



# THE ESSENTIALS OF FINANCIAL PLANNING & WEALTH MANAGEMENT FOR THE MUSLIM INVESTOR



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## About

*Patrick Mahdi O'Neill has over 20 years of experience, is an international Islamic Finance speaker, trainer and seasoned practitioner in the field. In his current role as Head of Islamic Wealth at Holborn Assets (UAE) he was responsible for creating an Islamic window incorporating holistic and market leading wealth management solutions. In 2009, he played a pivotal role in establishing Simply Shariah Ltd as a leader in the UK of Islamic pension and wealth advisory services. He has designed and delivered Islamic Finance training courses with a particular emphasis on promoting public welfare and achieving the objectives of sharia. His lectures and training subjects highlight the principles, benefits and ethics of an Islamic financial system. He is the Founder of the Islamic Financial Education Initiative – IFEI, which aims at making Islamic financial knowledge more accessible and to promote a just and equitable financial system for all. His articles have been published in various Islamic Finance magazines. Patrick Mahdi holds the CII Advanced Financial Planning Qualification, CISI Fundamentals of Islamic Banking & Finance and CISI Islamic Finance Qualification.*



## PRINCIPLES, VALUES & BELIEFS

In Islam, balance, moderation and performing actions with excellence and the right intentions are important principles. To be truly successful, it is vital to have the right attitude towards money, wealth and financial planning. The first realisation is that Allah is the owner of wealth "To Him belongs what is in the heavens and on earth, and all between them, and all beneath the soil." (S 20 v 5) We were created to worship Allah and this life is a just a test. We are only trustees of whatever wealth Allah has given us and will be accountable for it in the next life.

Secondly, our striving for wealth should not come at the expense of our religious duties and obligations. The pursuit of profit should not come at the expense of society, nor the detriment of the environment, or impose on the rights of others.

Over **90%** of a portfolio's return comes from asset allocation. ”

## GOALS AND FINANCIAL ORGANIZATION

The enjoyable and easy part of financial planning is thinking about your future goals. However to be effective you need to give them definition by quantifying the cost and timeframe for your financial goals to be achieved. It's also important to achieve a balance between your short and long term goals. Many people tend to neglect long term goals e.g. saving for retirement and focus on their more immediate needs and wants e.g. going on that nice holiday, saving for that car you always dreamed of etc.

The next crucial step is to get financially organised i.e. what financial resources do you have at your disposal to achieve your goals. You have to be your own accountant – list your assets and liabilities, income and expenditure. This should also include a cash flow projection for at least a year in advance.

**The second key aspect is to analyse your financial information and ask the relevant questions.**

**Example:**

- Are my assets working hard for me?
- Do I have enough emergency money?
- Do I have too much money sitting in cash?
- How much disposal income do I have?

The last question, should lead to an analysis of your

current expenditure. Many people find it difficult to save. The key question to ask, are my current lifestyle choices compromising my future goals? Are you spending more than necessary on rent, car loan, holidays, entertainment etc. You can liken it to a battle between your present and future self. In the present we like to spend money and enjoy life, whilst our future self would like you to work hard and save more. As ever, it's about getting the right balance. "Those who, when they spend, are not extravagant and not niggardly, but hold a just balance between those (extremes)" S 25 v 67 We live in a world dominated by interest based banking, financial transactions and products. Once you have gathered all your financial information it is also important to apply a Shari'ah audit. Are there any aspects of your finances i.e. bank accounts, investments, policies, home financing, debts which are not Shari'ah compliant?

**The benefits of being financially organized are twofold:**

- Firstly, so we can assess our financial resources and manage them efficiently and effectively to achieve success.
- Secondly, so we calculate our Zakat correctly and discharge this obligatory religious duty to the best of our ability.
- Thirdly, being financially organised and aware, allows you to take better control of your financial future.

## SOLUTIONS

The next key element is to assess the myriad of solutions available to achieve your goals. There will be lots of options with different costs, risks, pros and cons. One needs to carefully weigh one's choices to determine which is most suitable.

## RISK MANAGEMENT

Life is full of uncertainty and risks. A key part of any financial plan is contingency planning. You need to have sufficient emergency funds to cover for unexpected costs or change in circumstances e.g. losing your job. Other common risks such as a car accident, house fire and medical expenses can be covered by general Takaful policies.

