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Roadmap to Saving and Investing: Make a Financial Plan

Figuring Out Your Finances

You'll need to figure out on paper your current situation—what you own and what you owe. You'll be creating a "net worth statement." On one side of the page, list what you own. These are your "assets." And on the other side list what you owe other people, your "liabilities" or debts.

Your Net Worth Statement

Assets	Current Value	Liabilities	Amount
cash		mortgage balance	
checking account		credit cards	
savings		bank loans	
cash value of life insurance		car loans	
retirement accounts		personal loans	
real estate		real estate loans	
home			
other investments			
personal property			
Total		**Total**	

Subtract your liabilities from your assets. If your assets are larger than your liabilities, you have a "positive" net worth. If your liabilities are greater than your assets, you have a "negative" net worth. You'll want to update your "net worth statement" every year to keep track of how you are doing. Don't be discouraged if you have a negative net worth. If you follow a plan to get into a positive position, you're doing the right thing.

Know Your Income and Expenses

The next step is to keep track of your income and your expenses for every month. Write down what you and others in your family earn, and then your monthly expenses. Include a category for savings and investing. What are you paying yourself every month? Many people get into the habit of saving and investing by following this advice: always pay yourself or your family first. Many people find it easier to pay themselves first if they allow their bank to automatically remove money from their paycheck and deposit it into a savings or investment account.

Likely even better, for tax purposes, is to participate in an employer sponsored retirement plan such as a 401(k), 403(b), or 457(b). These plans will typically not only automatically deduct money from your paycheck, but will immediately reduce the taxes you are paying. Additionally, in many plans the employer matches some or all of your contribution. When your employer does that, it's offering "free money." Any time you have automatic deductions made from your paycheck or bank account, you'll increase the chances of being able to stick to your plan and to realize your goals.

"But I spend everything I make." If you are spending all your income, and never have money to save or invest, you'll need to look for ways to cut back on your expenses. When you watch where you spend your money, you will be surprised how small everyday expenses that you can do without add up over a year.

Small Savings Add Up to Big Money

How much does a cup of coffee cost you? Would you believe $465.84? Or more? If you buy a cup of coffee every day for $1.00 (an awfully good price for a decent cup of coffee, nowadays), that adds up to $365.00 a year. If you saved that $365.00 for just one year, and put it into a savings account or investment that earns 5% a year, it would grow to $465.84 by the end of 5 years, and by the end of 30 years, to $1,577.50.

That's the power of "compounding." With compound interest, you earn interest on the money you save and on the interest that money earns. Over time, even a small amount saved can add up to big money. If you are willing to watch what you spend and look for little ways to save on a regular schedule, you can make money grow. You just did it with one cup of coffee. If a small cup of coffee can make such a huge difference, start looking at how you could make your money grow if you decided to spend less on other things and save those extra dollars.

If you buy on impulse, make a rule that you'll always wait 24 hours to buy anything. You may lose your desire to buy it after a day. And try emptying your pockets and wallet of spare change at the end of each day. You'll be surprised how quickly those nickels and dimes add up!

Pay Off Credit Card or Other High Interest Debt

Speaking of things adding up, there is no investment strategy anywhere that pays off as well as, or with less risk than, merely paying off all high interest debt you may have. Many people have wallets filled with credit cards, some of which they've "maxed out" (meaning they've spent up to their credit limit). Credit cards can make it seem easy to buy expensive things when you don't have the cash in your pocket—or in the bank. But credit cards aren't free money.

Most credit cards charge high interest rates—as much as 18 percent or more—if you don't pay off your balance in full each month. If you owe money on your credit cards, the wisest thing you can do is pay off the balance in full as quickly as possible. Virtually no investment will give you the high returns you'll need to keep pace with an 18 percent interest charge. That's why you're better off eliminating all credit card debt before investing savings. Once you've paid off your credit cards, you can budget your money and begin to save and invest. Here are some tips for avoiding credit card debt:

- **Put Away the Plastic**—Don't use a credit card unless your debt is at a manageable level and you know you'll have the money to pay the bill when it arrives.
- **Know What You Owe**—It's easy to forget how much you've charged on your credit card. Every time you use a credit card, write down how much you have spent and figure out how much you'll have to pay that month. If you know you won't be able to pay your balance in full, try to figure out how much you can pay each month and how long it'll take to pay the balance in full.
- **Pay Off the Card with the Highest Rate**—If you've got unpaid balances on several credit cards, you should first pay down the card that charges the highest rate. Pay as much as you can toward that debt each month until your balance is once again zero, while still paying the minimum on your other cards. The same advice goes for any other high interest debt (about 8% or above) which does not offer the tax advantages of, for example, a mortgage.

Once you understand your income and expenses, have identified spending areas which could be curtailed, and paid off credit card and other high-interest debt, you'll have freed up some money to reach your saving and investment goals.