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TURN \$1000 INTO \$10,000

You don't need a lot of money to explore different investment strategies but you do need to know what you're doing

IF YOU BEGAN WITH \$1000 LAST year and picked the best-performing share in the S&P/ASX200 in each month of 2009, you could have turned \$1000 into \$1 million by year's end. Yes, that's right, \$1 million (see Turning \$1000 into \$1 million on page 49). Of course the million dollars is with the benefit of hindsight. Does it mean our quest to turn \$1000 into a mere \$10,000 is child's play? If only!

Increasing your cash tenfold is no easy task – but it can be done. We show how you could make it in less than a year if you are prepared to follow a very high-risk strategy.

Of course, if you reduce the risks you lengthen the time it takes to reach your goal.

Our million-dollar example also shows how our current volatile markets can offer a world of opportunity to rev up your wealth, even though you may feel you really want to take cover. Start with a small sum, money that you can afford to risk without jeopardising your budget or your lifestyle, follow one of our strategies, and see what you can achieve.

By taking plenty of risks and harnessing the magic power of compounding, a skilful investor can turn their \$1000 into much more. Investments all carry some sort of risk, but

they should yield more than your savings in a cash account over the long term. Savings preserve your money and are your security blanket that keeps you from being poor.

Once you have adequate savings you can invest your spare money to build wealth, though you may have to put up with occasional losses.

There are all sorts of investment strategies that investors can use to grow \$1000 to \$10,000. It's important to start and not put off investing, because the sooner your money is invested, the quicker it will grow.

Which investment strategy you choose will depend on how much risk you are prepared to take and how investment savvy you are (see Sharemarket Basics, page 88). You can put your toe in the water and do it slowly. Or do something more radical and jump right in.

How long does it take? Money asked the experts to put forward their investment strategies for turning \$1000 into \$10,000.

Financial planner Stephen Smallcalder, from Beresfords Personal Wealth Management, Chris Weston and Ben Potter from IG Markets, and Eric Blewitt, general manager of margin lending at Leveraged Equities, outlined different strategies at five speeds – from

low risk and very slow to aggressive and high risk but potentially fast.

If you are risk averse and keep your \$1000 in "cash", your money will reach \$1050 after one year and take around 14½ years to double. At this rate, Smallcalder estimates it would take 48 years to reach \$10,000. Too long!

But if you take on more risk and invest in Australian shares managed funds, you can halve the time to 22 years.

"It's quite confronting for investors to realise that there's no quick way to double their money," says Smallcalder. He points out that those investors have no control over the growth of their investments. "All the growth estimates are based on historical returns and don't offer any guarantee for what will happen in the future," he says.

Investors need to look at their goals and time frame and select the most appropriate strategy for their investment. Smallcalder recommends investors ask themselves whether the investment meets their risk profile and is right for their stage of life.

If you want to turbocharge your investing, gearing is a tool that helps it go full throttle.

"Margin lending works very well if used effectively and it is managed properly," says



Turn \$1000 into \$10,000

Every investor should know that, since 1900, Australian shares have outperformed inflation by roughly 7.7%pa, according to economic researchers Elroy Dimson, Paul Marsh and Mike Staunton. How does that compare with other investments? It's a far better return. Here's a speed guide for moving from \$1000 to \$10,000.

Turbocharged: You need excellent skills in security picking and market timing for CFD investing as you are betting on the direction of the price of the security. When the market moves in your favour, you can make profits very quickly. In the case of the example in the discussion of CFDs, Biota (see page 46), it could take just nine months to reach \$10,000. With the CFD index example, it could take 16 months. But it is very risky and you need to apply some risk management brakes to your investment in case the market turns the wrong way, so you can limit your losses.

Aggressive and fast: Gearing revs up the speed of your investments. It is a powerful tool if the risks are managed well and you maintain a conservative gearing level, plus keep some assets at hand that can be liquidated to pay for a margin call. Leveraged Equities' example of taking out a loan of \$1700 and a gearing level of 63% (page 47) shows it takes 11½ years for a gross return of \$10,000, or 13½ years for a net return of \$10,000 after capital gains tax and loan repayments are deducted.

