Money Goals SRL

Easy plan to get rich with stocks in the long run (24-30 Ott. 2023)

Introduction

What do you think it takes to get financially free with stocks? An incredible ability? Forecasting superpowers? What if I told you that you will be financially secure without studying hundreds of financial statements or betting your house? Would you be sceptic?

In this document, I am going to show you that you can really obtain financial freedom, with some minor adjustment to your spending, saving and investing! Let's go!

A simple 4 step plan

The plan to become financially free is really simple, so simple that the problem is just that it *is* too simple.

1) Find your current financial status (assets or debts, income and expenses) and your target asset amount
2) Pick a monthly investing number from your monthly net income.
3) Pick a low-cost all-world stock ETFs (i.e. VWCE or SWDA).
4) Start and repeat every month until you reach the target number to cover all your expenses.

Next, I'll provide some explanations about every step.

Step 1.1: find your current net income or net loss

The first thing to do is to gather all your *past* financial data:

- Your gross earnings, ideally separating different income sources
- Your total expenses, ideally separating different type of expenses (the more, the better)

The minimum should be at least 12 months of data collection, the best for data averaging is 3 years. But, if you recently sharply increased (or reduced) your monthly income or you do plan some new and recurring expense in the near future, you could consider a short-term projection of data using your new earning situation; this projection should not get over 6 months in the future.

Once you gather your data, you can calculate for every income and expense source the average monthly amount (total amount over number of months, for every category of income and expense). You should obtain a pretty accurate prospect of your monthly income statement. Now, the most important number is the monthly net income, calculated as the sum of your monthly income sources and the sum of your monthly expenses. Finally, you can multiply the monthly net income by 12 to obtain your annual net income.

For debts, is would be important to separate your principal repayments amount from the interest repayment amount, as only the second number should be subtracted from the gross income; the debt repayment is not a real loss for you, but it is a value you are removing from your assets and also from you debt, leaving your equity the same (see step 1.2).

Step 1.2: find your current "net worth"

The second thing to do is to gather all your *present* financial data, related to what you have:

- Your assets, or everything you have in your name and in your bank accounts, and all your investments.

- Your debts (liabilities), money you owe to other people, to banks or to the government.

You should state every asset or liability you have and its economic value.

For the assets, you should be conservative in the evaluation, meaning that if you count your car as an asset, you shouldn't use the purchase price as the current value. For liquid assets (back account, stocks) you should use face or conservative market value. To be conservative, I do not count the value of my short-lived assets, such as my car, my laptop or my bike.

For your debts, you should use the face value. Interest payments have been already considered in the previous part.

To find your current equity, you subtract your total liabilities from your total assets.

A little note on equity (or net-worth): due to the uncertain nature of this number, you should not focus on getting the number right. Oftentimes, it is just better to use a range between a bad guess value and a standard guess value for the assets you have to calculate your equity.

Step 1.3: evaluate your financial condition (not mandatory, but suggested)

At this point, you could also have fun calculating some useful numbers to evaluate your financial strength:

- Last year return on equity (ROE): this is the prime indicator of your going forward (or backward) in you journey to financial freedom. ROE is calculated by dividing your yearly net income figure divided by your current equity. If you have a net worth of 100€ and last year you gained a net income of 5'000€ (say you started working full time), you achieved a ROE of 5'000%! If instead your equity would be 1'000'000€, your ROE would be 0.5%. In such case, you should really not be working that job because your ROE would be too low and an index fund would yield a 2 to 6% yield, or 20'000€ to 60'000€ of net income. The concept I just mentioned is the reason why if you have little to no money, the best thing you could do is to find a job to make your ROE skyrocket.
- Last year free cashflow (FCF): I put this parameter as the second most important one for evaluating your financial strength after ROE. FCF is the amount of cash you have been able to generate in the last 12 months, considering only your cash transactions! Usually, the FCF is calculated by this procedure: take your net income, add your ingoing cash and remove your outgoing cash. Be careful to not double count income for FCF. For an individual, it is difficult to have the standard ingoing and outgoing of cash of a company beside income and expenses. One of the few values to be removed from net income as outgoing cash is debt principal repayment: in step 1.1 I suggested to not consider the debt principal repayment as an expense to calculate net income, but in this case, you should remove that amount from net income to get FCF. The more FCF, the better. If instead your FCF is negative for last year, really consider being careful in your cash management as a prolonged period of negative cashflow could mean your inability to repat your debts on schedule and, eventually, default.
- Current coverage (CC): for me this ratio is a clear indication of how your financial situation is sustainable for the next years. The CC ratio is calculated as the total debt repayments for the last year (or 12 months), considering not only principal repayments but also interest expenses, divided by your total gross income. This figure is kind of composed of two usual financial parameters: (i) your last-year total current debt, or the total debt principal you should have been repaying for the past 12 months and (ii) the total interest payments you made in the last 12 months. The CC shows you how much your debt is currently eating from your total gross income as a percentage of it. So, if last year you spent 300€ per month of principal repayment, 200€ per month of interest and you gained 1200€ gross per month, your CC would be 42%, meaning that for every gross 1.00€ you gain, 0.42€ go into your debt repayments.
- Last year net margin (NM): net margin is the percentage of net income you are generating for the total gross amount of income you received, or how much have you been able to convert your revenues in added value for your financial position. To calculate NM, you simply divide net income you kept for the total gross income you received in the same period of time. A slight variation of this parameter could be the free cashflow margin, obtained by dividing FCF for your gross income, to better capture how much cash you kept from your sources of revenue.

