INVEST Your Way to FINANCIAL FREEDOM

A SIMPLE GUIDE TO EVERYTHING
YOU NEED TO KNOW

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CONTENTS

INTRODUCTION: ARE YOU READY TO CLIMB A MOUNTAIN?

We're not going to waste any time here. Let's cut straight to the chase: *most young people today are living under an illusion*.

This isn't a new phenomenon. Young people have always been susceptible to it and probably always will be. But, as we'll explain, it's an illusion that will have far more serious consequences for people in their 20s and early 30s today than it had for their parents or grandparents.

What, then, is the illusion we're referring to?

It's the illusion that money doesn't matter; that it's something only older people need to worry about; that things are bound to work out in the end; and that life's too short not to spend money in the here and now on whatever it is you want.

Don't get us wrong. Both of your authors may be long past the first flush of youth, but we've been there too. Youth should be embraced. It's one of the luxuries of being young that you can afford to dream, and to think about things other than work, money and responsibilities.

But dreams should be tempered with harsh reality. Money is important and it requires your focus *now*. Indeed, the earlier in life you focus on it, the less likely you are to worry about it in the years to come.

Marketing professor, author and blogger Scott Galloway sums it up like this:

> Successful people often unwittingly head-fake young people with the humblebrags of 'follow your passion' and 'don't think about money'. This is (mostly) bullshit. Achieving economic security requires hard work, talent, and a tremendous amount of focus on… money. Yes, some people's genius will be a tsunami that overwhelms a lack

of focus and discipline. Assume you are not that person.

This book is intended to encourage, inspire and empower you; not leave you feeling anxious. We're going to show you simple rules to set you on the path to financial freedom.

We define financial freedom as being able to live the life you want without having to work for money to someone else's timetable and without having to rely on luck, or others' generosity.

We're not going to pretend that any of this stuff is easy or that it doesn't require discipline and sacrifice. Young people today have a mountain to climb if they want to be as wealthy as their parents.

We'll start by explaining why.

THE BAD NEWS

In the great scheme of things, people born in Britain since the start of the 20th century have been, at least in a financial sense, extraordinarily fortunate. But some generations have been more fortunate than others.

Yes, there was the little matter of world wars, but assuming you survived those, the post-war years saw a steady improvement in living standards. Take Robin's family, for example. His grandparents enjoyed the comparative luxury of council housing, the new National Health Service and a fairly generous state pension. Those in the next generation – the so-called baby boomers – were even luckier, with most people owning their own home and foreign holidays becoming the norm.

Robin is from Generation X, which has arguably been the most fortunate of all. Not only did living standards keep on rising, but the state continued to provide a safety net, as well as free grants for school leavers to go to university.

Ben is one of the older members of Generation Y, often called millennials, and for that cohort, financial independence will be harder to achieve. It will be harder still for Generation Z – those born from the mid-to-late 1990s onwards.

So, what happened? Why were the baby boomers so much more secure financially than many of those entering the world of work today are ever likely to be?

Less generous pensions

Perhaps the most important factor is that pension provision for older generations was rather more substantial than it is today. Most workplace pension schemes in the past were defined benefit (DB) schemes; in other words, you were guaranteed to be paid an agreed percentage of your final salary, or your average career salary, in retirement.

Nowadays, however, almost all pensions are defined contribution (DC) schemes; in other words, the employee and employer agree to contribute a certain amount to the scheme, but the value of the pension pot goes up and down depending on how the underlying investments perform.

In short, DC schemes are much less generous than DB schemes. It's true that, as things stand, everyone with a total of 30 qualifying years of National Insurance contributions or credits is also entitled to a basic State Pension. But the State Pension is only a relatively small amount – £179.60 per week in 2021 – and there's no guarantee that there will even be a State Pension in the future.

Asset price boom

Another reason why young people face an uphill struggle financially is precisely the same reason why older generations have had it so good. Simply put, asset prices have boomed.

Houses, in particular, are far less affordable for first-time buyers today than they were for previous generations. In the 2010s alone, UK property prices rose by more than 40%, while most global stock markets doubled in value. Why? Largely because of Quantitative Easing – a policy adopted by central banks in response to the global financial crisis of 2007–9, to keep interest rates low and fuel the economy.

This boom in asset prices naturally benefited those invested in the property and stock markets, but it made both of those markets much more expensive for new, younger investors to buy into.

Slowing salary growth

A final reason why young people today are at a financial disadvantage compared to their parents and grandparents is that salaries, in real terms, have fallen in recent years.

A survey published by the Institute of Fiscal Studies in October 2019 found that "those born in the 1980s have income that is no higher in their early 30s than did those born ten years before – and this is the first time since (at least) the Second World War that that has happened."

Since then, of course, we have witnessed a global pandemic. A report by the Resolution Foundation published in March 2021 warned that, as a result of the coronavirus, many young people are at risk of pay "scarring" in the years ahead.