Normal speed: History has shown that Australian shares do reward investors over the long term with healthy growth and dividend income as well. Unless you want an income from your share investment, it's best to select a managed fund with a low turnover of stocks, so you don't lose too much in capital gains tax. Beresfords' Stephen Smallcalder (page 49) says a fund with a low turnover will take 25 years to reach \$10,000, which is seven years less than it would take a fund with high stock turnover (for investors paying 31.5% tax).

Patient and slow: Fixed interest is a bit quicker than cash but only by 12 years. It will take 34 years if you don't pay tax but by then the future value of your money will be worth only \$4319. At a 31.5% marginal tax rate, it takes 50 years and by then your \$10,000 has a future value of \$2909. Don't fall into the trap of believing your fixed interest investments are as safe as cash. For the extra 2%pa return, there is some risk if government debt increases massively or a company collapses.

Snail's pace: While keeping your investments in cash allows you to sleep at night, you risk losing the purchasing power of your capital over time. If you are paying no tax, expect your cash to take 48 years to reach \$10,000, but by then inflation has eaten into the future value of your money. It will be worth only \$3056. At the marginal rate of 31.5%, it will take 69 years and it will only be worth around \$1819.



“Investments **all carry some sort of risk** but they should yield more than a cash account over the long term”

Eric Blewitt, general manager of margin lending at Leveraged Equities. “Most people borrow to buy a house or car. If you want to borrow to buy something, there’s a sensible way to go about it.”

If you take your \$1000 and a loan of \$1700 (or 63% gearing) to invest in the Australian sharemarket, you could reach \$10,000 in 11½ years, according to Leveraged Equities.

Contracts for difference (CFDs) allow very high levels of gearing – in the case of blue-chip shares you can borrow 95% of the value of underlying asset.

Here are five strategies for building your wealth

TURBOCHARGED

If you don’t mind a roller-coaster ride and can sleep at night no matter where your money is invested, one of the quickest ways to turn \$1000 to \$10,000 is with contracts for difference. That is, if everything goes right.

CFDs are for the sophisticated investor –

you enter into a contract with the CFD issuer which involves you betting on the future price movement of a particular asset. CFDs allow you to take an exposure to a much bigger parcel of shares than would have been possible with the same amount of money because of the inbuilt gearing.

IG Markets, winner of *Money’s Best CFD Provider* award for 2010, provided an example of how someone could use CFDs to turn \$1000 to \$10,000 by taking a position on Biota shares. Biota is an anti-infective drug development company which is involved with drugs for influenza and hepatitis C. Using real CFD trades, IG Markets’ institutional dealer Chris Weston says that last year it would have been possible to turn \$1000 into \$10,000 in around nine months when Biota’s share price rose.

Last March Biota shares were trading at 54¢. Weston says if you used a 15% deposit you could buy 6166 shares at an initial margin of \$500. Weston suggests a stop loss on the shares at 46¢ to limit the loss to around \$500. The idea of the stop loss is in case there are

falls in the sharemarket and the trade goes against you.

“As the swine flu epidemic gathered pace, so did the share price,” explains Ben Potter, market analyst at IG Markets. “This series of higher highs and higher lows was not broken until mid-December 2009, when Biota broke down below \$2.50.”

At \$2.50 you would have netted a healthy profit of \$1.96 on each share. This means that the 6166 shares would provide a net profit of \$12,085. It would have taken nine months to make the money.

CFD index trading, that allows you to take a position in a basket of stocks such as those in the S&P/ASX200 Index, has become very popular in volatile markets because it provides diversification that a single share doesn’t.

If you believed that the sharemarket was going to fall and had sold short a contract in the Australian 200 cash index when the Australian market was at 6310 at the end of 2007, you could have made some serious gains.

You sell one contract for \$200 and you limit

NEED TO KNOW

Fees can put a brake on growth

In the rush to make big money, don’t forget to pay close attention to fees. Always ask about costs; shop around and compare different investments.

If you buy managed funds or have a separately managed account through a financial planner, you are most likely paying annual fees of around 3%. This is made up of 1% to the planner for advice, 1% for investment management fees and 1% for the administration platform.

