



The *Financial Principles Guidebook* is a comprehensive collection of our planners' insights to help you along your pursuit of financial independence.

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Do you remember your first investment? Perhaps you were in high school and opened an IRA, or bought a stock, with savings from your summer job. Perhaps it was enrolling in the 401(k) plan at your first job after graduating. Whatever the experience, there was probably a mix of emotions: fear, excitement, confusion, and even pride. We have prepared this Guidebook as a resource for young investors who may just be starting out and are likely experiencing that same mix of emotions. ***We hope that you find this information valuable. Should you have any questions, please do not hesitate to contact our office. If you have a friend, family member, colleague, or client who may benefit from this Guidebook, please do not hesitate to share it with them.***

FOCUSED ON YOUR FINANCIAL INDEPENDENCE

COMMON MISTAKES AND MISCONCEPTIONS OF THE YOUNG INVESTOR

Young investors often find themselves procrastinating from getting started on their saving and investing journey. That's because young investors are exposed to a number of misconceptions about investing that can lead to this procrastination, or lead to mistakes when they finally do set out on that journey.

INVESTING IS FOR THE RICH.....

Investors just starting out often think that they need a lot of money to make investments that will have a meaningful impact on their future. This could not be further from the truth. Using common investment products, you can obtain a diversified portfolio with an investment as small as \$50.

INVESTING IS COMPLICATED AND RISKY.....

All investing does involve risks, including the loss of principal. However, not all investments are created equal (nor are their risks). All investments need to be suitable with your risk tolerance and time horizon. To that end, investing can seem complicated, but the basics are quite simple—especially when you have a trusted guide. This is why we are happy to work with the friends and family of our existing clients to provide the advice that they need to get started on the right path for their financial future.

TIME IS ON MY SIDE, AND I AM GOING TO MAKE A LOT MORE MONEY TO SAVE LATER IN MY CAREER.....

Benjamin Franklin said, "Never leave that till tomorrow which you can do today." As with most things in life, saving and investing are better started **sooner, rather than later!** Let's take the example of a 25-year-old who saves \$250 per month. They can amass nearly half of a million dollars (assuming a hypothetical 6% annual rate of return) by age 65. However, if they waited until age 35 to start saving that same \$250 per month, they would only amass a quarter of a million dollars by age 65.

When considering that time is on your side, **don't focus on the short term.** It is easy to get caught up in the short-term movements of the market, both to the upside and downside—especially in today's fast paced and technologically advanced world. The young investor who is saving for their retirement and longer-term financial goals has a 30-year, 40-year, or even longer time horizon. Young investors should work with an advisor to create a financial plan and focus on long-term investment goals, rather than the short-term market movements.

MY INVESTMENTS GENERATE INCOME, THAT MEANS I CAN SPEND MORE!

Many investments do generate income which is often through the form of interest or a dividend. The concept of earning interest on the interest that is generated on an initial investment is called compound interest. While in the short-term that dividend payment may seem like a way to fund a purchase, allowing your returns to compound over the long-term can have strong effects on the value of your investments. For example, let's assume that you make a \$10,000 investment in ABC company stock which pays a 3% annual dividend and the stock price grows by an average 5% per year over a ten-year period. If you took your 3% annual dividend and did not reinvest the dividend, you could have \$16,289 after ten years. However, if you reinvested that annual dividend, you could potentially have \$21,589!

I AM YOUNG AND CAN TAKE RISKS, I AM GOING TO INVEST IN STARTUPS AND STRIKE IT RICH!

Generally, a young investor with time on their side will be able to take on a higher level of risk and volatility with their investments than an older investor who is closer to retirement. However, this does not mean that the same sound investment principles of diversification and maintaining an appropriate asset allocation don't apply. A young investor will often look for big returns and chase hot stocks, startups, new technologies, and even fad investments. We call this speculation, and it is a lot like gambling. Investors should focus on building and maintaining a diversified portfolio invested in a range of asset classes within their risk tolerance for the long term. Remember, your journey to retirement is a marathon, not a sprint.



SAVING FOR RETIREMENT AND FOR OTHER GOALS IS IMPORTANT, BUT HOW DOES ONE GET STARTED?

ACCORDING TO BANKRATE, ONLY 23% OF THOSE AGED 18 TO 37 FEEL THAT THE STOCK MARKET IS THE BEST PLACE TO PUT MONEY FOR A TEN-YEAR PERIOD, COMPARED WITH 33% OF GENERATION X AND 38% OF BABY BOOMERS.

