GYC
Grow Your Capital

14 June 2015

Important Financial Advice for Young Working Professionals

by Aw Choon Hui, Deputy CEO

Quotes from this article were used in the article "Got your first pay-cheque? Start saving" in the Invest section of The Sunday Times on 14 Jun 2015. Photo credit: Monica Zhuang.

Earning your first paycheck can bring with it the dizzying thrill of financial freedom. Young professionals just entering the workforce may not always be aware of how to responsibly manage their newfound financial power, and so here we present a few guidelines on how to lead a fiscally prudent life.

Living within your means

Unfortunately, this piece of common sense is not very common. Many people spend far more than they earn on things they do not really need, pressured to keep up with their peers or seduced by slick advertisements promising a better, more satisfying life if you only buy their products. We are immersed in a consumerist culture dependent on making us perpetually insecure and dissatisfied with what we already have, and it can be difficult to escape its lure.

© GYC Financial Advisory Pte Ltd - All rights reserved. Not to be distributed, reproduced or copied without permission.

However, living within your means is a basic tenet of your entire financial plan. Learn how to prepare a simple budget and stick to it. Make a firm commitment to not give in to the pressures of materialism with its ultimately empty promises of fulfilment. If your friends snub you for the clothes or shoes or car you have, get better friends who judge people on less superficial measures.

Investing

Investing need not be complicated. The rule of thumb is to never invest in what you do not understand, or in anything that seems too good to be true. That said, it is highly recommended that young working professionals take the time to learn and understand the basics of investing. A strong foundation in the basics will help you be more critical and avoid being taken in by scams or ill-advised investments (of which there are plenty – emu investing, anyone?). At the same time, you will discover how to take advantage of powerful, time-tested investment concepts like compounding, dollar-cost averaging and asset allocation.

Most young professionals avoid investing because of lack of knowledge, risk aversion or just having too many demands on their limited resources. Many use the excuse of wanting to wait until they have acquired more money with which to invest. This is a serious mistake. Each year that goes by is an additional handicap on your ability to grow your future wealth, for time is your most powerful asset in investing. While investing has its risks, so does doing nothing, for inflation will continue without fail to decrease the value of your savings – a confirmed loss, versus the potential gains of being in the market.

Risk aversion often stems from a lack of knowledge about how the market works. That is why education is important. You need to know enough about equities to feel comfortable investing in them, simply because you cannot afford not to. This is not to say that you should put all your savings on equities; but you need to start somewhere, and then slowly increase your exposure as you get more familiar with how the markets behave.

The moment you start earning an income is the moment you should start investing for the future. Ideally, you should set aside 15 to 25% of your monthly income to invest into a basket of global funds (either unit trusts or ETFs). Avoid direct stocks, unless you enjoy spending significant amounts of time studying and monitoring your stock portfolio.

It is important to be aware of how your investments are expected to behave in both up and especially down markets, so that you can be prepared regardless of which scenario unfolds. Greed and fear are powerful emotions that could potentially destroy your investments. You need to be able to recognize their influence and avoid making rash decisions – in refusing to take profits when markets are high due to expectations of more returns, or panicking and selling when markets have collapsed. A good case in point is the Global Financial Crisis of 2008 when many investors sold out at the bottom and realized losses because market commentators were predicting further declines. The strong market rally that began in March 2009 took many investors by surprise, but they did not get back into the market until much later, missing the chance to regain their losses.

Find a good financial adviser to manage your investments. Ask them about the processes they have to manage market downturns. Who would manage your investments in the advis-

© GYC Financial Advisory Pte Ltd - All rights reserved. Not to be distributed, reproduced or copied without permission.

er's absence or departure? What is the adviser's and firm's track record in managing investments? Are they diligent with regular reports and updates? Do they have a proper process and transparent system?

Emergency Fund

Everyone should try and build up an emergency cash fund comprising at least 6 to 12 months of one's average monthly expenses. This will become crucial in the event you cannot work, for instance if you lose your job or encounter unforeseen emergency situations. Set this money aside in savings or a fixed deposit that you can access in a hurry. Once you have this emergency cash fund, the rest of your savings should be invested.

Basic Insurance

Insurance is one of the most amazing financial instruments available – where for a small sum of money, you are promised a much larger sum should death, disability or critical illness occur. Although there are many types of insurance out there, every young professional should aim to be covered by at least the basic types:

1. <u>Hospitalisation Insurance:</u> This type of insurance would cover most of the expenses should you need to be hospitalised. With the rising cost of healthcare in Singapore and around the world, this is one type of insurance you cannot afford not to have. At minimum, you should get an Integrated Shield Plan (soon to be replaced by Medishield Life integrated plans). This would cover catastrophic medical expenses that would otherwise have to come out of your savings. (Note that you can use your Medisave funds to cover the premiums of some of these plans.) It is important to sign up for a plan as soon as you are able and when you are in good health, for your options and coverage would be severely limited should you try and sign up only after being beset by chronic medical conditions.