A total of 3%pa over time can slice through your returns and slow down the accumulation of your wealth. Instead of taking 22 years to reach \$10,000, after paying 3%pa, it will take 32 years or 10 more years.

Understand that if your investment earns 10% a year over 10 years, a 3%pa fee is the same as paying out 30% of your profit.

You can buy managed funds or index funds directly, cutting out the financial planner and administration fees. The average

fees for wholesale Australian share funds are around 0.5% and 1.86% for retail funds. Index funds are typically around 0.7%; exchange-traded funds offer the lowest fees at around 0.28%.

With geared investment products, watch the interest rate on the money borrowed. It is around 2% above the benchmark, LIBOR, which is currently about 9%. You can claim the interest payments as a tax deduction, making them tax effective investments.

your losses with a stop loss at 100 points away at 6410. At a cost of \$5 for every index point movement, you could potentially lose \$500. “As negative sentiment gathered momentum, markets globally collapsed,” says Potter.

“It wasn’t until early 2009 that markets began to show signs of a reversal. When the index broke up through the 3817 level, the position was exited.”

The profit is 2493 points x \$5 for each point = \$12,465 net profit. It took 16 months to reach \$10,000-plus.

Watch out for: The Australian Securities and Investments Commission (ASIC) says CFDs are very risky. They suit experienced share traders who have day-traded shares, options, futures and short-term derivatives.

“It’s much riskier than a flutter on the horses or a night at the casino,” says ASIC. “Your losses are potentially unlimited and can far exceed the money you’ve wagered.

“You could wipe yourself out in a single day. For example, just a 0.5% or 1% change in the price can turn into a 10% or 20% loss. In today’s markets, daily price changes like this happen quite frequently.”

ASIC recommends that you use risk control that involves a fail-safe trading system set up to stop unacceptable losses.

Potter says that CFDs are a bit like fast cars that can be dangerous in the wrong hands. “But you can educate yourself about how CFDs work and the risks,” he says.

To cut down the risk and limit the losses on CFDs you can take a stop loss and specify the level at which you want your position closed should the market move against you. It acts like insurance and incurs an additional fee.

“In the bull markets the large majority of investors didn’t use stops,” says Weston of IG Markets. “Now people are trading with risk management and education. It’s important that you calculate how much you are prepared to lose and put that in.”

However it’s a fine line between being sav-

vy about risk and missing out on investment opportunities. “The biggest mistake is people taking a profit too early,” says Weston. “You can let your profits run if technically there is no reason to sell out.”

HOW IT WAS DONE: Bought 6166 shares in Biota at 54¢ in March 2009 and held them until they reached \$2.50 in December 2009, netting a healthy profit of a \$1.96. To control your potential losses put a stop loss on the trade at 46¢, risking \$500. Using leverage with a 15% deposit, 6166 Biota shares could be purchased so that the initial investment turns into \$12,085, after nine months.

AGGRESSIVE & FAST

Borrowing to invest in shares is still popular despite the large number of margin calls during the global financial crisis. In fact it grew by \$900 million in the December quarter of 2009 to reach \$19.2 billion.

Around 70% of the 217,000 margin loan accounts invest in Australian banks and well-known mining and industrial companies. Margin loans have an average loan size of around \$85,000, down from \$190,000 at the beginning of the bear market. The average loan to valuation ratio was around 50% on accounts.

“Minimising and managing your risk is the appropriate way to go,” says Blewitt of Leveraged Equities. He says investors have typically managed the risk on their margin accounts by diversifying their portfolios, increasing the number of direct shares to reduce the concentration.

Investors can keep their level of gearing to a sensible 50%, he says. The average level is 40%-45% across the margin lending market.

If you borrow the money to invest in shares you can speed up your wealth accumulation, as shown in this example from Leveraged Equities. It recommends you boost your \$1000 with borrowings of \$1700, providing a gear-

ing ratio of 63%. Based on return assumptions of 12% growth a year, including 4.5% worth of fully-franked dividends each year, and a 9% interest cost, an investor paying 31.5% marginal tax rate will reach \$10,000 in 11½ years.

But after they pay back the loan and capital gains tax it will take around 13½ years.

