Saving and investing
The ultimate power couple

Morningstar Investment Management South Africa

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For Financial Advisors and their Clients

When you earn and/or have money, you have the ability to control how you spend it, save it and/or invest it. This is where the cardinal rule comes into play of making sure you control your money, instead of your money controlling you.

Let's first consider the difference between saving and investing.

Whether you set aside extra money in a physical piggy bank or your bank account, the act of **saving** is simply storing away any extra cash to use later. People save for various reasons, but the ultimate reason is to gather a certain amount to spend later or ensure a comfortable retirement.

Investing involves putting money into instruments like shares, bonds, property etc. to achieve a certain goal. Different investments have different risk and return profiles, so an investor's portfolio will vary based on the goal.

The magic really happens when you combine the two

Yes, having cash in the bank is a secure way of gaining access to your savings quickly. There's also comfort in knowing that the amount you have in the bank, is yours to keep and unless you withdraw or spend this money, the value shouldn't decrease. Whilst this is true, certain factors impact the value of your cash in the bank –

- Inflation erodes the value of your money over time, meaning, you'll be able to purchase less with your money as time goes on.
- Savings rates on bank accounts barely beat inflation

Investing has its risk too, but you get to decide how much risk you would like to take on. In theory, investors that take on more risk should be compensated for taking on this risk with higher returns. Investment risk[1] is the possibility that an investment's actual return won't match its expected return.

It's daunting to think about saving versus investing your money. Those already invested have seen (and felt) the impact of poor returns over the past three years. Those that are thinking about investing keep reading about the doom and gloom of the foreseeable future in the media.

The key is just to start, and once you do, you'll realise it's a lot easier than it seems

Unfortunately, the harsh reality is that without savings, no returns are possible. The old saying "money doesn't grow on trees" remains true. However, you can grow your money when you

[1] Source: Morningstar "What is investment risk"

save and invest wisely. Working toward securing your financial well-being is one of the most important and rewarding goals you can have. The great part is you don't have to be a genius to do it.

Every successful investor starts with the basics. Only a few people stumble into financial security by, for example, inheriting a large sum or winning the lottery. For most people, the only way to attain financial security is to save and invest and thereafter, wait patiently for their money to compound over time.

As boring and uninspiring as that may sound, there is something remarkable about it too. Regardless of how much you invest, if you just have the patience to let your investment compound and the discipline to continue saving through good, bad and boring times and to not get distracted, you will be amazed by the power of compounding over time. It is in fact, the eighth wonder of the modern world. In a way, it is the factor that levels the playing field for those that don't make millions with a tech start-up overnight.

The minimum requirement to save can be as little as R500 or even R100, depending on what vehicle you choose. You may ask, what if I don't have any money left after spending? Once you start analysing what you spend your money on, you will be surprised how small everyday expenses (that you can do without) add up over a year. If you save as little as R200 per month, you can set yourself up to become a millionaire – more on this in our article "How to become a millionaire". In the following article "How can I save when I have nothing left to save at the end of the month" we share some tips on how to find areas where you could save more.

Many people get into the habit of saving and investing by following the basic rule of thumb - always pay yourself first and spend what is left. The easiest way to get into a habit of consistent saving is to set up a debit order with your bank to automatically redirect money into a savings or investment account.

Lots of people do ask "what is the point of saving if my rate of return is sub-par"?

The amount saved is more important than the returns generated

At the end of the day, money can only grow if it is saved. We all want the best-performing portfolio but the reality is that performance is only one of the components on the journey to wealth creation. While you can't control how markets will perform and/or your investments, you can control the amount you save every month.

The table below shows you the end value of investing a certain percentage of your disposable income every year for 30 years.

- On the left-hand side, we show you the rate of return assumption, and at the top is the percentage you have saved of your disposable income.
- We use the assumption that the investor's disposable income is R500 000, that it remains unchanged for 30 years and we have made no tax assumptions, to keep things simple.

Amount saved	5 000	10 000	15 000	20 000	25 000	30 000	35 000	40 000	45 000	50 000
	% of Disposable Income saved every year for 30 years									
Rate of return	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%
1%	173 924	347 849	521 773	695 698	869 622	1 043 547	1 217 471	1 391 396	1 565 320	1 739 245
2%	202 840	405 681	608 521	811 362	1 014 202	1 217 042	1 419 883	1 622 723	1 825 564	2 028 404
3%	237 877	475 754	713 631	951 508	1 189 385	1 427 262	1 665 140	1 903 017	2 140 894	2 378 771
4%	280 425	560 849	841 274	1 121 699	1 402 123	1 682 548	1 962 973	2 243 398	2 523 822	2 804 247
5%	332 194	664 388	996 583	1 328 777	1 660 971	1 993 165	2 325 360	2 657 554	2 989 748	3 321 942
6%	395 291	790 582	1 185 873	1 581 164	1 976 455	2 371 746	2 767 037	3 162 327	3 557 618	3 952 909
7%	472 304	944 608	1 416 912	1 889 216	2 361 520	2 833 824	3 306 128	3 778 431	4 250 735	4 723 039
8%	566 416	1 132 832	1 699 248	2 265 664	2 832 080	3 398 496	3 964 912	4 531 328	5 097 745	5 664 161
9%	681 538	1 363 075	2 044 613	2 726 151	3 407 688	4 089 226	4 770 764	5 452 302	6 133 839	6 815 377
10%	822 470	1 644 940	2 467 410	3 289 880	4 112 351	4 934 821	5 757 291	6 579 761	7 402 231	8 224 701

Source: Compoundadvisers.com "Why saving is more important than investing"; Adapted by Morningstar Investment Management. Data as at 28 September 2022. Note: The table assumes no taxes on investment gains and a constant disposable income of R500,000. For illustrative purposes only.

What does this teach us?

- If you generate a 10% per annum return for 30 years, but you only save 1% of your disposable income (in other words, R5000) you end up with R822 000 – displayed in the red block.
- On the other hand, looking at the top right section - if you generate an investment return of only 1% but saved 10% of your disposable income you end up with R1.7 million (as displayed in the green block).

This shows how extremely important the habit of saving is; and that you can end up with a 111% higher ending balance if you save 10% compared to saving only 1% - even though the annualised investment returns were 9% lower!

In conclusion

Life is a constant balance between giving in to the ease of procrastinating or overcoming the pain of discipline. The same goes for our finances. Leave it up to chance, or act today and get your ducks in a row? What is life, if not the sum of a hundred thousand daily battles and tiny decisions that can shape the future of our financial success?

Start today. It's easier than you think and the reward one day will be bliss.

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