2. <u>Critical Illness Insurance:</u> This type of insurance will pay you when you contract any critical illness that is covered on the insurer's list, e.g. cancer or heart attack. The insurance payout would be for you to spend as you like – perhaps to cover the cost of overseas specialist treatment, or to take a few years off work to recover from the illness. Without this coverage, you would need to dip into your savings at a time when you can ill afford to do so. Like with hospitalisation insurance, it is vital that you get covered while you are still in relative good health. Developing any medical condition could render you uninsurable. However, critical illness insurance is generally more expensive than most other types of insurance, and it would be best to get it as a rider to a whole life policy.

3. <u>Life Insurance:</u> This type of insurance is especially important when you have dependents (spouse, children, parents) who rely on your income to put food on the table and a roof over their heads. The principle is that should you suddenly pass away or be permanently disabled, the life insurance pay out should then be sufficient to still pay for the necessary living expenses so that life can continue on as close to normal for your dependents.

The above types of insurance would help alleviate the financial (and emotional) burden

© GYC Financial Advisory Pte Ltd - All rights reserved. Not to be distributed, reproduced or copied without permission.

should you contract a serious disease or pass away. Without this, there would be the added stress of worrying how long your meagre savings would last or the guilt of using up your parent's or siblings' precious savings to pay for your medical treatment, especially if the illness is protracted.

Depending on your personal situation, there are also other types of insurance that you should consider as you begin to earn more. A good financial adviser would be able to help you with a roadmap. Remember that a wise person always insures what he/she cannot afford to lose, one of which is your future income.

Buying your first home

Buying a home is probably the single most expensive undertaking in one's life, and is a decision that needs to be very carefully considered. For most young working professionals, the cost of buying a house is probably way out of your means – due to the large downpayment required, and regular mortgage servicing commitment. Stay with your parents for as long as possible or until you get married. Even if you do get married, if everyone is agreeable, it would be financially best for you and your spouse to continue living with one set of your parents; that way, your savings will have more time to grow before you make the huge withdrawal necessary for a home.

However, if you can afford it and really want to buy a property, consider the following:

1. Property prices have cycles. Buying at the top of the cycle is extremely foolhardy, and can result in financial misery for a very, very long time. Do not underestimate the potential severity of this. In the Asian Financial Crisis, when property prices suddenly plunged, those who had bought at the top of the cycle experienced 'negative equity' – when the price of one's property falls lower than the bank loan. Banks might then ask you to reduce your loan amount with more cash, or else face foreclosure. And this could happen at a time when you could be facing retrenchment or a pay cut, as companies struggle to keep afloat. All in all an entirely unappealing prospect!

2. Watch interest rates. With the current low interest rates, mortgage repayments look deceptively affordable. This can change overnight if interest rates rise, so never over-commit on the purchase of a new house. Build in some buffer, so that when mortgage repayments get revised upwards, you can still afford the higher monthly repayments.

3. Buy as cheaply as you can for your first home. A HDB flat is good value for money. Whatever money is saved from being sucked up by monthly mortgage repayments can instead be used for building future capital and your war-chest, allowing you to take advantage of opportunities when property prices crash and you discover your dream home being sold at a depressed price!

Final Tips

I strongly recommend that every young working professional find a few older persons whom you trust and respect to form your unofficial board of advisors or mentors. Buy them lunch

© GYC Financial Advisory Pte Ltd - All rights reserved. Not to be distributed, reproduced or copied without permission.

from time to time, and tap on their wealth of experience to help you in your own decision making – be it in financial or career and other life matters. This could help you avoid many painful and expensive 'tuition fees' in life.

A second often overlooked consideration is that your spouse is often a major determinant of your financial future. If you marry a person with expensive lifestyle habits and tastes, you are setting yourself up for financial disaster if your combined salaries cannot support the level of luxury he or she desires or is used to. On the other hand, a wise and prudent spouse will help keep your spending in check, inculcate good financial habits in your children and set aside enough for the future.

www.gyc.com.sg enquiries@gyc.com.sg +65 6349 1441

GYC is a licensed Financial Adviser, Registered Fund Management Company (RFMC) and Exempt Insurance Broker.

GYC Financial Advisory Pte Ltd | Co Reg No: 199806191-K | 1 Raffles Place #15-01 One Raffles Place, Singapore 048616

IMPORTANT NOTES: This document may not be reproduced in any form without the express permission of GYC Financial Advisory Pte Ltd. The above information is strictly for information purposes and should not be construed as an offer or solicitation to deal in any product offered by GYC Financial Advisory. Any such investment products offered by GYC Financial Advisory are not obligations of, deposits in, or guaranteed by GYC Financial Advisory Pte Ltd. Any investment product, including investments in unit trusts, is subject to investment risks, including the possible loss of the principal amount invested. Investors may wish to seek advice from a financial adviser before making a commitment to invest in any investment product. In the event that an investor chooses not to seek advice from a financial adviser, the investor should consider whether the investment product is suitable for him or her.

© GYC Financial Advisory Pte Ltd - All rights reserved. Not to be distributed, reproduced or copied without permission.