Leveraged Equities points out that this example does not allow for any topping up of the investment, which usually happens. To compare it with other investments *Money* requested no additional payments to the account.

In the example, the gearing drops from 63% to 16% as the value grows. Investors typically readjust their borrowing level every few years to keep a constant gearing level of around 50% to 75%.

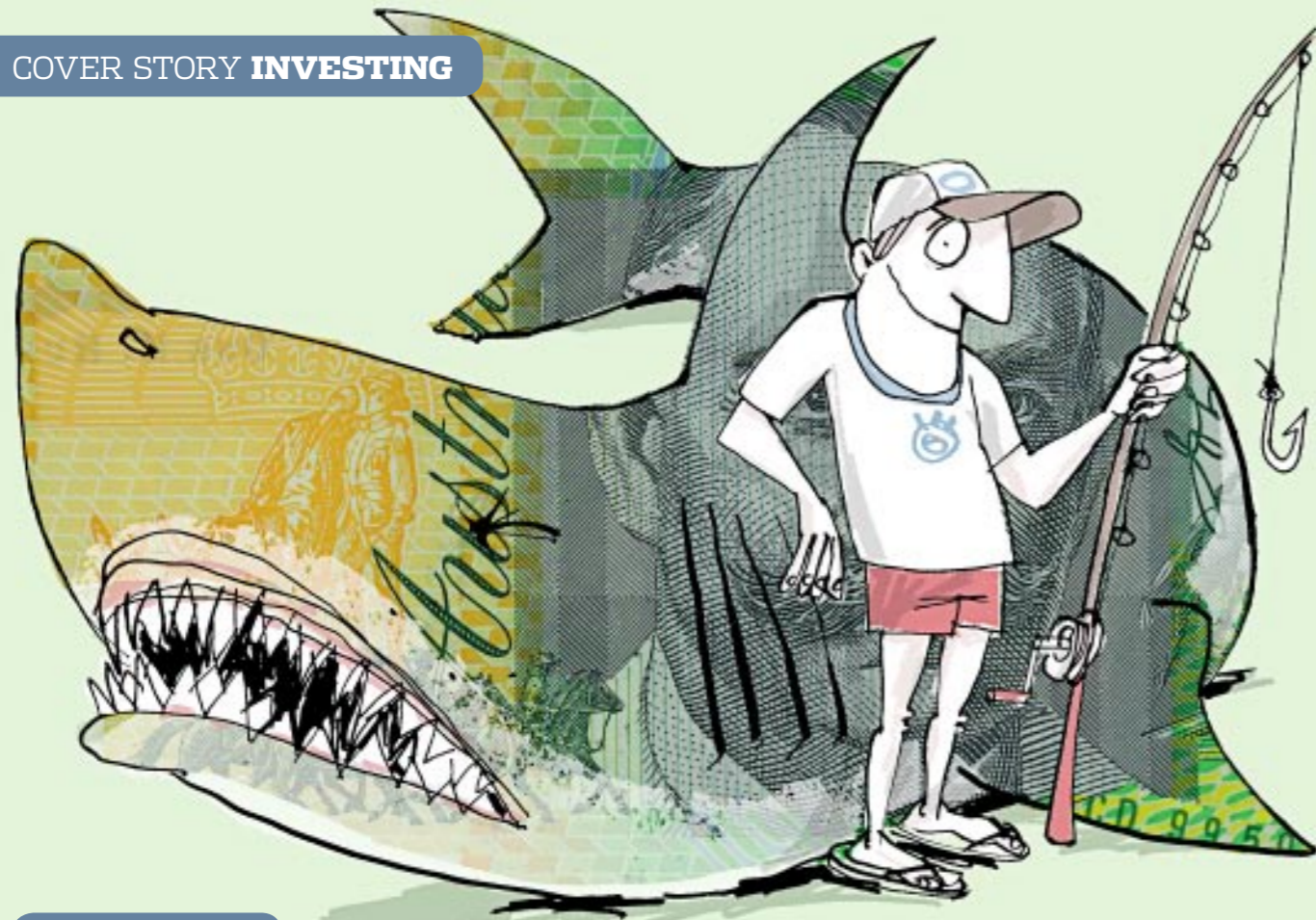
For the aggressive investor, there are margin lending products that offer gearing into alternative asset classes, or call options or short-selling products. As with sophisticated strategies, investors need to examine their liability when the unexpected happens, such as seesawing, volatile markets.