In that same 2018 study, 41% of millennials admitted to having saved nothing for retirement. With millennials very unlikely to be the recipients of corporate and public pensions, which more than half of those over age 60 have received, this is a startling statistic. Below is an explanation of some of the different types of accounts available to young investors to save for retirement and some tips for getting on their way.

FIRST, ESTABLISH AN EMERGENCY FUND

Life is full of the unexpected. The loss of a job, an unexpected medical bill, or even a fender-bender, can have quite the financial impact on a young person. In conjunction with setting savings goals for your future, it is a good practice to try to accumulate at least three months of living expenses in a liquid savings account in case of an emergency. Odds are your bank will offer a very modest (or near 0%) interest rate for a savings account. However, an online savings account will generally offer a higher interest rate with a very low, or no, minimum required account balance.



YOUR EMPLOYER SPONSORED RETIREMENT PLAN

If your employer offers a retirement plan to you, it is a valuable benefit that offers you the ability to save for retirement, and even potentially gives you a tax benefit today for doing so. There are many different types of retirement plans offered by employers such as the 401(k), 457, 403(b), and Simple IRA. Some of the plans have different contribution limits, but all offer you the ability to contribute pre-tax dollars to fund your retirement. This means that your contributions will reduce your taxable income today (a tax benefit), while allowing the funds in the plan to grow tax-deferred until withdrawn in retirement (at which time the withdrawals are taxed as ordinary income). Some plans may offer you the ability to make contributions designated as Roth using after tax funds. You would not receive a tax benefit today for making Roth contributions, but the funds would grow tax-deferred and be able to potentially be withdrawn tax-free in retirement! For younger investors who are generally in lower tax brackets and have a long-time horizon, the Roth is a great long-term option that should be considered.

Many plans offer a matching contribution where the employer will match your contributions up to a certain limit. While you should contribute as much as your cash flow allows to your retirement plan, you should always contribute at least enough to receive your full matching contribution.

THE TRADITIONAL AND ROTH IRA

An IRA is a tax advantaged savings vehicle to help save for retirement. Young savers can contribute the lesser of 100% of earned income or \$6,000 per year to a Traditional or Roth IRA. You can contribute to an IRA even if you participate in, and maximized your contributions to, an employer-sponsored plan such as a 401(k).

Funds in an IRA can be invested and grow to help fund your expenses in retirement. A contribution to a Traditional IRA can be tax deductible today (subject to IRS limitations), and all taxes on earnings in the IRA are deferred until withdrawn in retirement. When withdrawals from a Traditional IRA are taken in retirement, the full amount of the withdrawal is taxable as ordinary income. A contribution to a Roth IRA is not tax deductible today, but the benefit of not taking that tax deduction today is that all earnings and growth are tax-free when withdrawn in retirement. For

young investors who generally are in lower tax brackets today and have longer time horizons to realize the tax benefits of the Roth IRA, we typically recommend the Roth IRA option.

Funds contributed to an IRA or Roth IRA are meant to be long term savings for retirement, all withdrawals prior to age 59 ½ may be subject to taxation and a 10% IRS penalty.

A “NON-RETIREMENT” BROKERAGE ACCOUNT

Because tax advantaged retirement accounts have contribution limits, diligent savers need another type of account that they can use to save. A brokerage account, like a retirement account, offers you a place to save and invest, but there is not a tax preference for using these types of accounts. This means that each year, you will receive a 1099 statement from the custodian and you will be required to report on your tax return (and pay taxes on) any interest, dividends, and capital gains realized in the account. Other than the payment of capital gains taxes on the sale of a security, there are generally no concerns with withdrawing money from a brokerage account. Therefore, a brokerage account can be used to help fund cash flow needs in the event an emergency, to save and invest for different near-term goals throughout your life, as well as to supplement your long-term retirement savings goals.

BALANCE YOUR SHORT AND LONG-TERM SAVINGS GOALS

While saving for retirement in your workplace plan and IRA are very important, so are your shorter-term savings goals. Perhaps you are saving for your first new car, or purchasing your first condo/home—you need to balance your long-term retirement savings needs and short-term goals.



Creating “buckets of money” is a great strategy for balancing your shorter- and longer-term savings goals. For example, let’s assume that you want to save \$15,000 into your emergency fund (an immediate goal), \$15,000 into your new car fund (something for some time next year), and \$50,000 into your condo down-payment fund (a three to five-year goal). If you open three different accounts or “buckets” for these goals, and we assume that you can save \$2,000 per month after your retirement plan contributions are made, perhaps you contribute \$1,000 per month to your emergency fund and \$500 per month to your other two buckets. When your emergency bucket is filled, you can then reallocate your savings each month until the other two buckets are met, at which time you can start allocating more money to your long-term savings goals.