The most devastating risk of course is if something serious happens to your health or you die prematurely. This can completely destroy your financial plans and financial security for your family. It is important to assess the impact this would have on your financial situation and family. Family takaful covering life, critical illness and loss of income are the ideal solutions to cover this risk. It is also vital to ensure that cover is in place to pay off outstanding debts. It is a very serious situation for a Muslim to die leaving unpaid debts behind them. "It is better for you to leave your inheritors wealthy than to leave them poor begging others." (Hadith related by Anas bin Malik Bukhari)

## HOME PURCHASE & PROPERTY INVESTMENT

Rent is a major drain on your financial resources and builds up nothing for the future. Eventually, owning your own place outright and no longer having to pay rent or mortgage repayments is a huge source of financial security. It is a flexible asset – if you no longer live there you can let it out. Depending on location, you could even consider holiday lettings where you can potentially increase your rental return by 50 to 100%. Remember; get your assets to work hard for you so you do not have to work so hard in the future.

Depending on which part of the world you live in, Islamic mortgages may be plentiful or non-existent. Where there are none available, one needs to think of more innovative ways of acquiring property assets whilst avoiding interest based mortgages. One such method is to take advantage of property lease purchase agreements. This is where the seller is willing to take instalment or deferred payments over a period of time. It's very similar to a Murabaha except ownership only passes on final payment.

When investing in property abroad, the investor needs to be conscious of future exchange rate risk i.e. the risk of the currency of your foreign property investment declining against your home currency. Over the long term this can have a huge positive or negative effect on your returns. Other factors to take into account are taxation i.e. property acquisition and annual taxes, income tax on rental income, capital gains tax and tax on death.

## REGULAR SAVINGS

This is closely tied in with your financial goals. Ideally, you should have 3 pots focusing on the short, medium and long term. Short term savings should cover your emergency fund and planned major expenditures within the next few years. Medium term is usually aimed towards university fees planning, creating capital to invest in property or even towards obtaining a golden visa. The focus of long term is securing a comfortable lifestyle in retirement. You should select the savings vehicle according to the savings timeframe. So for short term typically one would use Islamic bank savings accounts. The returns are very low, but the money is safe and easily accessible. For medium and long term one can consider equity linked savings plans. The potential returns are much higher, but one needs to pay careful attention to flexibility, costs, charges and early redemption penalties.

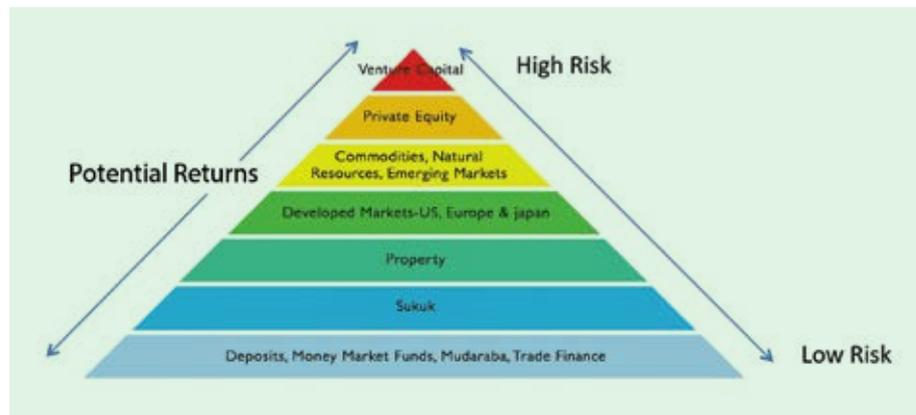
It is important to get a balance between all 3 areas. One should also, bear in mind the opportunity cost of

having substantial short term savings – because of a combination of very low returns, inflation and annual zakat deductions of 2.5% - both the real and nominal value of your short term savings will progressively decline.

## INVESTMENT PLANNING

What is your time horizon? What sort of flexibility and access do you need from your investment? Are you investing for capital growth or income or a balance between both? What is your attitude towards risk? An understanding of risk and your tolerance towards risk and volatility is absolutely crucial before considering any investment decisions. Unfortunately, many investors lose substantial amounts of money or end up very disappointed with returns by neglecting a careful consideration of risk. Your appetite for risk will dictate the type of investments which are suitable for you to consider. Consider the diagram below which shows the different types of assets, levels of risk and potential returns.

Another critical aspect of investment planning is



diversification. A well-diversified portfolio helps to mitigate risk. Getting the right balance between the different asset classes is essential. Different studies have shown that over 90% of a portfolio's return comes from asset allocation. Get the asset allocation right first and then choose the individual funds within the asset classes.

**In terms of choosing funds, there is excellent choice of funds across all the asset classes. According to Reuters, there are over 900 Shari'ah compliant funds. The key factors to look at when choosing funds are:**

- Where Domiciled, Regulatory Status and Investor Protection
- Size
- Currency Denomination
- Track Record
- Fund Manager and Charges (Initial, Annual and Exit).

There are now many ETF Islamic funds covering most asset classes which offer a cheap option for investing. There are also many well established fund managers which have good track records.