FINANCE

You Don't Need a Fortune to Practice Good Financial Management

by Bere Lindley and Julia Lucich

At the beginning of each grading period in the eighth grade, Mr. Dove, my P.E. teacher, would explain his grading philosophy to us. "Every one of you," he preached, "starts this quarter with an A. Whether you still have an A at the end of this quarter depends on what you do between now and then." That was startlingly encouraging to me; I had always thought I started the quarter with an F, and that my performance during that quarter merely determined how far I had risen above the F mark.

But to see that I really had an A, and that all I had to do was maintain it, rather than attain it, was a new perspective on the old facts. This perspective allowed me to adopt higher standards. What Mr. Dove showed us was simply a way of pointing out the opportunity that all of us had, yet might have overlooked.

Similarly, many of us who have the good fortune of being Americans have financial opportunity that can be described in the same terms that Mr. Dove used. We embark on our financial courses with an ample retirement income (and we are not talking about social security here). How much of that retirement income we still have when we choose to retire depends largely on what we have done to maintain the bounty that was our opportunity to begin with.

Just how real is that opportunity, and how big is it? Most Americans can afford to save a significant portion of their earnings. If I make $20,000 a year I might be able to live on $18,000. If I make $60,000 I might still be comfortable on $55,000 or even $50,000. When I get raises, I could still have a good living if I committed half the increase to savings. What this comes down to us that the opportunity is very much within reach; the opportunity is real.

The size of the opportunity is surprising to most people. If I sock away an average of $3,000 a year for 30 years (less at first, but more later), I will invest it for a return that might average 9 percent over 30 years of fluctuating interest rates. Given these facts, I will have deprived myself of $90,000 of spending. But at the end of the 30 year period, that $3,000 a year will have accumulated to more than $334,000. As I begin my retirement with $334,000 in the bank, I can draw a perpetual income of about $30,000 a year without ever depleting my savings and investments.

That is how big the opportunity is. If you take into account that the cost of living will be substantially higher 30 years from now, you must also acknowledge that your rising income will increase your ability to save for retirement, and that investment opportunities will be enhanced by inflation. For example, if inflation makes it possible for you to save an annual average of $5,000, and interest rates average only one point higher at 10 percent, your retirement fund will then be worth more than $822,000.

The reason most of us do not follow this course is that we don't realize the imminence of the opportunity. Yet, if we put this opportunity in the same terms that Mr. Dove used back in eighth grade P.E., it can be said that we all start out with a fortune. How much of it we still have at retirement depends on what we do in the meantime. You don't need a fortune to practice good financial management. Even so, you may very well lose a fortune you did not know you had if you don't seek out and use good financial management.

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NEXT WEEK: After the Crash

Organizing Your Finances

Creating organization for our finances is as important and valuable for the person earning $20,000 a year or less as it is for the person earning $150,000 per year or more. The flip side of that is that the person earning the high wage is as likely to be chaotic in his or her approach to financial planning as the person at the lower end of the scale. Knowing how to make money doesn't necessarily mean that we know how to make money work.

The benefit of organizing our finances is that we get a handle on *where* we are spending our money, if we are saving our money and whether we are achieving our financial objectives. This implies, of course, that we know what our objectives *are*, and frequently that is exactly the place to begin.

Since our objectives may often conflict with each other it is also important to give them some weight of priority. As an example, an objective to obtain a new car may be at odds with our desire to put aside money for a child's future college education. Once we are clear on their respective priorities, we have a better opportunity to distribute available monies between them or defer one or the other totally to a future time. This process also gives much greater meaning and understanding to our choice of savings or investment tools.

In the following and future articles we will be exploring in greater detail how some of those financial tools operate and how they can also serve to either support or undermine each other's performance.