There are many more financial indicators you could use to evaluate your financial position: debt/equity ratio, expenses ratio (for every category of expense), income and expense breakdown, income growth rate, ecc..

I inserted 4 of my most important ratios for the individual, but you are free to evaluate your finances as you wish. The more the better, but do not overcomplicate things.

Step 1.4) Find your target asset amount

Step 2) Pick a monthly investing number from your monthly net income

Once you have clear indications of your net income figure, you can choose a magic number between 0 and your net income. The choice should not be random of course, but it should reflect (i) how much you can "afford" to pay yourself every month and (ii) how much you want to accelerate the path for your financial freedom. The number you are going to pick is the one you will have to invest every month for your long-term strategy to financial freedom, so it can be in a sense defined as the easiest, yet the most difficult choice you have to make in your life.

What is the amount of it you are comfortable investing for your strategy? Ideally, you would invest 100% of your net income to get there faster, but things are not so straightforward. The net income figure should have been calculated by already considering every expense you made in the last year so that the figure would be a pure increase in your net worth (if you were really on it, you could have removed one-time expenses from your calculations, but it would be a risky thing to do). But being conservative is the most important requirement, so you could consider using 50% to 80% of your calculated monthly net income as the base monthly contribution to your recurring investment, and adjust your investment figure when you understand the feeling of seeing less money in your bank account (but more money for you in the future) and you are more comfortable in investing your net income.

I currently invest 500€ per month, as that value is the maximum amount I can afford to invest (I also actively invest in stocks with my company and I plan to get more income from my real estate property, but those methods are far from a passive approach to financial freedom). My goal is clear: maximize current net income to maximize the growth of my absolute returns over time. I really hope that in the future I will be able to state that I invest 10'000€ per month for my future; that would be great news for me!

Step 3: Pick a low-cost all-world stock ETFs

If you do not know what an ETF is, I have good news for you: as of October 2023, www.google.com will give you all the information you need about ETFs. Maybe too much information, so be careful to filter out BS.

There are thousands of ETFs you could choose, but you need just the right one to succeed: an All-World stock accumulation ETF. Why? Well, because you are in the game for the long run, and in the long run stocks are your best bet to get good returns. You also do not want to be exposed to the risk of a country being in war or economically depressed, so you just buy *everything* at once. ETFs are easy to buy, have low costs and offer you exposure to all stock markets, based on market capitalization.

Do not be fooled: right now, "all-world" means 63% USA, 16% Europe, 6% Japan, 3% China (others: 12%), you are not getting much more of the diversification you would get by buying a SP500 ETF. And 35% of the current value of SP500 depends on the market value of the biggest 15 companies of the SP500 index.

On paper, this is not the absolute best strategy, but for the individual investor the simplicity, efficiency and effectiveness of using an all-world ETF strategy, makes it the most valuable one by far.

What are currently the best all-world accumulating ETFs you could pick from?

- VWCE (IE00BK5BQT80) – Vanguard – TER: 0.22%
- FWRA (IE000716YHJ7) – Invesco – TER: 0.15%

Those two ETFs are just two of the about 10 all-world ETFs right now on the market.

I currently invest in the VWCE 500€ per month.

On the accumulation ETF vs distribution ETF: simply put, accumulation ETFs are much more cost efficient, as the dividend reinvestment is automated inside the ETF and the investor does not receive taxable dividends. Moreover, you would need to make extra purchases in your brokerage account to keep compounding your returns, incurring in more fees. If you do not already have reached your target capital which would cover your expenses with yearly gains, you should select an accumulation ETF.

Step 4: Start and repeat every month until you reach the target number to cover all your expenses

This step is self-explanatory: you have to start to invest in the ETF you have chosen the amount you have determined. Do this, and you are ready to go! You do not have to do anything else, or better: you must not do anything else! Do not be distracted by short term opinion or (un)professional suggestions that could cause a lot of dagame to your future self.

This is not just an accumulation plan which does not yield anything, this is an investment accumulation plan and it will certainly vary in value, up and down from your total contributions value. But there are two key factors for your long-term success:

- Fiat value going down: your accumulation plan not only should keep the total value you invested, but it should also maintain purchase power of your money. By investing in the global ETF, you are becoming a partial owner of the biggest corporations of the world; they have power and pricing power! So when your fiat money value goes down, companies at least can maintain earnings power increasing their product price. As a owner of a company, you have much more power than as an individual (of course you will not choose company investments direction)
- Dividend reinvestment: Other than the companies increasing earnings over time, you can benefit from the reinvestment of dividend payments from the companies inside the ETF. Say you have a ETF valued at 100€, and the companies in that ETF pay for the next year 1€ in dividends. At the end of the year, the ETF now has a value of 101€ (assuming that market value of the companies has not changed over the 12 months, which is a pretty big assumption). You own more % of the biggest companies, and you have more % of earning rights!

Conclusion

This is a strategy so simple and so effective, that you will not believe how many “investors” will discard it because of its inactivity or slow approach to investing. Answer this question: “Why over 90% of active investors lose money during a time frame of over 5 years?”. The main problem is in the activity part, followed by the poor investment choices. With the passive ETF plan, you are neither active nor choosing your investments, you buy it all.

As always, this is a text for the me of the future, to:

- If I will be making much more money with other strategies, to brag about how I was wrong.
- If I will be making way less money with other strategies, to finger point myself and my bad choices.
- If I will follow this strategy (and I will), to see how thing are going

Let’s see you (which is me) in 5 years and we are going to evaluate how it is going.

Castelvetro di Modena (MO), Italy, 30 ott. 23.

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