IDEAS

HERE ARE THE NUMBERS YOU NEED TO KNOW

Keep your financial health sound by tracking these figures

Liz Weston
NerdWallet

Your doctor needs to know certain numbers to judge your physical health, such as your weight, your blood pressure and your cholesterol levels.

Similarly, you need to know certain numbers to monitor your own financial health, including:

After-tax income and 'must-have' expenses

Your after-tax income is your gross income minus the taxes you pay (federal, state and local income taxes, plus Social Security and Medicare taxes). If you get a steady paycheck, you can use your latest pay stub to calculate this figure. Otherwise, check your most recent tax return.

Divide your after-tax income by the number of hours you worked to earn it. That gives you a rough idea of how much time you're trading when you buy something. For example, if you make $20 an hour after tax and something costs $100, you have to work five hours to afford it. Knowing that figure can help you make more conscious money decisions.

Your after-tax income also is the basis for the 50/30/20 budget, a spending plan that helps you balance current expenses, debt payments and savings. That budget suggests limiting your essential or must-have expenses – shelter, utilities, transportation, food, insurance, minimum loan payments and child care needed to work – to 50% of after-tax income. Wants, such as vacations and dining out, make up 30%. That leaves 20% for savings and extra debt payments.

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GETTY IMAGES

Financial tips for the twenty-somethings in your life

Bray Creech
Columnist

Recently, I spoke with a 27-year-old who works at a local manufacturing company. Our office helps to manage his employer's 401(k) plan, and, on this particular occasion, he called to discuss a recent case of FOMO, or the "fear of missing out." He expressed that he feels he's foregoing the perceived giant gains his peers are making from trading in speculative stocks like GameStop or investing in cryptocurrencies like Bitcoin.

Then, just this morning as I was writing this column, I received an email from a former intern — a 21-year-old college student who had just received his latest Federal coronavirus stimulus payment. He explained that he had been thinking of using the money on prudent investment options, but some of his friends were calling him "lame" for not jumping onto the Bitcoin or nonfungible token (NFT) bandwagons.

While this is not a scientific sampling by any means, I think these two 20-somethings are tapping into a trend that should give some of us pause: a growing societal message about how to build wealth in the 21st century. And it reads like a threat. "If you're not here for the party, then you're doing something wrong — and you're going to regret it for the rest of your life."

If you have a 20-something in your life who is willing to consider your advice, you may want to share with them the following tips about building wealth and financial security over a lifetime.

Tip No. 1: At this stage of life, focus on developing your human capital: the sum total of your educational and work experiences as well as the hard and soft skills you acquire along the way. Your human capital will be a significant determinant of your earnings over time. Invest in yourself but be careful about taking on too much debt in student loans. College is one path to maximizing your earnings potential, but training that can build a valuable skillset over time counts as well.

Tip No. 2: Borrow responsibly. It's better to take on debt for assets that are likely to appreciate in value, such as a home, rather than for things that tend to go down in value, like a car. Pay attention to interest rates, not just the monthly payment quoted to you. Check your credit report once a year from all three national credit reporting agencies (Equifax, Experian, and TransUnion) at AnnualCreditReport.com. It's possible there's some junk on there that's not yours.

Tip No. 3: Be clear with your financial goals. Write them down, whether it's saving for a house or for retirement, paying down high-interest debt, or saving for a vacation in Belize. Set a timeline for these goals.

Tip No. 4: Spend less than you earn. Many financial professionals suggest

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Capping must-haves can help you survive a job loss or other financial setback. You also can use the limits to determine if you can afford a new loan payment. If the payment pushes your must-haves over the 50% mark, the answer may be no.

Lifetime income and net worth

You can access your Social Security statement, including your lifetime earnings history, by signing up at socialsecurity.gov/myaccount. Add up your annual earnings, plus any other income you've received such as gifts, inheritances, investment income, pensions, under-the-table earnings or government benefits. (Estimates are fine.)

