Chapter 1

The pathway to financial freedom

We wrote this book because we both believe that investing has the power to transform lives. We may start out and end up in different places, but no matter our age, income and savings, we can all begin our journey towards financial security and independence. This book provides a blueprint for success, however you define it.

'Whatever we do,' wrote American novelist James Salter, 'even whatever we do not do, prevents us from doing its opposite. Acts demolish their alternatives, that is the paradox.' Part of the allure of youth is the notion of limitless possibilities. The nostalgia for that time stems from the belief that once we could have become anything. This may not reflect how we felt at the time or the actual opportunities we had, so much as how our perception of our lives changes as time passes. The decisions we make as we age tend to reduce our future options. If you pursue one career, it closes off other professional opportunities. Choosing a partner means forsaking potential others. Acts demolish their alternatives.

Just as the process of ageing involves closing off options, investing can open them up. This book is designed to help you on your journey towards financial freedom. Each of us may define such freedom differently, yet one commonality is the notion that freedom is synonymous with choice.

Having an emergency fund means not going into debt when life's inevitable reverses occur. Debt is one important way that financial decisions limit choices. Saving and investing for retirement provide more opportunities to do what you want after you finish work. Investing allows you to retire early, pursue part-time work or switch careers. Investing isn't about getting rich; it's about incrementally improving your future by making choices today with that future in mind.

Gaining financial freedom is more than providing the things you want in life. It also gives you the freedom to escape situations you don't want to be in — to leave an unhealthy relationship or walk away from a toxic work environment.

According to the Australian Psychological Society, the number-one source of stress for Australians is money. Relationships Australia finds one of the leading causes of divorce is financial pressure. Investing is a means to an end, and that end can be whatever you want it to be. But ultimately it is about enabling a better life.

Can everyone transform their lives through investing?

We know that many people reading this book are already investors. Those readers don't need convincing, so for them this chapter is simply a reminder of all that can be accomplished.

We also know that our readers will include investing sceptics. We hear the reasons for this scepticism all the time: investing is too complicated; it's rigged in favour of professionals and the wealthy; it's too risky; it's not for them. Even for people who are already investors, this scepticism can creep into their decision making.

While we wholeheartedly disagree with this scepticism and believe investing is for everyone, we are also sympathetic to these arguments. It's not some baseless conspiracy theory. Given the way investing is presented, these feelings make a good deal of sense.

Shani says ...

I grew up in a household where investing wasn't discussed. When I looked at investors, I didn't see anyone I could relate to, anyone who looked like me. It isn't surprising I didn't think investing was for me. One of my first jobs was working in client services at a prominent fund manager. I answered questions about client portfolios and was constantly reviewing account histories. I started to notice the habits that led to success. I saw that making small investments consistently over a long period was the pathway to building wealth. And it occurred to me that there was nothing stopping me from doing the same thing and achieving the same outcomes.

A simple diagram (figure 1.1) shows you at one end of a continuum and your goals at the other. Everything in the middle we've called the *investment industrial complex*, with a nod to Eisenhower's famous warning about the military industrial complex.

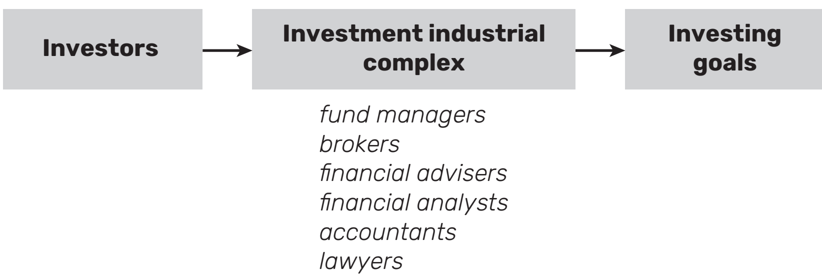

Figure 1.1: The investment industrial complex

The investment industrial complex includes all the people and companies that create investment products, give you advice on which investments to buy, help you access those investments and help you deal with aspects of investing such as taxes. Here we're talking about fund managers, brokers, financial advisers, financial analysts, accountants and lawyers.

We have spent our careers in the investment industrial complex. While there are bad actors in any industry, we don't think any of the professions in this industry are fundamentally evil. They are simply trying to make a living by charging fees to investors for their services. We will spend time stressing the importance of minimising these fees, because they all detract from your ability to achieve your goals. For now we want to focus on their motivations.

