You REALLY Need to Do This!

Donald Cassidy, Founder and President
Retirement Investing Institute
www. R-I-I .org * 303-988-2296

It's time for Americans to get serious. About taking responsibility for our own retirement finances. No one (except maybe high-pressure investment sales people who have their own motivations) is going to take the initiative if you don't. Today is not too soon. It's a lot better than next year or five years from now.

Latest government figures say that Americans had a negative savings rate in both 2005 and 2006. That, simply out, means we spent more than we made. This is the first time that's happened since the Great Depression, when 20%+ of people were out of work. We have no such excuse today. Some economists will argue that the figures are too negative since they do not include the rising value of consumers' assets: their homes (oops!) and their securities investments (and we remember from 2000-2002 that those are not exactly fixed either). You KNOW if you are saving or not. Review your credit card balances vs. a year ago if you need help.

Benjamin Franklin, who published much wisdom on many subjects, counseled that we should put away 10% of our annual income for the future. If you are not doing so, it is time to get to that number just as rapidly as you can! And you now have the benefit of a wonderful device that had not been invented in ol' Ben's day: the workplace savings/investment plan. Yours may be called a 401(k), a 403(b), a 457, or a SARSEP. Whatever it is, get on board now; if you are already participating, raise your contribution percentage now, and every time you get a raise in the future. What's great about these plans is that they almost always involve an employer "match" – typically 50 cents or even $1.00 for every buck you put in, up to some published limit. That match money is a free bonus for doing the right thing. How can you pass up a 50% or 100% immediate return? Especially when your own contribution comes out of pre-tax dollars, so you will feel only about $2 in shorter take-home pay for every $3 you commit to your future in one of these plans!

A recent survey said that 70% of people are confident about their retirement finances even though half have less that $50,000 set aside. And 60% expect money from a "pension" even though only 40% work for employers who still have such dinosaur plans. Talk about living in financial dreamland! Wake up and get real, folks!

The big excuses against becoming investors (and studies show that about 30% of people who could be in their employer plans are not participating!) are that people do not want to lose any money, that they don't know how to invest smartly, and that they don't know where they could possibly find the money to put away every payday. Put down your third Starbucks grande of the day, please, while we take those in reverse order.

You will never have money for the future if you do not get onto a disciplined style of money handling now, literally spending less a day than you make. No one else will do this for you, so you need to start. The most dependable way is to “pay yourself first” since if you promise to save what’s left over at the end of each pay cycle, there will always be nothing left over. So the money needs to come out of your check before you even see it. Company plans as named above will do that for you, and you can also send a set amount to a bank or mutual fund account by automatic debit. Call up your favorite one and ask them to set it up for you.

The best way to approach getting spending and saving in proper alignment with income is to pretend in a very serious way that you are about to be laid off or take a pay cut. Such an unpleasant emergency would force you to get serious fast. So get serious now anyway. Many of us spend “little” amounts regularly in an unconscious way. The stop for a cup of coffee and maybe a muffin on the way to work (brew it at home; a thermos will pay for itself in about 3 days!). For those who prefer a canned soda to java, buy them when on sale at the supermarket (about $0.99 per six-pack) instead of feeding 75 cents each, or more, to the vending machine or the convenience store. It all adds up – in their pocket or in yours!

Those routine lunches out: depending on where in the country you work, even a modest lunch-out habit can cost from $5 to $15 a day. In 240 workdays, that comes to $1,200 to $3,600 a year in after-tax dollars. Brown-bag it! Make going out an occasional conscious decision, not a daily programmed habit. Split my two numbers halfway: if you can stop unconsciously shelling out $2,400 a year for lunches, that is $3,600 pretax that you can put into your 401(k) or similar plan, with reduced taxes making up the difference. And if you are not maxing out already, your employer’s match will make it worth even more.

OK, now the big one… cars. The automobile built this country’s economy a century ago. Our current addiction will destroy many a family’s financial future if you don’t change habits and fast. A fairly typical $27,000 new vehicle, once every three years, costs you $9,000 a year plus sales tax (let’s say about 6.5% for a rough average) of $1,750 each time, or another $583 a year. Control the urge by buying only every four years and the annual outlay drops from $9,583 to just $7,188, a savings of $2,395 or in popular parlance $200 a month in after-tax money. And my estimate is clearly low, since you will pay less in annual vehicle tax and insurance each year on a modestly older average vehicle. And I have not even touched on the car-loan interest you will save by having a lower average lifetime balance!

Space prohibits more ideas for saving, but uncontrolled cable and cellphone bills sure are easy next targets. Let’s now turn to the issue of not feeling expert enough to be an investor. There’s good news on four fronts. First, there IS NO perfect formula you need to discover and learn, so stop agonizing over every choice! Second, a fairly new breed of funds called target-date or lifecycle funds can literally make your choice a once-for-life event if you don’t want to learn and do dread the process of choosing and monitoring investments. These funds, available in many employer plans, have dates in their names.

Choose the date nearest when you want to retire. (Next problem?) Third. there are books in libraries from which you can learn the investing craft. That process of reading to learn may not be as much fun, and is more mentally taxing, than watching the nightly “talent” and (un)reality TV fare, but it will help you spend your later years in comfort long after those shows are forgotten. Our website, listed at the top of this article, features lists of investment books on several subjects. What you should NOT read are books that promise fast and easy wealth. It doesn’t work that way. The “hot” titles in 2000 were on Internet investing and two years ago on flipping real estate. The pattern will ever be thus, with only the details differing.

And fourth, there are non-book ways to learn about investing in situations where you will not be sold the product of the month (and will not be given a “free” lunch or dinner!). Two great organizations with nationwide presence are the American Association of Individual Investors (www . AAII . com) and Better Investing (www. Better-Investing .org). You can attend their teaching sessions and/or buy their software/books/tapes without needing to become a member, although membership provides discounts and a deeper experience. You can also do some learning on the R-I-I website named above. To the degree you learn to be a smart investor, you can save thousands in commissions because you will be able to choose your investments just as well as or better than the average salesperson! And you will not be buying their product of the month.

Finally, there’s that issue about not wanting to lose money. Markets go up and they go down. Over the long term, stocks return about 9%-10% a year on average. Bonds, maybe 6%. Those numbers are before taxes and inflation. Money funds, although lately offering yields well above 4%, usually give you 2% to 3% before inflation and taxes, or less than zero afterward. So you NEED to take risk in the financial markets. There has almost never been a 10-year period in which stocks were down. No such events in 20-year windows. The first key to getting over your fear of falling is to diversify your money so it all does not move in the same direction at the same time (bond and stock funds, domestic and international, and so on). The second key is to be sure you do not watch the market every day or week. The fluctuations will, I guarantee, make you get scared and sell out at the bottoms, and make you greedy and giddy and buy more at tops. If you can resist this harmful stimulation, that single habit will make you a lot more money than choosing between the better fund and an average fund.

One more perspective on losing money in the markets: take October 19, 1987 as a worst-case scenario. The Dow lost 23% in one day, by far the worst in a century. If you had put $8 into a mutual fund the day before, you’d still have $6 left (and even without reinvested dividends it would now be worth about 9 times that much). The $8 once spent on lunch (or whatever else) is gone forever, all $8 of it. Think about your financial future and get on the investing train! There are no absolute promises, except that if you do nothing you will be very short in the future. The average American spends more time planning a vacation or a car purchase than they do planning their future. You need to step above the crowd and do the opposite. Financial independence is a wonderful thing, and you CAN decide to have it! The younger you are, the greater will be your reward.