“CASH IS KING” JUST NOT FOR THE LONG-TERM

That same Bankrate study mentioned earlier found that 30% of millennials believe that cash is their favored long-term investment vehicle. For the long-term, this is not a prudent investment philosophy as with interest rates at lows, after inflation, returns in cash are near 0%, and even potentially negative. If you are saving for a goal that is two to five years away, there are short-term investments that you may want to consider other than cash, and if you are saving for a goal that is more than five years away you should consider investing those funds. You should consult with a financial advisor to craft a savings and investment plan that caters to both your short and long-term savings goals.

CREATE A BUDGET, AND STICK TO IT!

According to a 2017 US Bank study, only 41% of Americans use a budget to track their monthly expenditures. Knowing this, perhaps you may not be surprised to learn that according to a 2018 NerdWallet study, 48% of

households carry credit card debt (with an average balance of \$6,961). When setting your savings and investing goals, it is helpful to have a financial plan and a budget to understand how your savings and investing goals impact your current standard of living. You can use our [Budgeting Guidebook](#) as a resource, and we hope that you find the below expense organizer helpful in analyzing your current living expenses so that you can set attainable savings and investing goals.

Expense Organizer

| | Monthly | Annually | | Monthly | Annually |
|--------------------------------------|---------|----------|--|---------|----------|
| Household | | | Medical and Healthcare | | |
| Mortgage/Rent | \$ | \$ | Health Insurance | \$ | \$ |
| Property Taxes | \$ | \$ | Life Insurance | \$ | \$ |
| Maintenance | \$ | \$ | Long Term Care Insurance | \$ | \$ |
| Home/Renter's Insurance | \$ | \$ | Disability Insurance | \$ | \$ |
| Electricity | \$ | \$ | Dental Expenses | \$ | \$ |
| Oil/Gas | \$ | \$ | Prescriptions | \$ | \$ |
| Water/Sewer | \$ | \$ | Out of Pocket Medical | \$ | \$ |
| Garbage | \$ | \$ | Other: | \$ | \$ |
| Cable, Phone, Internet | \$ | \$ | Family Care | | |
| Cell Phone | \$ | \$ | Parent/Child Care | \$ | \$ |
| Groceries | \$ | \$ | Education | \$ | \$ |
| Student Loans and other Debts | \$ | \$ | Clothing | \$ | \$ |
| Other: | \$ | \$ | Other: | \$ | \$ |
| Other: | \$ | \$ | Other: | \$ | \$ |
| Other: | \$ | \$ | Personal Care and Discretionary | | |
| Automobile and Transportation | | | Clothing | \$ | \$ |
| Car Lease/Payment | \$ | \$ | Beauty/Barber | \$ | \$ |
| Car Maintenance | \$ | \$ | Entertainment | \$ | \$ |
| Gasoline | \$ | \$ | Dining Out | \$ | \$ |
| Registration | \$ | \$ | Hobbies: | \$ | \$ |
| Insurance | \$ | \$ | Publications and Subscriptions | \$ | \$ |
| Tolls | \$ | \$ | Travelling and Vacations | \$ | \$ |
| Public Transportation | \$ | \$ | Charitable Contributions | \$ | \$ |
| | | | Gifts | \$ | \$ |
| | | | Gym Membership | \$ | \$ |
| | | | Other: | \$ | \$ |
| | | | Other: | \$ | \$ |
| | | | Other: | \$ | \$ |



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Call or email your advisor with a suggestion for a topic to be covered in The Guidebook. If we have covered it, we will send you that edition. If we haven't, we will cover it!



**HAVE A FRIEND, NEIGHBOR,
COWORKER, OR RELATIVE
WHO COULD BENEFIT FROM
THIS GUIDEBOOK?**

Feel free to forward our Guidebook to anyone you feel would benefit from this information. We would be happy to speak with them and answer any questions that they may have.



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<https://www.bankrate.com/retirement/millennials-retirement-savings-dilemma/>

<https://www.marketwatch.com/story/young-investors-this-is-the-most-important-investment-decision-youll-ever-make-2019-03-06>

<https://www.bankrate.com/personal-finance/millennials-stocks-risk-savings-accounts/>