They all take a cut of the money you save and invest. It isn't surprising that people think investing is for the wealthy. Many of the fees are basis-point fees, which means they take a percentage of how much you invest, so it's natural that they would rather serve wealthy investors than those with less money. Some fees are based on trading activity, which means the more you trade the more money they make, so it's natural they want customers who trade more often.

Like any set of businesses, the investment industrial complex needs to justify the cut it takes. In this case, the justification matters more because the cuts are often large. University of Chicago professor Harold Pollack, who famously wrote that everything you need to know about money fits on an index card, estimated that financial advice fees globally are more than a staggering US$1 trillion a year.

The actions of this group contribute to why people think investing is too complex. To get people to hire them and to justify high fees, the investment industrial complex portrays investing as complex and requiring constant activity and a substantial time commitment.

If you fall for that, you are more likely to hire someone else to do it for you. Like many industries, investing is riddled with jargon that serves to separate insiders from outsiders, reinforcing the notion that to invest successfully you need professional assistance.

Throughout history, successful investors have been portrayed in certain ways. When Mark was growing up, it was perhaps best captured in Oliver Stone's movie *Wall Street*, which gives the impression that a successful investor is a god-like man (yes, they were all men) constantly taking audacious actions by yelling into six phones at once.

The fictional masters of the universe in the movie aren't too different from the way a star fund manager is portrayed in the marketing material — this omniscient genius who works all day and into the night to make all the right moves to beat the market.

The focus on the star fund manager was still around when Shani was growing up, but technology now plays a greater role. Data mining, statistical analysis and having three monitors filled with pulsing charts are sold to the public as the secret to investing success.

In both cases the underlying message is the same: you can't do this on your own. Successful investing is hard. Successful investing requires constant activity, and you don't have the time to do it well. Successful investing requires resources and skills you don't have. Once this message has been pounded into your head you discover that — conveniently — there are geniuses who know everything whom you can hire to help. People with access to fancy technology and complex data. People who know what the efficient frontier is and why your portfolio needs to be perched on it.

We think all of this marketing spin is just that — spin. People will hire someone to help, and we support that. Many readers bought this book to help them on their journey, and we certainly support that! But we believe that with some effort anyone can do this on their own, while paying fees only when absolutely necessary.

You don't need a fancy degree. You don't need to dedicate all your time to managing your investments. And you don't need a lot of money to get started. All you need to do is build some knowledge, come up with a plan designed around your personal circumstances, and apply patience and consistency. Those are the ingredients for using investing to create a better life. That is what we teach you in this book.

Mark says ...

Investing has always given me this sense of empowerment. I was in total control of my outcomes. And how many things in life can you truly say that about? It didn't matter what natural talents I was born with or where I went to university. My marks didn't matter or what job I managed to get. And as a natural introvert, it just appealed to me. Investing was this private endeavour in which my efforts and results weren't visible to the outside world. It was all on me. It was up to me to build knowledge. It was up to me to have the discipline to stick to my plan.

Why should you invest?

This is a simple question to answer. There's no practical way to achieve financial freedom without investing. You simply can't save your way to financial freedom. Making more money won't get you there. If you don't save and invest some of it, you will be forever dependent on others.

To illustrate this, we'll explore the *rule of 72*. It's a simple concept. Divide 72 by the annual return to calculate how many years it takes to double your investment. If you achieve a 7.2 per cent annual return an investment will double in 10 years. Too easy. But like everything in investing, some additional nuance helps.

Exercise: How many doubles to financial freedom?

Before getting into the rule of 72, here's a simple exercise for you to try. This is especially critical if you are sceptical about investing. Take a back-of-the-envelope guess at how many times you need to double your money to fund a comfortable retirement.

This will vary based on your age and it will be easier if you have a retirement goal. If you don't have a goal yet, we have you covered later in the book. What did you come up with? Keep this number in mind as you learn about how investing can help you achieve your goals.

Why not investing isn't an option

Every year the investment manager Vanguard releases a chart of 30-year returns for different asset classes. An asset class is simply a high-level categorisation of different types of investments. For instance, shares are one asset class and bonds are another. Using the rule of 72, table 1.1 (overleaf) shows how many years an investment in each asset class would take to double, based on the 2024 edition of Vanguard's chart.

This is a critical chart for anyone on the fence about investing. To have any chance of financial freedom, you need to shorten the time it takes to double your money, and the only way to do that is by investing.

