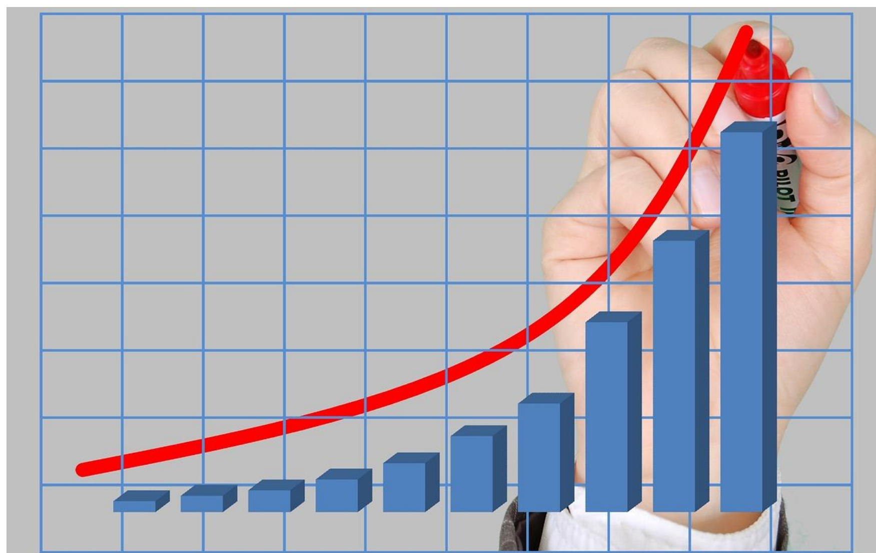
Strong Money Australia

Investing for Financial Independence

10 Principles for Lifetime Wealth and Passive Income



Hi, I'm Dave from Strong Money Australia. In this guide, I'll share the timeless lessons and investing principles you can use to invest for Financial Independence and create lifetime wealth and passive income.

The best part is, this stuff isn't complicated. When you're done, you'll be able to pass these lessons on to your friends and maybe even your kids to help get them started investing too.

To be clear, I'm not a finance professional and I wasn't born knowing any of this stuff. These are simply things I've learned (and continue to learn) over the years, from my own reading and personal experience.

It took me a while to realise the power in some of these principles. But they have really helped me on my own journey. So I'm happy to pay it forward and I truly hope they help you too.

Here are my top 10 principles to follow when investing for Financial Independence.

#1. Choose a simple investment strategy.

Investing is simple. Don't make it complex. Many smart and highly paid people spend time trying to convince us we need their expertise to invest well.

This simply isn't true. By understanding a few key concepts and following a set of sensible principles, we can take control of our finances and invest without the need for high-paid helpers. Because after all, nobody cares about your wealth more than you.

A simple investment strategy comes with multiple benefits, such as...

1. Less up-front research needed, so you can get started sooner.
2. Easier to follow, manage and stick with over time.
3. Less time required, which you can spend on more valuable things (hobbies, family, free time).
4. Less decisions to make or things to worry about.
5. Higher likelihood of long term success due to the above.

#2. Shares vs property.

Property and shares both have [their pros and cons.] And both are suitable for building long term wealth. But for achieving Financial Independence and passive income in a short space of time, I believe shares are the better option. Here's why...

More diversified. It should be pretty obvious that owning a few hundred or thousand companies is a lot more diversified than one house, in a particular suburb of one city.

With shares, your money is spread across a huge number of businesses in different industries. In contrast, a massive amount of money is tied up in each property you own, so there's a lot riding on the performance of that single asset.

Less hassle. Investing in shares is more passive than property. Even if you have a property manager, there always seems to be something going on (when you have multiple properties). Something needs fixed, tenants are moving out and so on.

These emails mount up and make owning property much less enjoyable. With shares, there is literally nothing to do. The companies take care of themselves, and the dividends land in your bank account. Much more in line with the FIRE lifestyle ;)

Less costs. When you purchase a property, the costs are huge. Stamp duty, conveyancing, and other charges add up to tens of thousands of dollars in many cases. And to sell, you'll be up for agent's fees and other closing costs, amounting to another five-figure sum!

To buy or sell shares using a low-cost online broker like Pearler or Selfwealth, it costs $9.50. With property, the ongoing costs are also painful.

In my experience, all the various costs tend to gobble up around 40% of the rental income (sometimes more). With shares, the cost of a diversified portfolio (managed for you) starts at about 0.10% per year in fees.

That's $100 per year for every $100,000 you have invested. Which is nothing!