Now, calculate your net worth by subtracting what you owe (your debts, including loans, credit card debts and mortgages) from what you own (your assets, such as your home, retirement accounts, investments and savings). Compare your net worth to your lifetime income to see what you've done with the money that came into your hands.

There's no objective scoring system. Like the hourly wage figure, this exercise is meant to make you more aware of what you do with your money. If you think you should have more to show for the money you've received, consider trying to save more of your income.

Related links

Social Security MyAccount: https://www.ssa.gov/myaccount/

Budget calculator: http://bit.ly/nerdwallet-budget-caclulator

Full retirement age and expected Social Security benefit

Your full retirement age is the age at which you are entitled to 100% of the Social Security benefits you've earned. If you apply for benefits before that age, your checks will be permanently reduced. If you delay your application until after full retirement age, you can qualify for delayed retirement credits that boost your benefit by 8% each year until 70 years old, when benefits max out.

The full retirement age has gradually been increasing. For those born 1943 through 1954, your full retirement age was 66. After that, full retirement age increases by two months each year: it's 66 and two months for people born in 1955; 66 and four months for people born in 1956, and so on. The full retirement age is 67 for people born in 1960 and later.

To better plan for retirement, you should have some idea of how much you can expect from Social Security. You'll find estimated benefits in your Social Security statement. (While Social Security is facing a shortfall, the system will still collect enough taxes to pay at least 75% of promised benefits even if Congress doesn't act to shore up its finances.)

Retirement savings rate

How much of your income are you saving for retirement? Is your savings plan likely to let you retire when you want? Anything you can do to close this gap may help you have a more comfortable retirement.

Credit scores and debt-to-income ratio

You'll have a better idea of how lenders view your credit applications if you know your credit scores and debt-to-income ratio. (Good credit also can save you money in myriad ways, from interest payments to insurance premiums.) Monitoring at least one of your scores can allow you to see your progress in building credit and alert you to problems, such as identity theft. To calculate your debt-to-income ratio, combine your monthly debt payments with your current rent or mortgage payment and compare that with your monthly income. A debt-to-income ratio of 36% or less is considered good by most lenders. A ratio over 50% could make it difficult to get approved for new loans. If your ratio is in between those two points, paying off some of your debt could help you qualify for the loans you want (and help you sleep easier at night).

Tips

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saving at least 10-15 percent of your gross salary.

Tip No. 5: Make a budget and give every dollar a job. You can use a spreadsheet or a budgeting app that automatically aggregates your accounts. Read your paystub and have a general sense of the taxes that impact your take-home pay.

Tip No. 6: Unless you're counting on a significant inheritance, your accumulated savings and Social Security will be your main sources of retirement income. But Social Security likely won't account for all of it — and don't count on a pension, either. While 52 percent of those age 71 and older have access to a pension, only 14 percent of Millennials do, according to recent data from JPMorgan Asset Management.

Tip No. 7: Save early and save often to harness the power of long-term compounding. Time is the powerful ingredient here. Even Albert Einstein is said to have once called compounding "the most powerful force in the universe." As a young person with an assumed long life ahead, you've got time in abundance. Harness the power of time to your advantage.

Tip No. 8: When you invest, have a sensible asset allocation tailored to your time horizon, risk tolerance, and financial goals. Studies have shown that asset allocation accounts for approximately 86 percent of portfolio returns. The performance of different asset classes varies year to year, so having a well-diversified portfolio is one way to capture consistent returns over time.

Tip No. 9: Have an emergency savings account of at least three to six months of basic living expenses, and be sure to take full advantage of any employer matches that may be available in your retirement plan.

Tip No. 10: If you feel compelled to invest in speculative things such as Bitcoin or NFTs, scratch that itch with no more than five percent of your total investment portfolio — but, preferably, much less than that. Just be aware that these are, by definition, high-risk investments. And don't check this account every 15 minutes! Go outside and enjoy the sunshine instead.

Talking about money with young people can be hard. But if you're an influential adult in a 20-something's life, your financial wisdom and different perspective may just steer them in the right direction, allowing them to navigate the many money messages out there right now.

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