Table 1.1: nominal asset class returns and duration to double your investment

Asset class	Nominal annual return over 30 years (%)	Years to double investment
US shares	11.10	6.48
Australian shares	9.10	7.91
International shares	8.20	8.78
Australian listed property	7.80	9.23
Australian bonds	5.60	12.85
Cash	4.20	17.14

Source: Adapted from the Vanguard 2024 Index Chart

If you are already an investor, this chart is still important. The investment industrial complex spends a lot of time talking about which individual shares, funds and exchange traded funds (ETFs) to buy. However, the asset classes you invest in matters far more than picking individual securities for your portfolio. A mix of asset classes in any portfolio will have the biggest impact on the outcome. More on this later.

According to a 2023 study at the University of Queensland, the average Australian works for a salary for 45 years. Assuming returns over the past 30 years are sustained in the future, an investor in US shares could double a portfolio 6.17 times during their working years. An investor who remained in cash would double their portfolio 2.33 times.

That is a huge difference. Imagine you start with $10 000 and earn the historic return on US shares. With no additional savings, you would retire with $673 848 after 40 years. If you earned the historic return on cash, you would have accrued just $51 848. The 'safety' of more conservative investments such as cash does not translate into safety when considering life outcomes. As we noted at the beginning of this section, there is no practical way to achieve financial freedom without investing.

Don't forget inflation

Since COVID, periods of high inflation have been felt more acutely than in the recent past. Yet even low levels of inflation can eat away at the spending power of your savings over time. Our first exploration of the rule of 72 did not include inflation. Almost all of the returns you see publicised by the investment industrial complex do not take inflation into account either. They are selling returns and don't want to highlight anything that detracts from that. In theoretical investment land, inflation doesn't matter. In real life it does, because the reason all of us save and invest is to grow our money so we can spend it later. The purchasing power of our assets matters.

Table 1.1 showed nominal or non-inflation-adjusted returns. The picture is different if we use real, inflation-adjusted returns. These returns represent how much purchasing power will increase for each asset class. We will talk about inflation a lot in this book. Financial freedom requires saving and investing money so you can spend it in the future, so it matters how much it is going to cost to buy what you want. Compare table 1.2 with table 1.1.

Table 1.2: real asset class returns and duration to double your investment

Asset class	Real annual return over 30 years (%)	Years to double investment
US shares	8.40	8.57
Australian shares	6.40	11.25
International shares	5.50	13.09
Australian listed property	5.10	14.11
Australian bonds	2.90	24.82
Cash	1.50	48

Source: Adapted from the Vanguard 2024 Index Chart

Inflation changes outcomes drastically and further reinforces the need to focus on the importance of investing to achieve your goals. When we adjust returns for inflation it becomes clear how critical it is to invest in growth assets like shares over the long term. Real returns for US shares are 24 per cent lower than the nominal return. Real returns for cash are 64 per cent lower than the nominal returns.

This is mathematically obvious since allowing for inflation takes away more of a lower nominal return than of a higher nominal return. Many investors struggle with conceptualising this arithmetic, which is why arguments against investing can seem sensible. Once you understand the maths, however, those arguments stop making sense.

It is important to point out that over the 30-year period Vanguard surveyed, inflation was low at only 2.70 per cent a year. Since COVID it has been much higher. In any type of inflationary environment, investing in growth assets like shares leads to much better outcomes.

How inflation impacts retirement savings

The impact of inflation is particularly pronounced over the long term. Saving for retirement is one of the longest, if not the longest, time horizon on a goal you will ever have. As an example, we can consider a 30-year-old with $100 000 saved for retirement. In our hypothetical example we can assume our retirement saver will leave the workforce at 65 after contributing $15 000 to their super each year and achieving an annual return of 8 per cent with annual inflation of 2.5 per cent. At 65 the account balance would be $4 063 286.

Sounds impressive. However, that fails to take account of inflation. Remember that what matters is not how much money you have but how much you can buy with that money. The purchasing power of that $4 063 286 portfolio is only $1 712 151 in today's dollars. Not so impressive.

Building wealth is the process of amassing financial assets or passive income to create independence. When we use the rule of 72 to explore how many years it takes to double the real spending power of a portfolio, it becomes painfully obvious that it is impossible to build wealth with defensive assets.

It would take more than their working life for most Australians to double real or inflation-adjusted wealth in cash. With Australian bonds an investor can't even reach two 'doubles' of wealth in a working lifetime.

Did your outcome change?

Has your estimate for the number of doubles needed for your money changed since you learned about the rule of 72? Do you still not know what you should aim for? Later we will outline the steps needed to estimate how much you need for a goal like retirement.

