Project how compound interest’s magic can make you richer

It’s easy to work out how the magic of compound interest can pay you future riches – you just need to know where to look.

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Everyone dreams of becoming wealthy, but too few have a road map to direct them there.

Without a map, you may be driving around in financial circles, wondering what’s around the next corner.

However, one powerful money trick can pay off handsomely: projecting your future financial destination with the magic of compound interest.

Whether it’s through online calculators, a financial planner or creating your own spreadsheet, financial projections provide clear targets and often show that you’ll be richer than you think if you stick to the road.

Tribeca Financial CEO Ryan Watson says four out of five people think visually, so a projected asset value “brings it to life”.

“People can then look to change their behaviour or change strategy,” he says.

Marinis Financial Group managing director Theo Marinis says many advisers and super funds do projections and it’s “best practice” to forecast the future.

“If you have an idea, you have a greater level of comfort,” he says.

COMPOUND INTEREST

Plugging your numbers into a free online compound interest calculator can be used to project the growth of any asset you own including shares, investment funds, real estate and cash in the bank. Moneysmart.gov.au has a good calculator and there are plenty of others on the internet.

Tribeca Financial CEO Ryan Watson says good planners share projections with their clients.

Remember to base the annual percentage rises on realistic historical data, and not the asset's latest moves – such as the recent property and stockmarket booms.

A calculator will show you that a $20,000 share portfolio growing at 7 per cent a year compounds to $40,100 after a decade and $80,800 after 20 years even if you make no extra deposits.

"People think investment is speculating, but investment is buy and hold," Marinis says.

"Even if markets come off in the next six to 12 months, projections show the long term, and smooth the peaks and troughs."

SUPER PROJECTIONS

There are many free superannuation calculators online, including several at MoneySmart and at the Association of Superannuation Funds of Australia's superguru.com.au website.

They allow you to enter current balances, investment options, wages, extra contributions and fees to get an idea of how much super you'll have at retirement.

Others show how much retirement income your future nest egg should produce, or how much your super balance should be today to deliver what you want.

Super funds often should show projected retirement balances online and in annual statements, or you can just phone them.

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Marinis says he has seen people who are clearly rich enough to retire comfortably “but they don’t realise they can retire”.

“They have no idea – there’s misconceptions of how much you need,” he says.

ADVISER ACTION

Watson says a good financial planner will share projections. He says his firm provides and regularly updates projections for clients’ retirement and for the next 10 years.

“If we see a couple in their 40s, 25 years is a long time away and there’s a significant life event every three years on average – births, deaths, marriages,” he says.

Projections can shift dramatically if your employment changes or investments plunge, but always focus on the long term.

SPREADSHEET SKILLS

Sometimes a simple spreadsheet is all you need to produce a good forecast.

“There’s a lot of people who are good at Excel,” Watson says.

And if it brings goals into sharper focus just like a professional online calculator or super fund figures, “it’s great, because that’s the same type of outcome”.

Meagan and Leon Jacobsen work with a financial planner. Picture: Tricia Watkinson

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COUPLE WITH A PLAN

Meagan Jacobsen and husband Leon work with an adviser and have a plan and projections that map out their short-term and long-term financial future and goals.

She says it is a “massive relief” to know that if they sick to their plan, they will retire comfortably and without stress.

“We are confident that our long term plan is going to be successful, so we don’t worry about short term changes in the market,” Jacobsen says.

“There are always going to be fluctuations – some harsher than others – but it’s important to remember the time span we are dealing with,” she says.

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