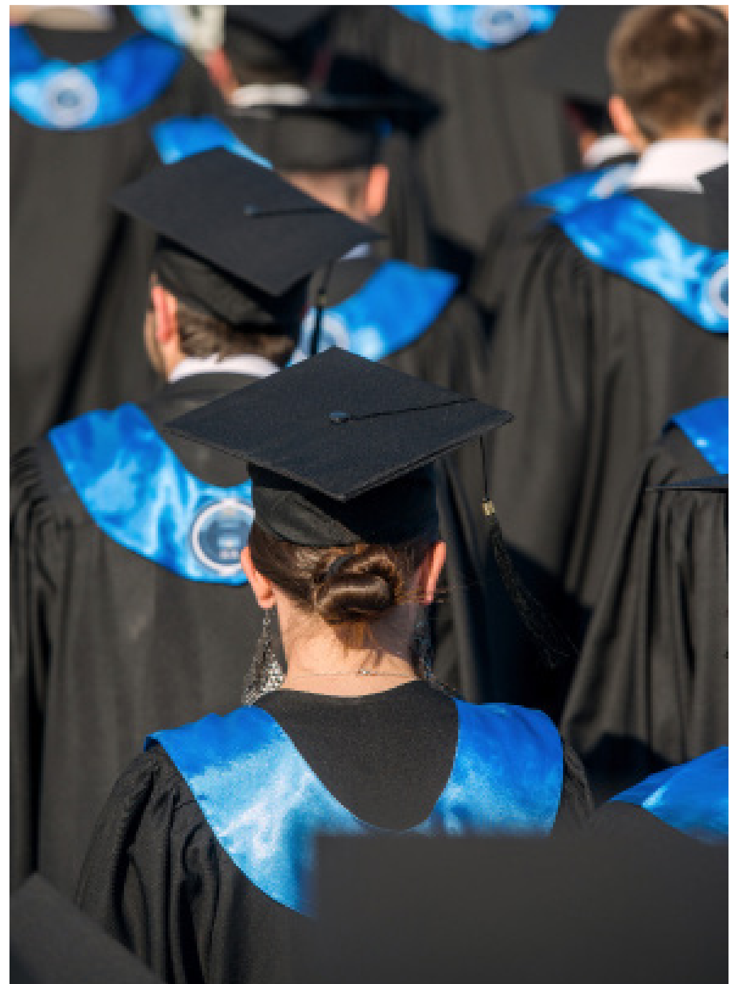
On Your Money for Millennials

by Kevin McKinley



Hello!

Many of the little decisions we make in our teens, twenties, and thirties can have a big impact on the rest of our lives. But we often are forced to make these choices with little knowledge and even less experience. By the time we learn what we should have done instead, it's often too late to make a difference.

I have been fortunate to work as a financial advisor for the last 28 years, and in the process of serving people who are for sure older, probably wiser, and likely wealthier than most young adults, I have learned what it takes to use the money you have to get the life that you want.

Hopefully these tips and suggestions will help you get your adult life off on the right foot, or make important changes to your habits while you're still young.

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Spend less, have more!®

Kevin McKinley

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How to Become Financially Independent

The most crucial number

You might think that your financial independence is determined by how much money you earn, how (and how much) you invest, and how long you work. Those factors are certainly important, and we will discuss those in a bit.

But the single most important factor determining when you will have enough money to retire, or be financially free, is how much you spend in a typical month.

The more money you spend, the less money you have to save. But the more money you spend, the more money you need to save to support your lifestyle and expenses.

As a general rule of thumb, you need to accumulate about 300 times your typical net monthly expenses to be financially-independent for the rest of your life.

That means if you spend, say, $5,000 per month, you need to have about $1.5 million accumulated to retire early and forever.

Don't get overwhelmed by that huge figure. First, you're very likely to have Social Security and/or pension payments by the time you reach your sixties, which will help cover your expenses, and greatly reduce what you need to save.

Second, you have a very long time to save to reach that number. And the sooner you start saving, the less you need set aside to accumulate to reach financial independence.

Just a few dollars a day

Let's say you would like reach a net worth of one million dollars by the time you turn 65 years old, and you're going to earn a hypothetical annual rate of return of 6% per year on your investments.

If you wait until you're 55 years old, you would need to save over $6,000 per month ($72,000 per year!) to reach a million dollars by the time you turn 65.

But if you start when you're 45 years old, then you "only" have to save about $2,200 per month. Begin at 35, and it's just about a thousand bucks each month. At 25, saving only $520 per month could make you a millionaire by the time you're 65.