Short-selling accounts allow investors who believe that shares are going to fall to sell shares they don’t own, then buy them back at a cheaper price in the future. If the shares go up instead of down, the investor will lose money rather than make money.

Investors can also double gear by gearing into geared share funds, such as those available from Colonial First State, to magnify their gains.

Blewitt says that double gearing has a place in an investor’s margin lending portfolio and it could make up around 10% of your whole gearing portfolio.

Watch out for: Borrowing to invest through a margin loan introduces some additional risks. In volatile markets one risk is having to respond to a margin call. One way to lower risk is to adopt lower gearing, of



NEED TO KNOW

Look for tax-effective investing

How much tax you pay on your investments will impact on your wealth building. If you don't pay any tax, you'll accumulate wealth much more quickly. Those on the highest marginal tax rate of 46.5% will accumulate wealth more slowly than people paying tax rates of 31.5% or 15%.

There are few ways to sidestep paying tax that are legal. If you over 60 and drawing down an income from your superannuation fund – in the pension phase – you pay no tax. Some family trusts are structured so that they are not taxed, or only pay 15% tax.

Tax is one reason why investors accumulate their wealth through superannuation. Very few investments have tax advantages; superannuation is one of them. Both contributions to super and investment earnings of super are taxed at 15%, a lot less than most people's marginal tax rate.

What this means is that superannuation investments grow much more quickly than any investments outside of superannuation. However, in return for the tax benefits, you must leave your money until your preservation age, which is currently 55.

Stephen Smallcalder of Beresfords Personal Wealth Management says that if you are able to get the government co-contribution paid into your superannuation, you can boost your return and the \$1000 will grow to \$10,000 much more quickly.

If you don't hold your investments in superannuation, you will have to pay capital gains tax at personal tax rates on any investment earnings. "Capital gains tax blows out the time it takes to accumulate \$10,000," says Smallcalder. "If you are in the highest tax bracket, you lose half your profits in tax."

around 50%. It's always wise to make sure your current income after living expenses will meet interest costs and not to rely on dividends to meet the costs of a margin loan. Have some unencumbered liquid assets in case of a margin call.

You can request an early warning in the form of a buffer alert from your margin lender, to let you know when you are 10% off a margin call so you can get your money ready.

While gearing to a moderate level of leverage makes sense for many investors over the long term, anyone with a short-term horizon who uses margin lending is taking a highly speculative approach.

Gearing magnifies your gains and losses. You can minimise any potential losses by taking out a protected loan so that you never have to experience a margin call.

HOW IT WAS DONE: Bought into Colonial First State's Geared Share Fund in 1997 and sold out in 2007 – before the global financial crisis – and the \$1000 would have turned into \$10,000, according to Morningstar.

NORMAL SPEED

Direct shares require excellent stock-picking and market-timing skills. Take the example of gas explorer Karoon Gas. It would have been

a bonanza if you sold out at the right time. It peaked at \$11.45 in January 2010, before falling back to a low of \$4.51 in February 2010.

In October 2008 Karoon was as low as \$1.64. At the time of going to print the shares were approaching \$8. It rocketed over 600% over 15 months from October 2008 to \$11.45 in January 2010, and then plunged 60% over a month before moving up 60% over the next month.

If you were to bet everything on one share and change your bet monthly, you would need to average around 20% a month to accumulate \$10,000 from \$1000 over one year. Of course the odds of picking a 20% stock in any month

in 2009 were around one in 10, almost impossible. In less volatile years it is even harder to do. And to do that month after month is statistically close to impossible.

The minimum investment limit for buying direct shares makes it difficult to buy more than two shares with \$1000. Commsec has a minimum investment of \$500 a share. Instead, pool your money with other people to buy shares either through a managed fund or a separately managed account which gives you a diversified share portfolio.

Beresfords Personal Wealth Management has a separately managed account with 29 shares that has a low turnover of 20% a year which aims to minimise an investor's capital gains tax, says Smallcalder.

