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Wealth Planning

"Early to bed and early to rise until you get enough money to do otherwise" Peter's Almanac.

"What it means to be Poor ... One day a father of a very wealthy family took his son on a trip to the country with the firm purpose of showing his son how poor people can be. They spent a couple of days and nights on the farm of what would be considered a very poor family. On their return from their trip, the father asked his son "How was the trip?" "It was great Dad" the son replied. "Did you see how poor people can be?" the father asked. "Oh yeah" said the son. "So what did you learn from the trip?" asked the father. The son answered, "I saw that we have one dog and they have four. We have a pool that reaches to the middle of our garden and they have a creek that has no end. We have imported lanterns in our garden and they have the stars at night. Our patio reaches to the front yard and they have the whole horizon. We have a small piece of land to live on and they have fields that go beyond our sight. We have servants who serve us, but they serve others. We buy our food but they grow theirs. We have walls around our property to protect us, they are surrounded by friends." With this the boy's father was speechless. Then his son added, "Thanks dad for showing me how poor we are."" Unknown.

For those of you who haven't been following this series of articles, the focus is on planning. I have discussed estate planning, business operation planning and lifestyle planning. Following articles will discuss taxation planning, retirement planning and succession planning. In my first article where I discussed the need to plan holistically, I asked the question "where do you want to be in three, five, ten or twenty years time?" and "Is everything in place to make this happen?" An essential part of this is wealth planning.

As the above quote indicates everyone has a different perspective on what wealth is and what it's value is. How much wealth do you need? Everyone has a different answer to this from those who are possessed by accumulating as much wealth as possible to those who see it as a means to an end.

What is your definition of success? Our firm is a member of the Proactive Accountants Network. It's CEO and founder, Rob Nixon, defines success as "being able to do what you want, when you want, with whom you want in a manner that you want". Having enough wealth and particularly cash available for discretionary spending allows you to plan your business and life to be in a position to do this.

"There are three reasons we can't do that son. The first is we don't have the money and it doesn't matter a dam about the other two!" T Boone Pickens quotes his father in his book *The first Billion is the Hardest.*

Ask yourself this question. As at 30th June 2012 was my wealth greater than it was as at 30th June, 2011? Do you know the answer? If it decreased, why? Is this a trend? If it increased, are you happy with the amount it increased? If it increased by the same amount each year will that be enough to meet your goals. Your Balance Sheet or Statement of Assets and Liabilities or Statement of Financial Position should give you the answer to these questions. The one prepared by your accountant is generally prepared using historical figures and is not a true reflection of your net wealth at a given point in time. The one done for your bank is probably more accurate and more meaningful.

So, how do you accumulate wealth? Apart from winning lotto or receiving gifts or inheritances there are two ways. The first is to generate surpluses or savings. If each year there is a cash surplus from the operation after paying tax and living costs your wealth will be increasing. The second is as a result of what you do with these surpluses. If you invest the money into growth assets such as property and businesses (eg shares) then your wealth may grow with capital growth as well (it may also decrease, but hopefully if invested wisely over the long term it will grow). If the surpluses are used to reduce debt, your net wealth will have grown and your surpluses each year will be better from the interest savings. If you pour the surpluses back into your property you may increase it's value and may improve future cash flows as a result. Buying plant and equipment is not an investment. It is a prepaid expense and as such is not increasing your wealth. Such purchases would hopefully have a positive impact on cash flow in future years. Livestock producers may choose to have a lower surplus and allow their herd numbers to build up which may have a positive impact on increasing wealth.

Where do you want to see your wealth position or balance sheet in the future?

You need to consider what your target wealth is. When doing this try and focus on what wealth you would need to generate enough cash to allow you to do "what you want, when you want, with whom you want and in a manner you want".

What types of investments should you be accumulating?

Accumulating large primary production assets may be increasing your wealth, particularly if they have gone up in value considerably since you acquired them, but is there enough cash flow being generated from them? Your asset wealth may be large but are you always struggling to have enough cash to do what you would like to? Do you choose not to have a holiday because you cannot afford it when in fact you are worth millions? The issue is lack of discretionary cash. If the assets you accumulate do not generate income, then the only way to find cash to spend is by liquidating one of the assets (unless you want to borrow against the asset and run up some debt which is very dangerous).

When considering off farm investments there are many multitudes of investment products out there. However they all fit into three basic categories: cash, property or business. Cash includes term deposits, loans investment notes etc. Property includes residential property, commercial and industrial property, vacant land, farms etc. Business includes direct ownership in a business or indirect through holding shares in a company.

When choosing investments you need to consider the risks of each investment, the income or cash returns you should receive and the capital growth potential. One of the mistakes I often see from primary producers is that they choose low yielding assets. If they are borrowing to buy such assets they will most likely be adding cash flow stress on their farming operation. Getting good advice when choosing where to invest is essential.

Wealth is simply a means to an end. Planning your future is very important and this incorporates wealth planning. I am not advocating accumulating wealth for wealth's sake. It is all about balance. For those of you who like a game of chess consider the Italian Proverb: **"After the game, the king and the pawn go into the same box."**