Easier to get started. Property usually requires a minimum deposit of at least 5%, plus stamp duty and other costs. Realistically, that means around $50,000 for a $500,000 property. With shares, you can get started with $500! So, you can start compounding your money sooner and not stress about the big numbers involved.

No need for debt. With shares, there's no need to take on debt. Ever. You can build your portfolio with your savings and fully retire without taking on a huge pile of debt. It's just not feasible to buy property with cash, so a big mortgage is necessary. Yes, debt can amplify our returns, but we're also on the hook for that money. We continue paying that mortgage whether our property is tenanted or not, whether it's performing well or not. It also means less flexibility and room for problems with debt in the mix.

Better income and tax credits. Due to the costs I mentioned before, property in most parts of Australia is not very good at providing income. With rental yields around 3.5-4%, this is around 2% net after costs. Aussie shares, on the other hand, yield around 3-4%, plus we get franking credits, which further boost that by another 1-1.5%. So you're looking at 4-5%, with no costs. Around double the income!

You don't need leverage and growth to retire early. I took a long time to learn this. Wealth is built on saving, and to reach FI in 10 or 15 years, most of your progress will be driven by your savings rate, not your investment returns. I know it sounds strange (and maybe a little disappointing) but it's true. Check out this podcast for more.

More flexible. As I write this, part of our wealth is in property, and part is in shares. If I want a lump of cash (say $50,000) for any reason, where would I look to get it?

With property, I'd have to sell an entire property (worth much more than $50,000), go through a stressful experience, deal with the uncertainty of what price we'd get and pay considerable selling costs to get the cash.

With shares, I can take exactly what I need, at any time, and at minimal cost. The process is easy, cheap, and stress is minimised because I know exactly what price I would get if I sell today.

#3. Compound interest.

There's a reason Einstein called compound interest the Eighth Wonder of the World. Because it's truly incredible. I was floored when I first learned about compound interest. Here's an example.

Let's say $1,000 is invested for a child upon birth and they can receive it as a prize for reaching age 100. No money is ever added. Just this initial $1,000. What do you think this $1,000 would grow into? $5,000? $40,000? $90,000?

Try $1 million! Yep, with a return of 7.2% per year, this $1,000 would grow to $1,024,000. At this rate of return, money doubles every ten years. Like this...

Year 0: $1,000
Year 10: $2,000
Year 20: $4,000
Year 30: $8,000
Year 40: $16,000
Year 50: $32,000
Year 60: $64,000
Year 70: $128,000
Year 80: $256,000
Year 90: $512,000
Year 100: $1,024,000

Notice how half the wealth comes in the last ten years. And three quarters comes in the last 20 years. It looks like nothing is happening, then the value just explodes.

This principle still blows me away each time I come back to it! Compound interest is exponential and hard to wrap your head around. It seems too good to be true, but it's not.

What does this mean? You want to start investing as soon as possible. And you want to buy investments you can own forever, which grow by themselves.

#4. Fees matter.

Just like investment returns, fees compound over time too. So we want to make sure we're investing in shares in a way that is very conscious of fees.

While this principle is broadly accepted now, it was dismissed for a long time (usually by people offering high-fee managed funds).

But common sense has prevailed. With very few exceptions, investors will earn higher net returns in funds that have the lowest fees. The tricky part is, investment fees sound so small.

1%. It sounds like such a harmless amount. And we don't even see it since it's deducted from the value of our fund automatically. But think of it this way...

If you earn a return of 7% per year, then a 1% fee is actually 15% of your return being gobbled up in fees.

Put another way, if your fund is paying 4% per year in dividends, then ¼ of your dividends are being lost to fees. If you're not convinced yet, let's look at it in dollar terms.

Say you invested $100,000 at a 7% return before fees and left it alone for 30 years.
With a fund charging 1% p.a in fees, you'd be left with $564,000.
With a fund charging 0.2% p.a in fees, you end up with $716,000.

The higher cost fund actually leaves you with 20% less wealth after 30 years.

What does this mean? You want to pick low cost funds to invest in. Index funds are a solid choice.

#5. Invest consistently.

By far, the best thing you can do is to make investing a habit. Something you do every month. Simply adding to your portfolio on a regular basis will do the following...

1. Show and reinforce your commitment to your future wealth.
2. Create momentum as you regularly see your portfolio getting bigger.
3. Provide you with further motivation as it becomes a self-reinforcing loop.
4. Take your mind off the question *"when is the right time to invest?"*

Seeing your progress each month gives you something to look forward to. You'll love the fact that every time you invest, you now own more shares than before. And that means your future dividends are now larger too.