And if you're lucky, smart, and disciplined enough to begin saving at the age of 15, setting aside just $288 per month will net you a million dollars by the time you reach 65.

Even if inflation averages 3% per year, a million dollars a few decades from now will still buy what several hundred thousand dollars will get you today. And it's more than most 55 to 64 year old Americans have accumulated right now, according to the General Accounting Office.

Tracking your progress

You should certainly save as much as you can as soon as you can, but it's helpful to know how you're doing well before you need the money in retirement.

As a rule of thumb, you should have at least the following multiples of your net monthly spending accumulated in savings at these age ranges (see chart to the right)

For example, if you're in your twenties and you're spending $3,000 in a typical month, you should hopefully have accumulated 10 times that amount ($30,000) before turning 30.

AGE	MULTIPLE OF MONTHLY EXPENSES
20s	10 times spending
30s	25 times spending
40s	50 times spending
50s	100 times spending
60s	200 times spending

Tracking your action

It's impossible to know how well you're doing if you don't know how much you're spending. So get in the habit of writing down where your money goes every day, week, and month.

If you know where it's going, you not only have a baseline figure to compare to your future spending, but you'll also have a good list of expenses that can be reduced or eliminated if you need to increase your savings.

A simple pen and notebook is the easiest way, or maybe write down each day's spending in a small calendar or datebook. If you're adept at using spreadsheets, use Excel or Google Docs to create and maintain your figures.

You can also use an online service like Mint (www.mint.com) or You Need a Budget (www.ynab.com).

Advice for Money and Life

While in high school

1. Work hard to keep your grades up—by the time you find out your grades are too low to get in to the school of your choice, it's usually too late to improve them.

2. Take advanced placement or other classes that can give you college credit. Check with your counselor to see what other programs will allow you to accumulate college credits while still in high school.

3. If you're working, contribute money to a Roth IRA. Ask your parents or grandparents for help in opening the account, and perhaps they may even contribute some money for you.

4. Participate in as many extracurricular activities and volunteer opportunities as you can. You will get valuable experiences, help others, and round out your college application.

5. Take standardized tests (like the ACT) early, and often. Attend prep courses, as a few points can make a big difference in the schools that accept you, and even affect your financial aid.

6. Drive slowly and safely. Not only will you protect yourself, your passengers, and others on the road, but traffic tickets and accidents can cause your insurance premiums to skyrocket, and will take years to return to affordable levels.

7. If you have an interest in a particular career, contact adults in your area who work in that field, and see if you can meet with them to learn more about what they do. In the future these individuals may provide a reference, an internship, or even your first full-time job.

8. Search for scholarships on sites like www.fastweb.com and www.myscholly.com.

Choosing your post-secondary school

1. Generally two-year schools are more affordable and offer a better cost-benefit proposition. Start there if you're unsure about your field of study and potential career.

2. Four-year public universities are usually more affordable and offer a better cost-benefit proposition than many more-expensive private colleges and out-of-state public universities.

3. That said, sometimes the more-expensive schools offer enough financial aid to make the net cost of attendance competitive, or even more attractive. You can search the "net cost calculator" for your situation at many schools by visiting tinyurl.com/netcostcalc.

4. Apply for financial aid after October 1st of your junior year in high school, and every year after. This is the first step to getting any kind of aid awarded by the institution.

Deciding how much to borrow

Hopefully you can get your degree(s) while borrowing as little as possible. But this rule of thumb can help you decide if you are taking on too much debt for a major at a particular school:

1. Check with the school to get the employment rate for graduates in your intended major.

2. Then find out what the median first-year earnings are for those graduates from that schools who find jobs in their intended fields.

3. Multiply the employment rate by the median earnings to get an estimate of how much money you should borrow to get that degree from that institution.

4. For instance, if you're thinking of becoming a nurse, and 90% of graduates with that major from your school get jobs after graduation, and earn a median annual salary of $40,000, you would multiply 90% by $40,000 to get $36,000—an acceptable amount to borrow.

5. Generally federal student loans are better than private student loans, and if you qualify, it's better to take the subsided student loans than the unsubsidized version.

While in college

1. The best way to lower the cost of higher education is to get out with a degree as quickly as possible.

2. Working during the school year can help cover expenses, but it may be better to spend more time taking more credits per semester, and borrow what you would have otherwise earned.

3. Try to take additional credits during winter and summer break.

4. Continue to cultivate relationships with employers in your intended field of study. Request meetings with them, email updates on your situation, and express interest in working for an employer like them after you graduate.

5. Stay out of credit card debt, and pay your bills on time. A negative credit score can haunt you for years, even after you graduate.