For now, we can use a generic example to come up with an estimate for the number of doubles of savings are needed over a career in order to retire comfortably. The rule of thumb is to have 25 times your spending needs saved for retirement.

Assuming you save 12 per cent of your pre-tax salary a year for 40 years and your salary keeps up with inflation, you will need roughly 5.2 doubles over your working life. Chances are you will need more. Many people don't work for 40 years without interruption. Many find their salary growth falling behind inflation. The larger point remains that investing in defensive assets like cash or bonds will not get you anywhere close to 5.2 doubles.

To reiterate our earlier point, defensive assets feel safe over the short term. They provide security. It feels like the right trade-off to make for people who fear the roller-coaster ride of the sharemarket. The logic behind this view is based on how the trade-off is framed. And this matters. A better way to frame the trade-off is whether you want the perception of security or actual security.

The rule of 72 is a good rule of thumb by which to frame these trade-offs. Saving money matters. But ultimately you will need to invest in growth assets if you are to achieve financial independence. Keep focused on the long term and the doubles you need to achieve your goals. Ignore the periods when the sharemarket doesn't do well and things feel scary. Keep your outlook broad.

Why Mark invests

Right before writing this book I returned from leave that included a stop in Bangkok at my favourite hotel in the world. And I found myself floating in the hotel's beautiful pool doing what I always seem to do there: thinking about investing. Investing, not investments. There is a difference.

I wasn't thinking about a share or an ETF. I was thinking about the process of sacrificing today for a better future. That's investing. It is simply delayed gratification. Skipping a dinner out here and there to go on an amazing trip in 10 years' time. That's only possible if you earn a return that meaningfully exceeds inflation.

Many people either treat investing as a chore or fear it so much they avoid it. They see investing as separate from day-to-day life. But investing is tied to life. Our portfolios represent our hopes and dreams for the future, whether it be security, the trip of a lifetime or a better life for those we love.

Being a successful investor is not about finding the best ETF. It is about integrating your investment strategy and approach with your life in a symbiotic relationship. It is in this context that the necessity of investing for living a better life becomes clear.

My love for this particular hotel in Bangkok can be partially chalked up to nostalgia. I have been staying there throughout my life, and some of the nostalgia comes from my own happy memories. But some of it comes from a time before I was born and what unfolded afterwards.

When my parents first moved to Bangkok in the early seventies, early in their marriage and at the beginning of my father's career, they had little experience outside of the United States. I can imagine how they must have felt. Everything lay ahead of them. Like any newly married couple they must have seen the future as full of promise, with no roadblocks in sight.

This view of a future path free of impediments results in many people failing to achieve their investment dreams. There is no substitute for time and no way to get it back as it slowly slips away—an adage that applies to investing just as much as it does to life.

Floating in the pool and rotating slightly to the left I turned my gaze from where my parents lived to the restaurant where I spent Christmas with my family when I was 21, and I recalled the heated argument with my father over my plan to move to New York after my university graduation. I insisted there was nowhere else worth living. He countered that the world offered too many options to make such a blanket statement. But I knew better, and my decision was final.

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As it happened, four months after that conversation I started dating my now wife Haley and followed her to Boston. I am writing this book in Sydney, and I've now lived in Australia for more than 10 years. I have never lived in New York as an adult.

Putting yourself in a strong financial position not only provides protection if things go wrong but enables you to take advantage of opportunities that arise. And, as my father tried to tell me all those years ago, life presents an array of opportunities, many of which most of us won't be able to pursue.

My mother recently moved into a retirement community. She has had a storied life since those heady days in Bangkok along the Chao Priya River.

My parents' marriage deteriorated into acrimony and eventually divorce. The life they imagined at the start of their Thai adventure unfolded in ways they couldn't have foreseen.

The residents wandering the halls of my mother's new home have far more memories than possibilities for the future. I would argue those memories are less likely to be of things they owned than of experiences with friends and family. Perhaps they lament the opportunities they failed to take.

They will have achieved various levels of career and financial success. Did they think of their net worth as a marker of success? At a certain point, financial assets provide diminishing levels of security. They become little more than a scoreboard in a game no-one can win.

That hotel in Bangkok opened in 1876. The hallways are lined with pictures of famous guests who passed through on their life journeys. Perhaps I was the first guest to contemplate investing while staying there, but I'm certain I wouldn't have been the first person to think about what I wanted from life and how to achieve it.