By far the worst thing you can do is try to time the market. And by that I mean try to figure out when the 'best' time to invest is. I know many people who have done this.

Not only is it impossibly hard to do (with a lot of luck involved), these people tie themselves in knots and obsess over it, so it consumes more of their energy and thoughts than they expected. It's emotional torture. Don't do it to yourself.

Market-timing sounds great in theory. I wrote an article about the perils of market-timing here and the difficulty of making it work in practice.

If you think you might fall prey to this, consider automating your investing. Setup an automatic transfer from your bank into your brokerage account for the same time every month (or whenever suits you), and then log on and buy those shares.

There is actually one Aussie broker (which I've been using for a while now) where you can completely automate your investing. It's called Pearler.

If you're curious, check out my interview with the founder of Pearler, where I ask him about the platform and how it works.

#6. Diversify.

Diversification sounds boring, I know. But it's an important and useful thing to do. In simple terms, diversifying means spreading your money across different investments. This way, if one investment does poorly, it doesn't hurt your wealth too badly, or ruin your hopes of Financial Independence. Here are 4 different ways we can diversify...

Companies and sectors. By owning a diversified index fund, you own shares in a large group of businesses in all sorts of industries. Healthcare, technology, finance, retail, real estate, and so on. Each sector has its ups and downs, so one sector may be struggling, while another one is thriving. You're not reliant on one industry doing well.

Countries and economies. You can diversify between countries too. So, by owning shares in a global fund, you benefit from the growth of international companies which are usually bigger and more dominant than companies here in Australia. You also benefit from the strengths of other economies and industries that are not well represented in Australia, like technology giants and dominant consumer brands.

Time. By purchasing shares on a monthly or quarterly basis, we're buying shares at different prices and in different market environments. This is called dollar-cost averaging, and it's fantastic because it helps our purchases to 'average' out. As the market rises, our money purchases less shares, and as it falls, our money stretches further and purchases more shares.

Assets. We can also benefit by having our money spread between different assets. Things like Aussie shares, global shares, listed property, private real estate we own, cash, bonds, peer-to-peer lending, and numerous other options. If we own multiple assets, some will be doing better than others. This gives us more opportunities to buy assets which are offering good value.

These factors combine to ensure we get a better long term outcome, by protecting against things that could work against us. Overall, this makes our investment portfolio stronger and our Financial Independence more certain.

#7. Be an Owner, not a Trader.

What we're really trying to do by owning shares, is piggy-back on the success of business over time. By owning our slice of the market, we get to benefit from the returns generated by companies for as long as we own those shares.

Innovation, human endeavour, technology, and the increasing prosperity of the world is reflected in the sharemarket over time. So while prices can move all over the place from week to week, we need to remember what's happening behind the scenes.

We own a slice of hundreds or even thousands of businesses. Every day, there are thousands of employees going to work at these places, working hard to solve problems, innovate, create new products, and serve their customers. Ultimately, all this effort eventually becomes higher earnings and bigger dividends for shareholders.

What the price of Coles or ANZ today means absolutely nothing. Did their business change this week? Or did people simply keep shopping at Coles and paying their mortgage. Likewise for US companies. People are still using their Apple iPhones and searching on Google. You own a slice of these profitable companies. In the long run the share price follows the success of the business. So don't worry about the price!

Alright, what about trading? What's wrong with that? Well, trading means you'll be buying and selling frequently. That comes with the following problems…

More decisions to make. More brokerage costs. More capital gains taxes. More admin at tax time. More time spent tending to and thinking about your portfolio. More stress. More chance of things going wrong, due to your active decisions. And less freedom because of all these things (mental and otherwise).

And after all that, nearly always, traders underperform a buy-and-hold investor. You also disrupt the magic of compounding (see principle #3). I'm not saying you can never adjust your investments (I have multiple times), but you should be very mindful and consider any taxes and tradeoffs before you do it.

#8. Expect a bumpy ride, but ignore the noise.

Look, there's no sugar-coating it - markets are volatile. You will often see the value of your portfolio fall, and it won't feel good. Not only that, but when the market is falling, there will be endless predictions of how much worse *it's going to get.*

This happened during the Corona Crash in 2020, every downturn before that, and every downturn that hasn't happened yet.

As humans, we crave certainty, so we ask the experts what the markets will do next. They have no idea, of course. But they're asked for their best guess, so they comply.

Despite all the uncertainty, those who keep buying all the way down, and all the way back up (as the market recovers) are the winners.

