PRUDENTIAL
INVESTMENT MANAGERS

Prudential Investment Managers
Prudential Investment Managers

MARCH 2018

How to invest for your children's education

Every parent wants to give their children a world-class education, but this opportunity of a lifetime can require some serious financial planning. Read on to find out how to harness the power of time-based investing to make the dream of a quality education an easily attainable reality.

Take the break and go tax-free
Tax-free unit trusts are an excellent way of investing for education. Provided your contributions don't exceed the government's limit of R33,000 a year (up to a lifetime total of R500,000), the growth within the funds is free of all local tax on interest, dividends and capital gains. This means that you will have more savings to compound over time, leaving you with a larger investment sum when you need it.
You can make lump-sum or monthly contributions and, if you have a tax-free unit trust, you can access the funds in an emergency within two to three days if you really need to. Depending on your time horizon, you can choose from varying asset allocations with different risk profiles.

However, to maximise the benefits of tax-free investing, you should consider including growth assets like equities and listed property that deliver higher returns, and therefore generate more compound growth over time than cash or bond investments. Growth assets do come with more risk and volatility, and therefore require an investment horizon of five to seven years.

To make the most of tax-free investments you can open an account in each of your children's names and use your annual R100,000 donations tax-free allowance to contribute towards the investments. By the time your kids are ready to start their education, you will hopefully have accumulated enough tax-free savings to fund a large part of their expenses.   And, if there is any money left over, you will be able to switch your savings between different tax-free funds to ensure they are appropriately invested, based on your latest goals.

Get a slice of a balanced investment pie
Pooled investments like unit trusts offer easy access to diverse classes of local and offshore investments with varying asset allocations and risk profiles. Your choice of investment can depend on how many years you have until the school fees kick in, the anticipated total cost of the child's education and what level of risk you're willing to bear.

The earlier you start to invest, the more risk you can assume. If you're able to start from the moment your child is born, or at least five years, you could consider Prudential's Balanced Fund which has a broad asset allocation, helping to lower the risk involved. It includes a mix of local and offshore holdings spanning higher-risk equities (for higher capital growth over time), listed property, government and corporate bonds (for steady income) and cash. This blend across different assets makes it a medium-risk investment for time horizons of five years or more.
One of the advantages of this type of investment is that you're not bound by the same limits that apply to tax-free funds. You can invest as much as you want without any penalties and still withdraw funds whenever you like.

How much to invest?
This depends on what school you choose, how long you expect your children to be at university, and how early you start your educational investment plan. Use Prudential's goal calculator to help you to determine the amounts you should be investing every year. Do remember to be realistic about your selected growth

above inflation. With South Africa’s long-term inflation rate (CPI) at around 6.0%, and educational inflation at around 10%, your targeted growth should also be around 10% (or CPI + 4%), which is a reasonable expected annual return for balanced unit trusts over time.

Try to avoid debt

Change, as they say, is the only certainty. When investing for education, remember that your job circumstances and salary might change over time and that your children might decide they want to study something other than what you’d planned for. Faced with such challenges, some people rely on debt to pay for educational fees. However, try not to fall into this trap: In the same way that compound interest works in your favour when investing, the cost of interest on debt works very hard against you, especially if you’re borrowing over an extended period.

Prudential has an array of tax-free unit trusts, and local and offshore funds, geared towards short, medium and long-term horizons. We’re passionate abouthelping our clients provide for their children’s education. To find out more, speak to your financial adviser or contact us on 0860 105 775 or query@prudential.co.za.