Why Shani invests

Throughout history, women have found a way to take back some semblance of financial security in the face of often vigorous societal opposition. Far too many women still face these challenges. The main reason I invest is simple: I know it is the only way I can gain independence and financial freedom.

Financial independence is not a goal that is restricted to one gender. But I want to start with what has made this goal particularly important to me.

I moved to Australia from Sri Lanka as a child. Gold played a similar role for women in Sri Lanka as in other parts of the subcontinent. I was given gold at birth, and gold jewellery at auspicious or significant dates in my life. When I got engaged in 2019 my mother gave me ancestral gold bangles.

The tradition of giving gold stretches back centuries. Bestowing gold is the equivalent of providing women with an emergency fund. If you're in a situation that you need to get out of, you have your gold jewellery. It is easily transported and hidden and can always be exchanged for money.

As we were writing this book, Mark sent me a *New York Times* article about Sri Lanka's new female prime minister. They interviewed a Sri Lankan woman about her hopes for her country's future. She earns $100 a month as a garment worker and describes the challenges of the rising cost of living. Half her salary is spent on baby formula for her daughter. 'We don't need the government providing us with food — we can somehow manage. What we need is a country where I have the space to make a little extra cash so I can invest in my daughter — maybe a pair of gold earrings for her first birthday.'

Mark can be forgiven for asking how gold earrings could possibly be an investment. It doesn't fit the traditional idea

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of an investment in Western culture. However, for this mother it would be an investment in her daughter's financial independence, ensuring she had something to barter in emergencies, or could avoid being controlled financially.

For many Aussie investors, financial independence has come to mean something quite different. The popularity of movements like FIRE (Financial Independence, Retire Early) has turned the term financial independence into a blanket statement which means you are not, and will not be, reliant on anyone or anything for financial support.

For many of us this may not be a realistic outcome prior to retirement. Yet financial independence is similar to the pursuit of 'success'. Shaped by our experiences and our circumstances, it is deeply personal to us.

Financial independence is an evolving concept. The achievement of each milestone sets another in front of us. Just as we continue to grow as people over our lives we can continue to grow financially.

In my case, I had relatively modest goals. After university, I wanted to cover rent and all my associated living costs. That was within reach for me, and it gave me a sense of personal and financial freedom. Increasing my own financial independence was and remains at the core of my financial goals.

Since then I have married and have achieved growth in my career. My evolving notion of financial independence now means being able to support myself independently regardless of any unforeseen circumstances. I have my own bank account and control of my pay cheques, and I have structured my finances in a way that means I can spend (or save) money in whatever manner suits me. This assures me that I can maintain my independence however my life and circumstances change.

None of us knows what the future will bring. I can foresee no circumstances in which I won't be happy in my relationship. Some people think that keeping funds separate to better navigate a relationship breakdown is crass. I see it as a safety net in case the worst happens. It gives me peace of mind now and it would provide relief if a difficult time were to eventuate.

I feel lucky to have had the opportunity to make these choices. Many are finding alternative ways to build a sense of financial security in the face of the constraints they have. The Sri Lankan mother we spoke about earlier wants to build a secure future for her daughter, within the constraints she faces.

It wasn't so long ago that Australian women faced obstacles to achieving financial independence. It wasn't until 1971 that Australian women were granted loans without a male guarantor.

On my own journey to financial independence my next step is to limit my reliance on my employer.

A common dream is to be able to retire early, to leave a job and not look back. I haven't reached that point yet. I have built my emergency fund to cover four months of expenses. I expect I would be able to find new employment within that timeframe.

I know my understanding of financial independence will continue to evolve. At some point I expect I will no longer rely on a pay cheque to cover my expenses.

Key takeaways

You can't save your way to financial freedom. Getting there will require you to invest in growth assets such as shares. Understanding this concept is foundational to success, as there will be times when it will be hard to keep going. Investing is very different from its portrayal by those who have a vested interest in promoting how hard it is. Your goal is not to replicate investing as it is portrayed but to figure out your own approach designed specifically to help you achieve your unique goals.

The biggest takeaway from this first chapter is the discovery that *you can do this*. Everyone can be a successful investor. This book is designed to iteratively describe the structure needed to build financial independence. As you continue to read, you will define and develop a unique financial goal to help you live the life you want. For now, going through the exercise of estimating how many times you need to double your money will reinforce the reality that investing is not optional for financial freedom. Keep this double estimate handy for when you are tempted to quit investing as volatility starts to scare you.