Traditionally, people tend to move jobs more frequently early in their careers, boosting their pay as a result. But, researchers found that annual pay growth for those aged 18–24 fell from 12% in 2019 to 6% in 2020. Among those aged 25–34, it fell from 5% to 1%. This deterioration in pay, the report warned, comes on top of the fact that younger workers are more likely to have been affected by furloughing and job losses.

The combined effect of less generous pensions, missing out on the asset price boom and stagnating wage growth has had a huge impact. Consequently, young people will probably need to make bigger sacrifices than previous generations to become financially independent.

But enough of the bad news. There are still plenty of reasons to be cheerful.

THE GOOD NEWS

Inheriting wealth

This certainly won't apply to everyone, but a saving grace for many millennials will come in the form of an inheritance. According to a survey by Hargreaves Lansdown in May 2020, young and middle-aged people are more likely than over-55s to expect a generous bequest. Around 22% of those aged 18–34 and 23% of those aged 35–54 said they expect a "large" inheritance.

A report by the Institute of Fiscal Studies in July 2020 claimed that a quarter of people born in the 1980s are set to inherit £300,000 or more, with one in ten in line to receive at least £530,000.

Remember, though, that nothing in life can be taken for granted. Nobody knows what the future holds, and it may be that a large chunk of your inheritance ends up being spent on medical or nursing care for either one or both of your parents. Bear in mind as well that they may live for a very long time, so you might not receive your inheritance until you are retired.

Saving more, spending less

Another silver lining, alongside this increase in inheritance, is that, contrary to the stereotypical view that most young people are reckless spendthrifts, the truth is very different. A survey by the Foreign & Colonial Investment Trust found that 68% of people aged 18–35 had plans to save more in 2021 than they did in 2020, with strategies including eating out less and cutting unnecessary spending such as takeaway coffees. Six out of ten millennials also said they would rather miss out on social occasions than borrow money.

Good time to invest

But there's a third and final reason why the pensions time bomb that many are predicting to explode in the middle of this century may not be quite as severe as it could be. In a nutshell, there's arguably never been a better time to be an investor.

We're not talking here about market timing. We have no idea whether stock markets are about to rise or fall. Nor are we saying that, in the next few decades, market returns are going to be any higher than they have been in the past; indeed, there is actually evidence that suggests they may be lower.

No, what we mean is that, thanks to new technology, it has never been easier to keep on top of your personal finances. There's a wide range of online services that allow you to set up a globally diversified investment portfolio in minutes. You can also automate your savings and investments so that the money leaves your account without you even having to think about it.

More important still, the cost of investing has never been lower. The industry has come under enormous pressure to reduce fees and charges in recent years and that pressure is intensifying. Most investors are still paying too much, but if you're smart about it, you can keep your total ongoing costs down to less than half of one per cent. Over many decades of investing, that will save you a fortune.

In short, then, previous generations have enjoyed significant financial advantages that millennials don't. But, on the flip side, young people can now invest far more easily, cheaply and efficiently than their parents or grandparents could at their age. This book is going to show you how.

YOU CAN'T BE TOO SCEPTICAL

Please read this book with a beginner's mind. Try to put aside any preconceived ideas you might have about money and investing; be open to the possibility that some of your views and opinions might be wrong and need to be changed.

Humans are very social animals. We pay close attention to what others are doing. When someone we know appears to have made a killing, perhaps on a property deal or on Bitcoin, the temptation is to try to replicate their success. But, chances are, your friend or colleague isn't an investment genius, but simply got lucky and bought at just the right time. You might decide to copy them and invest your own money at just the *wrong* time.

Wherever you look – newspapers, investment magazines, financial websites or social media – there are plenty of seemingly expert opinions about how to invest. The arguments are often perfectly plausible. But always exercise caution when someone appears to have the answers. Ask yourself:

Why are these "experts" saying what they are saying?

Are they really as smart as they seem?

Are they genuinely trying to help me, or do they have a commercial agenda?

Is the advice they are giving genuinely good advice?

Is what they are saying supported by data and evidence?

LEARN FROM THE BEST

Gurus are best avoided. There is, however, one investment expert we suggest you do pay attention to.

Warren Buffett is widely recognised as the most successful, and highly respected, investor in the world. Over the years, Buffett has passed on a wealth of knowledge and insight to investors, both in interviews and, in particular, in his annual letter to shareholders of his company, Berkshire Hathaway.

This book, largely speaking, is based on what Buffett has urged investors (young investors in particular) to do. We're going to be giving you plenty of practical details as the book unfolds, but as you read through the chapters, try to keep in mind these six fundamental principles.

1. Develop good habits

What's true of dieting is also true of investing: when starting out, it's best to focus less on the end goal than on developing good habits. "The biggest mistake," says Buffett, "is not learning the habit of saving properly." In particular, "Do not save what is left after spending; instead spend what is left after saving."

2. Think long term

Never mind get-rich-quick; work on getting rich slowly, which is far more realistic. As Buffett once colourfully explained, "No matter how great the talent or efforts, some things just take time. You can't produce a baby in one month by getting nine women pregnant."