The returns from shares are hard to go past. Smallcalder has conservatively used a 7% growth estimate and 4% income from dividends. This places shares head and shoulders above cash and fixed interest.

Smallcalder estimates that if you invested \$1000 into shares, it would take 22 years to reach if you pay no tax, or 24 years if you have a 15% marginal rate, or 25 years if you are in the 31.5% tax bracket.

But watch out if your share exposure is invested in a managed fund that has high turnover. If the fund manager is buying and selling the shares regularly, you can be paying much higher capital gains tax on the income.

Smallcalder estimates the income from some fund managers can be as high as 11%pa year. This will slow down your wealth accumulation if you are in the higher tax brackets because you are paying tax on this income at your marginal tax rate.

It could take 32 years instead of 25 years to reach \$10,000 if you are paying 31.5% tax. "You can get to \$10,000 – if you minimise turnover – seven years faster," explains Smallcalder. It could be 41 years instead of 27 years if you are in the highest tax bracket of 46.5%.

Watch out for: Shares are volatile investments and best held for the long term.

HOW IT WAS DONE: Bought Karoon Gas shares at \$1 each in June 2006 and sold out in January 2010 when they were \$11.45. Your \$1000 reached \$11,450 in 3½ years, making a profit of \$10,450.

PATIENT & SLOW

There's been a rush to income investments such as fixed interest because people see them as "safe".

Fixed interest investments typically pay around 2%pa more than the cash rate, and the higher rate means it will compound the

\$1000 into \$10,000 faster than cash, according to Smallcalder's calculations – some 14 years faster. It will still take you 34 years if there's no tax on the gains, 50 years if you are taxed at 31.5% and 63 years if you pay the highest tax rate of 46.5%.

Watch out for: There is no certainty fixed interest investments will continue to pay 7%pa. The big risk with government or corporate bonds is that a rise in bond yields will cause a fall in the value of your investments. And you need to be wary of episodic shocks such as the crisis in Greece.

HOW IT WAS DONE: Invest \$1000 in a fixed interest fund returning 7%pa and in 34 years it will turn into \$10,000.

SNAIL'S PACE

During the global financial crisis, investors were keen to stay out of shares and keep their money safe in cash investments. This may be wise for the short term but you need to understand the cost of keeping it safe for a long stretch of time.

Putting your money in cash avoids one sort of risk (market risk) but watch out for inflation risk. This is where you risk losing the purchasing power of your capital.

While you preserve the purchasing power of the cash – which is important – your money doesn't really grow. After years and years, you are left with a meagre amount in real terms.

Smallcalder estimates it takes almost half a century to reach \$10,000 if you leave your money in cash earning 5%pa. If you pay no tax it will take 48 years. By then inflation will eat up the value of the \$10,000 so it's worth only \$3056.

It's even worse news for taxpayers. If you pay 31.5% tax it will take 69 years to turn \$1000 into \$10,000 and the real value of your money will be only \$1819. If you pay 46.5%, it will take 88 years and your money will be worth \$1138.

Watch out for: Cash is a great place to save but not to invest.

HOW IT WAS DONE: Keep \$1000 in a cash account earning 5% and in 48 years it will reach \$10,000. ☞

\$1000 TO \$1 MILLION

A dream strategy

If you started with \$1000 and each month in 2009 bought the best-performing share in the S&P/ASX200, you could have turned \$1000 into \$1 million in a year. This is how it worked:

In January you bought Babcock & Brown shares and sold when they soared 110%; in February you bought Emeco Holdings and sold when they jumped 76%. The process continued in March with Macquarie Communications Infrastructure Group, up a huge 176%; and in April with Pacific Brands, which rocketed by 186%.

At this stage your \$1000 was worth \$29,169. In May you bought Hastings Diversified and it jumped up 76%; in June it was Boart Longyear which went up 100%; in July Mincor Resources, up 42%; in August ING Industrial, up 87%; and in September Lynas Corporation, up 40%.

Your \$1000 is worth \$455,017 and this is invested in Southern Cross Media in October which goes up 20%.

In November it's Aquila Resources, up 52%; and in December Murchison Metals went up 47%, to reach a total of \$1,018,644 before fees and tax.

