The (Not So) Lazy Millennial's Guide to Financial Planning

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Millennials are entitled. Millennials are lazy. Millennials don't work hard. These are just a few of the stereotypes associated with millennials. Are these stereotypes true? Of course not. Millennials (generally defined as people born between 1982 and 2004) are anything but. In fact they have to work harder and smarter than previous generations to achieve financial wellbeing.

Whether your goal is saving for retirement, travelling the world, or just moving out of your parent's basement, the tips that follow will help millennials establish good financial habits that will pay dividends in the long run and maybe even get your baby boomer parents off your back.

1) <u>Track Your Expenses</u>

You may not think the saying "you don't know where you're going until you know where you've been" applies to personal finance, but it's actually very relevant. You can't control your expenses if you don't know where your money is going. Budgeting will help determine your cash flow and capacity for savings. Break your expenses into three categories: 1) essentials (food, shelter, clothing, debt payments, taxes, etc.), 2) wants (dining out, entertainment, travel, etc.) and 3) savings. Depending on your income and lifestyle, you may not have much left over to allocate to savings after covering your essentials and some of your wants. If that's the case then it may be time to step back and prioritize your needs versus wants. The key here is to live below your means by spending less than you make.

2) <u>Manage Your Debt</u>

Managing your debt is important. Pay attention to the interest rates on all your debt and prioritize paying down higher interest rate debt first. Credit cards typically have the highest interest rates–if you use a credit card (and you should) be sure to pay off the full balance each month to avoid interest charges. Student debt is another popular form that many millennials are commonly burdened with. If you do have student debt, consider paying down the higher interest loans first while making at least the minimum payment on the lower interest rate loans. If your cash flow is limited or the interest rates are high, it may be beneficial to consolidate or refinance your loans.

3) Establish a Rainy Day Fund

Saving for the proverbial "rainy day" is one of the most important things you can do. Life can be unpredictable–there's rarely a good time to get laid-off from work or for your car to break down, but if you've planned ahead and set some money aside for an emergency, you'll be much better off when something does go wrong. The rule of thumb is to have three to six months of living expenses sitting in the bank.

If you end up dipping into your emergency fund, replenish it as soon as possible.

4) Max Out Employer-Sponsored Retirement Plans

One of the best places to start your retirement savings plan is in an employer sponsored plan like a 401(k) or 403(b). In a traditional 401(k) or 403(b), you can defer a percentage of your salary ***before*** taxes into a tax-deferred investment account. This investment will grow tax-deferred until you eventually withdraw it. Age 59½ is the magic number it can be withdrawn without paying penalties; however, you will owe taxes at your then current rate. Another popular form of a 401(k)/403(b) to consider is a Roth. In a Roth 401(k)/403(b), you defer a percentage of your salary ***after*** taxes so that when you withdraw funds in retirement you do not have to pay any taxes. If you expect to be in a higher tax bracket later in your career or during retirement, a Roth vehicle may be better suited for you than a traditional plan.

Employers often incentivize employees to contribute to the company plan by offering a company match. With a company match, the employer will match the employee contribution up to a certain percentage. Find out what your company match is, and if you can afford to, contribute enough to maximize the employer match. This is as close to a "free lunch" as you'll find.

5) Save for Other Goals

Setting priorities and avoiding impulse purchases can go a long way when saving for your personal goals. At this point in your life, you may be saving for a vacation, wedding, or your first home. If the time horizon is short, you should keep your savings liquid and safe.

If you've already maxed out your employer sponsored retirement plan, consider investing excess savings into a Roth IRA (check here to see if you're eligible). Fun fact–you can withdraw up to $10,000 from a Roth IRA to purchase a home. Since you've already paid income tax on your contributions, you can also withdraw *all* of your contributions *at any time* without tax or penalty.

6) Invest According to Your Time Horizon and Goal

Depending on your time horizon and risk tolerance, you may choose to invest aggressively, conservatively, or somewhere in between. In any case, it's important to diversify your investments. A diversified portfolio may not generate the highest returns, but in the long run, it's the favored strategy for building and protecting wealth. The most cost-efficient way to diversify your portfolio is by investing in low-cost mutual funds and ETFs. Keep an eye on expenses like fees and trading costs. After all, it's not what you make; it's what you keep that matters.

7) Protect Yourself (and Your Family)

Another consideration for your financial wellbeing is risk management (i.e., health, disability, life, homeowner's/renter's, etc.). It should go without saying that you should have health insurance. If you own a home you should have a homeowner's policy. Your possessions aren't covered by your landlord's policy, so if you rent, renter's insurance is a wise idea.

Your family situation may dictate your need for life insurance. The need for life insurance for a single person with no dependents is much less than that of a married person with a spouse and/or kids. Life insurance premiums are lower when you're young and healthy, so if you anticipate a need for life insurance in the near future, it may be worth purchasing a policy now.

Although the probability is small, your chances of becoming disabled are far greater than dying, so disability insurance is an absolute necessity. If your employer offers disability insurance, participate in the plan. Another option is to purchase an individual policy. Doing so will give you additional coverage that will still be in place if you leave your current employer.

Last but not least, it's prudent to have your basic estate planning documents in order (i.e., health care proxy and durable power of attorney). Basically, these two documents give someone else whom you designate permission to make health care decisions and handle your finances if you become temporarily or permanently incapacitated.

Conclusion

Getting your financial house in order early on in your life and career can lead to a lifetime of financial security. There are a number of free apps and websites that help with this–a couple popular options are Mint and You Need a Budget.

It's important to monitor and re-evaluate your goals and progress annually or whenever there's a major change in your life. A bit of commitment and attention now can make all the difference.