3. Ignore market forecasts

Hand in hand with Buffett's long-term outlook goes his disdain for stock market forecasts. Nobody knows where markets are heading in the short term. "The only value of stock forecasters," he once declared, "is to make fortune tellers look good."

4. Be humble

Another important lesson that investors can learn from Warren Buffett is that they probably know less than they think they do. “What counts for most people in investing,” he says, “is not how much they know, but rather how realistically they define what they don’t know.”

5. Keep it simple

“There seems to be some perverse human characteristic,” says Buffett, “that likes to make easy things difficult.” Successful investing is far more simple than many investment professionals make it look. As Buffett once put it, “You only have to do a very few things right, so long as you don’t do too many things wrong.”

6. Stay calm

The final, and perhaps the most crucial, lesson Warren Buffett teaches investors is to stay calm when others around you are overly anxious or excited. Don’t be your own worst enemy. To use Buffett’s own words, “The most important quality for an investor is temperament, not intellect.”

YOU'RE ON YOUR OWN

To summarise, then, funding a comfortable standard of living for the rest of your life is a daunting challenge for those in their 20s and 30s. Don't kid yourself otherwise. That hefty inheritance you're banking on might never materialise; and let's face it, you're not going to win the jackpot on the lottery.

What choice do you have? People are living longer. Those in their 20s today can expect, on average, to live well into their 80s, and many will live beyond 100. Put off saving and investing now and you risk having to carry on working into your 70s. Worse still, imagine having to rely on the state, on charity or on friends and relatives to pay for your upkeep in your final years.

Ultimately, it's down to you. Providing for your future self is your responsibility and no one else's. But, if you focus on Buffett's six basic principles and take the steps we're going to recommend, financial freedom is perfectly achievable.

Let's get started.

CHAPTER 1. WHY YOU NEED TO SAVE

Brothers Dick and Mac McDonald opened up a drive-in restaurant in the 1940s modelled after a hot dog stand they frequented in San Bernardino, CA.

By the late 1940s they decided to reorganise the business to take advantage of some lessons learned and the changing dynamics in America. The McDonald brothers recognised the burgeoning middle class following World War Two was moving to the suburbs and feeling more rushed than ever because of their commutes and growing families. People wanted their food faster, so the brothers mechanised the food prep process by turning their kitchen into an assembly line and focusing exclusively on burgers, fries and shakes. This was the invention of fast food and a little restaurant you may have heard of called McDonald's.

Ray Kroc was a milkshake machine salesman who saw potential in the business model, eventually manoeuvring his way into a job as the restaurant's franchise agent in 1954 to expand their reach. The McDonald brothers were not in the empire building business, but Kroc was, so he eventually bought them out and helped turn McDonald's into one of the most well-known brands on the planet.

Many years later, Kroc was asked why he partnered with and then bought out the McDonald brothers when he could have simply copied the system they created. Part of it was the fact that it was by far the best operation Kroc had ever seen of the thousands of kitchens he'd frequented over the years as an appliance salesman. But it was also the name itself that mattered. McDonald's sounded right to him, while a chain named Kroc's didn't have the same appeal.

The connotations we place on certain words can change how people feel about them, just like McDonald's versus Kroc's. The Big Mac rolls off the tongue a little easier than the Big Kroc.

Saving money is like the Kroc's of personal finance.

So many experts invoke terms like ‘frugality’ and ‘delayed gratification’ when explaining the merits of saving. Frugal is just another word for cheap and no one wants to be labelled a cheapskate. And delaying gratification sounds awful when you can simply take your gratification now.

Saving needs to hire a new advertising firm.

Here’s how Don Draper might market the idea of saving money:

> It buys you time. Time is the most valuable resource on the planet and the only asset where there is no inequality. We all have a finite amount of time in any given day to work with. Saving money can give you more control over how you spend your time in the future. Time to spend doing what you love. Time with your family and friends. Time spent travelling to exciting destinations. Time not spent going to the office anymore.

Saving allows you to do what you want in the future without having to worry as much about the financial aspects of your decisions. Saving more now means replacing less of your current income when you finally become financially independent. A higher savings rate automatically means a lower spending rate. They go hand-in-hand. Saving is your front-row ticket to financial freedom.

Saving not only frees your time in the future but also gives you a buffer in the present. Saving money provides a margin of safety when life inevitably gets in the way of your best-laid plans. Life is stressful enough on its own, but adding financial problems can amplify the rough patches. The last thing you want to worry about when life throws you a curveball is money. Money issues amplify stressful situations.

The problem is most people don't dig deep enough when figuring out why they should save in the first place. Getting rich sounds like a reasonable answer, but living a rich life means different things to different people. A specific number doesn't make you rich. If you're constantly stressed out about money, it doesn't matter how much you have – you aren't rich if money still makes you worry.

Saving for life beyond work sounds impossible to some and too far off in the future for others. If you think about your savings in terms of buying units of time or freedom as opposed to units of money, it can help frame the decision into the proper context. Most people want to get rich but we would all be better off trying to not die poor, or better yet, defining what being rich means on our own terms.

Don’t worry if you haven’t got started yet. All it takes is some small wins to get the ball rolling.