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HOW TO MAXIMISE TFSA CONTRIBUTIONS

By Leslie Greyling - Registered Financial Planner™, Brenthurst Wealth JHB

Many South Africans have difficulty finding a silver lining as the rand hits new lows and the cost of living keeps soaring. Staying committed to a financial plan can be challenging in these conditions, especially when a greater portion of monthly budgets are consumed by debt and interest payments.

One antidote to this – see if you can squeeze out extra gains from Treasury's generosity in the form of the Tax-Free Savings Account (TFSA) benefit.

If you're not aware, you're allowed to save a maximum of R36,000 a year in a TFSA product, up to a lifetime limit of R500,000. The big drawcard is that these contributions plus growth are exempt from any tax. That means you pay no tax on interest earned and on the capital gain.

CONSIDERING THE TAX YOU'LL SAVE; THIS TRANSLATES INTO A WORTHWHILE SAVINGS

DON'T FALL INTO THE 'SAVINGS' TRAP

Before moving onto the main thrust of this article, which looks at the difference between saving monthly vs annually, I quickly want to share the best way to maximise your TFSA contributions.

Even though the word 'savings' is in the name, the interest/growth offered by banks barely keeps pace with inflation. Because tax-free savings is a longer-term investment, you can select more aggressive investment portfolios, as the market fluctuations will be less severe over the long term.

The easiest way to maximise your TFSA is to choose a market-linked TFSA product. There are more investment fund choices available on most platforms.

The biggest long-term benefit you get from investing, is earning compounding interest, although you also want to make sure your returns are higher than the average inflation for that period. Savings accounts and money market accounts unfortunately don't offer such attractive rates.

So, you're doing the right thing by saving, but you're losing buying power every month because inflation is eating into the value of your savings.

ANNUAL DEPOSITS MAXIMISE YOUR RETURNS

The second way to benefit from this tax-free initiative is to use compound interest by making an annual deposit, rather than monthly deposits.

Interest is calculated daily, so if you can start earning interest on a full year's contributions from the first day of the year, then you have 364 days of compound interest in your favour.

Not everyone has the resources to invest R36,000 in one go, but as I'll demonstrate, you do benefit from adopting this approach.

We're assuming you make your annual deposit on the 1st of January and will continue doing so until you've reached your R500,000 lifetime contribution limit. This will take about 14 years.

If, over this 14-year time period, your investment has grown at an average of 10% per year, you will end up with R969,403 by making annual contributions, compared to R934,622 if you'd contributed monthly. That gives you a gain of just under R35,000, at no additional effort or risk.

The above illustration assumes no annual increase in contribution. At this stage the maximum allowable contribution is R36,000 per year and R500,000 in your lifetime, but this amount may be increased by SARS in the future.

INTEGRATE TFSA WITH YOUR INVESTMENT PLAN

A word of advice about TFSAs – apart from 'stay away from pure savings accounts' – is that it will be most beneficial if you incorporate it in your strategy, as part of your wider financial plan.

One prudent way to use the tax-free benefits is to open an account for your children, to give them a healthy kickstart in life. They enjoy the same benefits and are subject to the same contribution thresholds as you, so saving on their behalf is a great way to leave a legacy.

I'd suggest discussing this strategy with a financial advisor because you could benefit from their expert insight into the most appropriate TFSA instrument for your situation. Knowing what to expect from the future is especially difficult when you're looking at a timeframe of at least 15 years.

Dozens of tax-free options, which are open to individual investors, are available on various platforms. Popular providers to consider include Allan Gray, Sygnia and NinetyOne.

The ease of use and regular contributions – from R500 to R3,000 a month, or R36,000 a year, as explained – make TFSAs a worthwhile proposition, especially if these tax-free incentives encourage more South African families to save towards their futures.

ADVISOR PROFILE: LESLIE GREYLING - REGISTERED FINANCIAL PLANNER™

LESLIE joined Brenthurst Wealth Management in 2018 as a Risk and Investment Advisor.

Leslie obtained her National Certificate in Financial Services, Wealth Management, in 2014. She has 22 years' experience in the financial services industry, having served 15 of those years as an Independent Financial Advisor.

She is a REGISTERED FINANCIAL PLANNER™ and a member of the Financial Planning Institute of South Africa and is fully qualified to give advice on all aspects of investments, retirement planning and life cover, which includes personal and business assurance.

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"If you are living abroad permanently, and have an offshore bank account, you might consider dollar-based life cover that is available to South Africans from some insurers."

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