After college

1. Even though you're hopefully earning more money, try to continue living like a college student for at least a few more years. Share an apartment, minimize spending on a car, and eat at home instead of dining out. Trips, nicer clothes, and other non-essential expenses should only be made if you can pay cash for them, and you already have your other financial obligations covered.

2. When looking for employment, don't just focus on the salary. Consider the cost of living in the area, and compare it to what you could earn if you took a job in a less-expensive locale.

3. Be careful about refinancing public student loans into private ones. You may forego helpful repayment options by doing so.

Prioritizing saving, spending, and paying off debt

When you have an extra dollar and don't know what to do with it, use this list (in order) to decide if you should spend it, save it, or use it to pay off debt.

1. Make only the minimum payments required on your student loans, credit cards and other debt.
2. Set aside at least three months' worth of living expenses in a savings account.
3. Contribute enough to a retirement plan at work to get any matching contribution from your employer.
4. Pay down balances on any debt with an interest rate greater than 10%
5. Set aside at least six months' worth of living expenses in a savings account.
6. Raise your contributions to an at-work retirement plan to 10% of your gross earnings.
7. Save money for future discretionary expenses, like a trip.
8. Raise your contributions to an at-work retirement plan to 20% of your gross earnings.
9. Save money for future long-term purchases, like a down payment for a house.
10. If you plan to have children, start saving 5% of your gross earnings for future college expenses.
11. Maximize your pre-tax retirement plan savings
12. Pay extra on the balance of your student loans.

When you can't make your student loan payments

It's easy to fall behind in paying off your student loans, but ignoring the problem won't make it go away--it will only get worse. Here's how to take action to minimize the damage of missing a payment.

1. It's difficult to get federal student loans reduced or forgiven, and nearly impossible to do so with private loans. Filing for bankruptcy may not even eliminate or reduce your obligation.
2. However, you may qualify for deferment, forbearance, a lower interest rate, and/or a longer repayment period, which could help you stay current on your payments for the time being.
3. At the first sign of problems, visit the following sites for more information:
   a. If you are struggling to make payments on federal student loans, go to studentloans.gov and ibrinfo.org for information on income-based repayment plans.
   b. For help with private student loans, visit consumerfinance.gov/students/.

Keep a good credit score

Your credit score and report will not only affect if you can borrow money, but how favorable the terms will be. It may also affect your attempts to lease an apartment. A bad score could cost you more in insurance premiums, and could even hurt your ability to get a job.

It takes just a couple missteps to hurt your score, and could take several months or more to repair it. Here's how to keep it at an acceptable level:

1. Pay for any credit card charges in full each month.
2. If you can't pay the bill in full, at least make the minimum payments on time.
3. Don't apply for credit cards that you don't need (such as those offered by stores or online retailers).
4. If you carry a credit card balance, don't allow to get to more than 25% of your available credit limit.
5. You can check your scores for a small fee at www.myfico.com, and you can also get a free estimate of your credit score at www.creditkarm.com, an ad-supported website. Checking your score on your own will not affect your score.
6. Try to build up a long relationship with one or two card companies. But if they don't offer you the best terms and rates, it's worth it to switch.

Buying a car

1. Try to avoid buying a car if you can help it, and instead use your bike, public transportation, Uber, Lyft, and ZipCar.

2. If you must buy a car and need to use it to commute to work, get the most reliable one you can afford. New cars are usually more reliable than used vehicles, but you'll pay more upfront for that reliability. If you have some extra cash saved for future repairs, a used car may be a better idea.

3. If you buy a used car, take it to an independent mechanic before you purchase it. It might cost $50-$100, but it could save you thousands in future repair costs.

4. Don't pay cash for the car, using up all of your savings. Instead, get a low-interest loan through your bank or credit union, and save your cash for emergencies and necessities.

5. Try to drive your car as long as you can. Most cars drop 10% to 20% in value each year, so the less expensive car you own, the less you'll lose to depreciation.

Picking a partner

It's impossible to know what the future will hold if you choose to spend your life with a certain person, but there are a few things that can help you choose a compatible mate, and stay together:

1. Discuss what's important in life, and in money. Do you both enjoy trips, a nice house, and expensive cars? Or do you both prefer the freedom and financial security that money can provide?

2. Either way, make sure you share the same goals and values.

3. Many couples are comprised of a "spender" and a "saver"—that's okay, as long as you acknowledge the worth of your partner's preferences, and find common ground between saving and spending.

4. If you're having trouble reaching an agreement on an acceptable level of spending by one or both of you, you should each write down a list of your short-term and long-term spending and saving goals. Rank them in order, and then combine them to get a mutually-agreed upon list of "allowances" and priorities.

