Php179,000.00, Php240,000.00, and Php321,000.00, respectively. However, even without any starting investment, small periodic investments of would be needed to reach the mentioned future values as shown below assuming a 6% p.a. return:

Years / Future Value	10	15	20
179,000	13,580	7,690	4,866
240,000	18,208	10,311	6,524
321,000	24,354	13,791	8,726

Having a longer time to prepare for retirement also gives the possibility to have exposure to assets with higher possible returns albeit with higher risk. People tend to have a propensity for risk-taking the older they get (remember that investing should continue throughout retirement). The last thing a potential or current retiree wants to hear is the value of his/her nest egg decreasing due to drop in market value of investments.

We are familiar with rules of thumb for asset allocation and example of this is the rule of 100, wherein the difference between 100 and age of client should be the portion allocated to equities. This rule provides only a general idea and should not be applied blindly. Numerical simulations with values and assumptions client is comfortable with should be the guide when planning for retirement. It cannot be overemphasized that consideration should be given to the risks associated with investing and that retirement plans should be revisited at least every year.

As mentioned, the estimated length of retirement also plays a huge part in retirement planning. Take note that the average lifespan of males and females in the Philippines is around 69 and 73, respectively. This life expectancy is expected to increase with the advances in healthcare and with people leaning towards healthier lifestyle practices. People tend to have a more pronounced fear of "dying too soon" when "living too long" or outliving retirement funds is also of concern. It would, therefore, be advisable to add a few more years of allowance to life expectancies.

As with the general scheme for financial planning, a holistic picture of retirement living – having a clear picture of desired retirement lifestyle allows for realistic simulations when estimating target retirement funds. Think of SMART goals (specific, measurable, attainable, relevant, time-bound) applied specifically to retirement.

To be continued…

Coach Hero is a Registered Financial Planner with a BS Chemistry degree cum laude from UP Diliman. He may be reached at hero@personalfinance.ph.

Editor's Note

Efren Ll. Cruz, RFP®
Editor-in-Chief

UNDERSTANDING TRADERS AND INVESTORS

The addition of 2.5 million jobs in May 2020 is to be expected as the US reopens. It will not lead to an immediate V-shaped recovery in 2020 because of the damage that has already been done.

But it seems that investors are already looking at 2021, making it look like prices are decoupled from the true state of the US economy. Traders and investors are always forward-looking.

A similar thing happened before in the Philippines when expectations of a high GDP growth number that was soon to be reported pushed the PSEi from 5,700 to around 7,300. Then, on the exact same day that the rosy GDP number was announced, the PSEi started its almost freefall, landing back at 5,700.

In a way, seasoned stock traders are not being manic-depressive. They are just doing what their DNA tells them to do, which is to buy low (especially when there is the proverbial blood in the streets) and to sell high. They know that the most money is made by being a contrarian.

The seasoned investor, for his part, just loves to buy during bargains especially since he is looking way into the future, and in this case even beyond 2021.

It is the uninformed investor who just goes with the flow, who lets his FGHIs (fear, greed, hope, ignorance) define his investing strategy and tactics who usually ends up getting trampled upon.

PFA EVENTS