

CHAPTER 1

SAVINGS

Why Save?

The **experts** say that good saving habits can begin in children as early as three years old . . . so if you are old enough to read this, you are old enough to have some of these habits. Financial skills are one of the most important skills you will need to navigate your life and those skills start with learning to save and budget.

whoever they are . . .

Unfortunately, at least here in the United States, saving is not a part of most people's behavior. Maybe it's because they did not develop savings habits when they were young—so let's change that.

Why do you need to save money? Because you need money to buy things. Maybe you are saving for a new bike, a new phone, your first car, or just spending money. Maybe you are saving for college. Maybe you are thinking long term and you are saving for your first car, or your first house. Or perhaps you are smart enough to start saving for retirement even though you haven't even gotten your first job. Or maybe you know that you should always have an emergency fund for unexpected costs.

Research has shown that the more you save, the more you want to save. So, build good money habits now and those good habits will stick with you for the rest of your life. Avoid the bad habits that will get you in trouble later.

Global Household Savings Rates

Do yourself a favor and do not follow the lead of most Americans when it comes to saving money. Compared to our neighbors elsewhere around the globe, we save terribly. China and India top the list with a whopping household savings rate around 34%. The global average is 20%. The United States is near the very bottom at 4%. That means, on average, Americans save only 4¢ out of every dollar earned. That's pathetic. Do not be like the average American!



So, how much of every dollar you make should you save? The professionals recommend that you shoot to save between 15–20% of your income. Surely you can at least match the global average.



DID YOU KNOW?

Nearly one-third of American adults have no savings at all for retirement. Almost one-half of all U.S. adults are not even thinking about saving for retirement. And, believe it or not, 21% of American adults actually think that winning the lottery is the best strategy for saving money for their retirement!

Compounding

The sooner you start saving, the better off you'll be. Not just because you will have saved more, but because not only are you making money on your initial **investment**, but you'll also be making money on more money. How so? Well, it's called "compounding"—and it is the power of compounding that will make you lots of money. Compounding is when you make money on an investment, and that money is added to the original investment which in turn makes even more money.

Let's look at an example . . . if your rate of **return** is 10% per year on your original investment of \$1,000, you make \$100 per year. After three years you have a total of \$1,300. But let's say that each year you reinvest the \$100 you made the prior year. . . after three years you would have \$1,331. This is because after the first year, the 10% return applies to \$1,100 rather than just \$1,000. And the second year, the 10% applies to \$1,210. So, the total is \$1,331.

investment: money you have put in an account or otherwise used to make more money for yourself

return: the amount you earn on your investment—usually expressed as a percentage

FUN FACT!

The power of compounding was said to be deemed the eighth wonder of the world by Albert Einstein.



An additional \$31 might not sound like that much money, but what if we increase the numbers and use a real-life example by comparing two savers: One (let's call him Chris) who starts saving when he is 20 years old and the other (we'll call her Katie) who waits until she

annual:
means
yearly

is 30 years old. Each one saves \$100 per month until they are 60 years old. They both get the same **annual** rate of return of 8.5%.

Chris is smart. He read this book and started saving \$100 per month when he was 20 years old and reinvests all earnings. When Chris is 60, he will have an astounding \$406,825!

Katie . . . well, she is not so smart. She didn't start saving as early and waited until she was 30 years old. She saves \$100 per month and also invests all earnings. When she turns 60, she will only have \$166,339.

Chris actually invested only \$12,000 more than Katie (\$100 per month times ten years) but has accumulated a whopping \$240,486 more than Katie! That is the power of compounding. And the earlier you start, the more compounding can work for you. So **start saving now!** Seriously, start now.

DID YOU KNOW?

*A **401K** is a savings plan set up by an employer for the benefit of its employees. In many cases, the employer will match a portion of the money the employee saves! So if you ever work for a company that offers a matching contribution to a 401K, make sure you take advantage of the matching amount the employer gives. It's free money!*

*An **IRA** is a retirement account that is similar to a 401K, but it isn't through your employer—you can set it up yourself. It provides tax savings that might enable your money to increase tax free. As soon as you have a job and earn "taxable income" you can set up an IRA. And remember: the earlier the better. Free money!*

More on
both of
these types
of accounts
in Chapter 7

FUN FACT!

The "Rule of 72" is a quick method to determine how long it will take for you to double your money. You simply divide the return rate into 72. The result is the approximate number of years that it will take for your investment to double. Similarly, if you flip it by dividing the number of years within which you want to double your money into 72, the result is the approximate return you'll need to earn to do so. For example, if you want to know how long it will take to double your money at 8% interest, divide 8 into 72 . . . the answer is 9 years.

TAKEAWAY #1:

Start saving early; let compounding work wonders for you!