5. In most partnerships, an exact 50/50 split of earnings, household work, and parenting responsibilities is impossible to reach. That doesn't mean you shouldn't try to get as close to that division as you possibly can, but don't be discouraged if you don't quite get there. And if you each feel like you're contributing more than your fair share, you're probably pretty even.

6. Don't worry about what other friends or family members think of your personal financial situation, arrangement, or choices. If it works for the two of you, it's the best way to go.

Having children

If given the choice, almost every parent would gladly choose to have children over again. But the cost of raising and supporting a child (or children) can have a serious effect on your finances.

The U.S. Department of Agriculture says that it costs about a quarter-million dollars to raise a child from birth to age 18, and that figure doesn't include college expenses.

Nor does it include the expense of private schools, higher housing costs to live in a "good" school district, or lost wages and foregone career opportunities.

So if you want to be a parent, go ahead and have children (less wealthy and well-equipped people than you have managed to do it just fine). Just know that there will be a dramatic adjustment to your financial situation.

Buying your first home

1. Don't buy a home until you are likely to be able to stay there for at least five years.

2. Start working on building your credit score before you start shopping for homes.

3. Meet with a lender first, so you can get an idea of what you might be able to afford, and any steps you need to ensure your loan application is approved when you're ready to buy.

4. Your home purchase price generally shouldn't exceed three times your gross annual income.

5. You should plan on making a down payment of at least 10%, and probably 20% of the home's purchase price. If you can't afford those figures, you're probably not ready for home ownership yet. Keep saving—there will still be homes for sale when you're in a stronger position.

6. If you're having trouble getting a seller to come down to a reasonable offer, hire your own appraiser. Either you'll find out that the house is worth more than you're offering, or the sellers will see that their asking price is unreasonable.

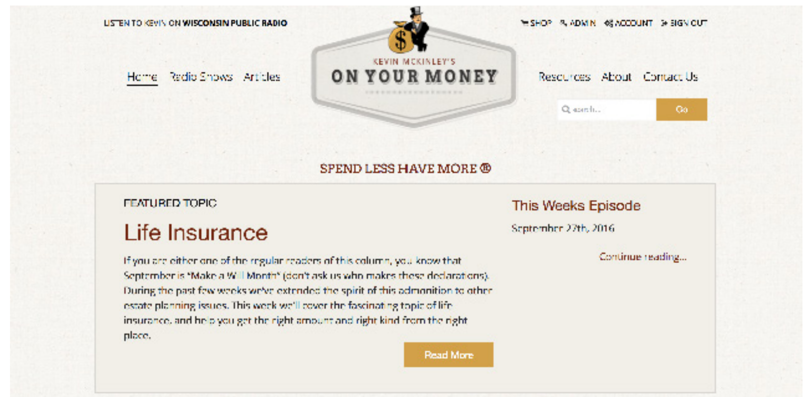
7. If you have or plan on having children, consider if the home is in a neighborhood with other young families, and what kind of schools are nearby.

8. Don't put any more than 20% down on the home. Save that money for repairs, upgrades, and other personal emergencies.

9. Get a 30 year fixed-rate mortgage. Pay it down as slowly as possible, and use any extra funds to save for retirement, college, or emergencies.

10. Try to move as few times as possible. Buy a home that will work for the next several years. It's usually easier to remodel your current home to suit your needs than it is to buy a new one.

Kevin McKinley bought his first share of stock at the age of 14, and began working for an investment firm when he was 17 years old. After graduating with a degree in economics and history from the University of Wisconsin in 1988, he became one of the youngest financial advisors in the country.



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He is now a financial planner and the Principal/Owner of McKinley Money LLC (www.mckinleymoney.com), a registered investment adviser with offices in Eau Claire and Madison that provides fee-based financial planning and investment management to individuals and families.

In 2002 Simon & Schuster published Kevin's book Make Your Kid a Millionaire--11 Easy Ways Anyone Can Secure a Child's Financial Future. The book become one of the best-selling money books for parents at Amazon.com.

Each week Kevin's show On Your Money appears statewide on Wisconsin Public Radio. He writes a weekly newspaper column, and in 2011 was named to the Wisconsin Governor's Council on Financial Literacy. His monthly columns on families and money appear in Wealth Management magazine, the leading trade publication for financial advisors. Kevin's investment expertise has been featured in the Wall Street Journal, USA TODAY, and the New York Times, as well as magazines such as Money, Parenting, and Reader's Digest.

He also speaks to the general public and financial advisors on saving, investing, and spending, and offers unique strategies to help people live by his trademarked phrase "Spend less, have more."

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