

Financial planning is all about planning for the future and making informed decisions. Recently we met with a young client who argued they couldn't afford to join KiwiSaver. After been shown how KiwiSaver worked, and hearing our story on the real cost of coffee, we both concluded he couldn't afford not to join KiwiSaver.

## COFFEE vs MORTGAGE

To illustrate, let us assume our model clients, Mr and Mrs Bean, purchased a home for \$450,000 and had \$150,000 towards the property from KiwiSaver and first home buyer grants, and other savings. They would therefore have a mortgage of \$300,000.00.

The very average terms of this mortgage are:

- Mortgage Sum           \$ 300,000
- Mortgage Term         25 years
- 5 Year fixed rate        5.35%
- Repayments             \$ 837 per fortnight ✓

Coffee?



Mr and Mrs Bean love their daily flat white coffee. Their local café sells a great cup for \$4.50. If they both purchased a flat white every day, they would have bought 14 coffees at a cost of \$63.00 per week.

As their financial adviser, we ask them "why don't you drink the coffee provided free in the staff room by your employer, and place the \$63.00 saved per week into your mortgage?". Of course, these astute clients followed our advice and increased their mortgage payments from \$837 per fortnight to \$963 per fortnight, reflecting the savings on coffee.

### So, what did they achieve by doing this?

- ✓ Mortgage term - reduced from 25 years to 19 years.
- ✓ Total interest - reduced from \$244,332 to \$180,537.
- ✓ Saving in interest over the 19 years - \$63,795.
- ✓ Weekly savings of \$63.93
- ✓ If we spread the savings over the 14 cups of coffee then the real cost of that flat white is not \$4.50, it is actually **\$9.00** per cup!

This illustrates the benefit of even small increases in mortgage payments, even in this extremely low interest rate environment. Imagine the savings if we used bought lunches, cigarettes, or couple of glasses of wine!

## COFFEE vs KIWISAVER

So, what does this have to do with KiwiSaver? Remember the young saver who claimed he couldn't afford to join KiwiSaver and we argued he couldn't afford not too? If that young saver was on the average wage of \$55,000.00 and had no mortgage, we have the following situation:

- Salary                       \$ 55,000 p.a.
- KiwiSaver Contributions   3.00%
- Employer Contributions   3.00% (*less tax*)
- Government Contributions \$10.00 / week
- Investment Return         5.00% p.a.
- Inflation – salary increase 2.00% p.a.
- Investment Term           25 years

The 3.00% contribution from our young saver is \$31.73 per week which is approximately the same cost of one flat white each day.

If our saver prudently decided not to buy a coffee, and instead placed the savings into starting a KiwiSaver account, after 25 years he would have accumulated \$168,953. His contributions to this would have been only \$52,152. The gain over and above his contributions by being in KiwiSaver is therefore an impressive \$116,801.

If we divide this by the 25 year term, and spread the cost across the 7 cups of flat white per week, the real cost of that coffee is not \$4.50, but **\$17.33 per cup!**

Now you know the real cost of that cup of coffee and can make an informed decision when the coffee cart arrives!