Fundamentals of Money Management

Investment Savings and You!

Opinion - In my prior articles, you learned the importance of doing a Spending Personality Assessment, Getting your Financial House in Order, Cash and Money Management, Credit and Debt Management. “Investment Saving and You” start the next phase in Wealth Building: Learning to Save!

The magic question: How much should I be saving?

The answer is: It depends…

It depends on how much your salary will grow in the course of your working life.

It depends on the **rate of inflation** (inflation eats away at the value of your money) so you will need to save more than the rate of inflation.

It depends on your Return on Investments (ROI). If you can generate 8% or more (as a rule of thumb), you will accumulate more value in your investment portfolio.

Start the Savings Habit

Believe it or not, saving money can be habit forming and addictive as any drug. The key to developing a saving habit has three very important components:

1. Most importantly, do not give it away! We all want to help our family members or someone in need, but you must ask yourself this question: If you were in need, would those people aid you?
2. Learn to say NO and sack your money away for yourself. You will need it in your retirement years.
3. Do not broadcast to the world how much money you are saving. It only paints a target on you that says “I have money, come and get it”. Others will always ask for it.

How do you get into the savings habit? Pay Yourself 1st!

Rule of Thumb: Always pay yourself 10% first and live off 90% of your take home pay.

Here are two of the most widely used methods for saving:

1. Use an employer based Defined Contribution Plan (DC Plan - 401(k), 457, 503 account).
2. Open an Individual Retirement Account (IRA) or a Roth IRA.

In a DC Plan, a percentage of your pay is automatically deducted from your pay check.

If you are saving less than 10%, it is okay, but do a Spending Personality Assessment to find ways to get to 10%.

If you are at 10%, try to save more.

By saving and investing in pretax dollars, you lower your current taxable income.

401(k), 403(b), and most 457 plans

	2018	2019
Age 49 and under	$18,500	$19,000
Age 50 and older	Additional $6,000	Additional $6,000

Roth and Traditional IRA contribution limits

	2018	2019
Age 49 and under	Up to $5,500 (must have employment compensation)	Up to $6,000 (must have employment compensation)
Age 50 and older	Additional $1,000	Additional $1,000

Getting Started

The chart below is an example of the difference between saving 10% in post-tax dollars versus pre-tax dollars. By investing in a Defined Contribution Plan (pre-taxed), your take home pay will actually be more than if you invest after you get your pay check and then invest.

Saving Goal	$312	each month			
Salary	$3,120				
Tax Bracket	25%				
Saving After Taxation					
	Pre tax Saving	25% Tax	Adjusted Income	Savings After Tax	Take Home
$3,120	$0	$780	$3,120	$312	$2,028
Pre-Taxation Saving					
$3,120	$312	$702	$2,808	$0	$2,808
$3,120	$412	$677	$2,708	$0	$2,708

As shown above, the two methods benefit you as follows:

1. Pre-tax means you will have to pay taxes on the income you receive at time of withdrawal. Since it is assumed that you will be in a lower tax bracket, your tax will be less then what it is now.
2. If you go the post-tax route, you pay taxes up front which means less take home pay now. However, when you withdraw, there is no penalty or taxation (Hint: Roth IRA).

It is your choice on which option to choose, but the key is to do something. Now that you have started the saving habit, what are you going to invest in to make your investments grow?

That will be the beginning of the next series: Investments - stocks, bonds, mutual funds.

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