THE MONEY MARATHON—THE IDEAL WAY TO SAVE—April 09

A well know financial advisor tells the story of having lunch with a multi-billionaire. At the lunch the advisor is interested in learning his secrets for success and asked what books have influenced him the most. He tells the advisor that the book that has influenced his success and wealth the most is a book he read to his kids and now reads to his grandkids regularly. The advisor eager to learn what one book this might be takes out his pen to write down the name and author. The billionaire tells him the book is *The Tortoise and the Hare*. As most of us know the moral to that story is slow and steady wins the race. Good things in life take time, discipline, hard work and a willingness to stick to it and not give up. Effective saving is like this too. It takes discipline, time and unwavering commitment to stick to it.

The realities of the current economic environment are that most everyone will need to save more. What is the best way to save? Ideally, I recommend people save in three baskets.

The breakdown of the percentage of income that should be saved in each basket is 5%, 5% and 10%. I am saying that ideally 20% of every dollar earned should be saved or $20 of every $100. Living expenses and giving (also very important) can come out of the rest. The first basket of 5% is for emergencies. What is an emergency? An emergency is a person’s car breaks down and he can’t get to work or he has an unexpected medical expense or accident or he needs money to live on after losing his job. Until an emergency fund has a minimum of $1000 the other baskets should not be funded. Over time financial advisors recommend that a person have three to six months of income in an emergency fund. So if a couple earns $40,000 annual they should ultimately have $10,000 to $20,000 in a safe and readily accessible fund like a savings or money market account.

The second basket of 5% of income is for short and intermediate goals- what a person needs to buy in one, three, five, ten or even twenty years. This could be saving for a car, a washer-dryer, a vacation, a down payment on a house, or a college education. Some of this money should be invested in totally safe investments like savings, money market funds or certificates of deposit. For longer term goals of three years or more investments in stock funds or other types of investments are acceptable.

The last basket of 10% is a long term permanent investment fund which can also be for retirement. Ideally, this money grows to where the original investment, the principal is never spent, only the earnings or interest. These funds should be invested using an asset allocation plan based on a person’s risk tolerance goals and years to retirement. This can be a mix of stock funds and fixed income according to a plan probably created in conjunction with a financial professional. A great deal of this money should make use of tax deductible retirement funds like 401 k plans or Individual Retirement Accounts (IRAs). These accounts provide an immediate tax deduction for contributions and the contributions grow tax deferred until retirement.

If a person is not able to save 5%/5%/10% he should do what he can. It might be half that 2 ½% /2 ½%/ 5%. Remember once the emergency basket is fully funded then that percentage can go into the other baskets. The discipline and regularity is more important than the amount.

People tell me that there is no money for them to save. I tell them that even $2 saved per day; growing in a retirement account at a 10% compounded rate of return would grow to $1,000,000 in a little over 51 years. Most people can save $2 a day if they work at it. In my case I have a habit of having a stiff drink every day after work-a large Cherry Doctor Pepper at one of the local drive-ins. After tip that costs me $2 a day. We all have our own Cherry Doctor Pepper habits that we could choose not to do. What is your habit that wouldn't have to be indulged and could be saved instead?

Remember slow and steady wins the race.

Remember every investor's situation is unique and it is important to review your specific situation with a financial professional).

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