Not because they pick the outsmarted everyone else. Precisely the opposite. They deliberately avoided trying to be too clever, and simply kept investing. *That's* why they win.

Even during good times, you'll hear that "market set to fall", "good times about to end" and so on. Endlessly. My best advice is to expect it, and understand that over the long term, it's just noise.

Also, I should add that the volatility of the markets is precisely why shares deliver higher long term returns than other assets. This is known as the 'equity risk premium'.

By the way, if you're a saver, lower share prices are exactly what you want. That way you can buy large quantities of shares while prices are low (see dollar cost averaging and principle #5), and benefit handsomely when the market eventually recovers.

Markets will continue to rise over time, thanks to the efforts, ideas, and productivity of the human race. So ignore the headlines, keep investing, and hold on tight.

#9. Your money works for you, not the other way round.

One mistake I see people make is the amount of time they spend on their investments. As a long term owner, there's no need to constantly read about markets, check our broker account multiple times per day, or work harder to try and improve our returns.

More often than not, this works against us. The smarter we think we're being, the worse our results. A good example of this is when people think they're up to speed on all the news and feel like a crash is coming.

They stop their regular investment plan and wait for the fall. It never comes. They're left bitter and thinking the market is in a big bubble because it didn't play out like they expected.

There's simply no need to try and find investments that are going to the moon and give us gigantic returns. Are we really better at picking stocks than the people who do it for a living? Probably not.

It's important to consider not just your return, but your return on the time you've invested. By owning an index fund, we can achieve attractive long term returns with minimal time involved.

Even if you can beat the market (extremely unlikely), spending hours upon hours every week on your investments is really just like another job. Unless you truly find it meaningful and satisfying, time is better spent on other aspects of our lives.

Remember, your money works for you, not the other way round. But it doesn't work harder because you're watching it!

#10. Focus on what you can control.

This point is very important. The best way to approach investing, and life for that matter, is to focus on the things we can control.

Not only does that make the experience more enjoyable and less stressful, but it keeps us motivated.

That's especially true because markets can be unpredictable and volatile.

So, what can you control when you're investing for Financial Independence? Here's a few things...

1. How much you put aside for investing each month.
2. Making sure you follow through and invest on a regular basis (no second-guessing whether it's a 'good time to invest').
3. Which funds you choose to invest in (broadly diversified, low cost funds).
4. Reinvesting your dividends.
5. Choosing to ignore the noise and remain focused on increasing your ownership of income producing assets.

If you want your investments to grow faster, here's an important tip...

Your input (how much savings you add) is way more important than the output (your investment returns).

Earning big returns from investments comes long after the saving has been done.

The truth is, the bulk of your portfolio (and whether you reach FI) over 10 or 15 years will be determined by [how much you save.]

Bonus tip #11: Don't get distracted.

There are always shiny new things which come onto your radar as an investor. Especially when your goal is to build wealth quickly to retire early. Almost every option you see will sound great, promise high returns, look fun and interesting.

But almost every single shiny new investment will, all things considered, be complete garbage compared to a simple sharemarket index fund.

Don't get me wrong, I've invested in many different things over the years. Some of them great, some not so great. But underneath it all, one thing never changed...

The most reliable, repeatable, time-tested investment for building passive income and growing your wealth is shares.

That's because the bulk of our civilization, culture, and society is built by so many of these people and companies. So it's no surprise the sharemarket is at the centre of wealth created in our world.

People can make tons of money with all sorts of things in the short term (speculative stocks, buying crypto, using options, etc.). But over the long run, they will struggle to beat the market's return.

And the only guaranteed way to get the market's return is by buying and holding a simple low cost index fund.

Final thoughts...

These principles may be simple, but in my experience, that's a good thing.

We're investing to build wealth, so our approach should not chase excitement. It should be sensible, repeatable, proven, and yes, even boring!

To recap, here are the 10 investment principles:

1. Choose a simple investment strategy.
2. Shares are the simplest and easiest way to invest for FI.
3. Invest as soon as possible to get compound interest started.
4. Fees matter, so invest in low fee index funds.
5. Commit to investing on a set schedule.
6. Diversify to ensure a good long term outcome.
7. Be a long term owner, not a trader.
8. Expect volatility, handle it like a Stoic, and ignore the noise.
9. Money works for you, not the other way round.
10. Focus on what you can control.

And the bonus tip: Don't get distracted by the shiny new thing.

That's it! I really hope you've found this guide valuable, and I hope it helps you on your FI journey.

I wish you all the best with your investing!

-Dave

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