FranklyFinancial.com

119 Cedar Street
East Hanover, NJ 07936

973-515-5184 • Fax: 973-515-5190
frank@franklyfinancial.com

**Frank McKinley**
Financial Wellness Coach

financial $uccess

**FEBRUARY 2022**

# An Investment Plan for College

To meet your goal for funding a child's college education, you typically need to develop an investment plan. One of the more important factors is your child's age:

✔**Children aged 10 or younger** — With eight or more years until college, you should be able to fund your child's education by setting aside reasonable sums. Since inflation can have a major impact, consider investments with higher return potential. Your long time frame should give you time to overcome any short-term setbacks while keeping ahead of inflation.

✔**Children aged 11 to 14** — With four to seven years until college, you may want to select more conservative investments. If you are just starting to save now, you may find the needed amounts quite large. However, start saving so you'll have some funds accumulated by the time your child enters college.

✔**Children aged 15 to 18** — At this point, continue switching to more conservative investments as college quickly approaches. If you are just starting to plan for college now, it may be very difficult to save the large sums needed in such a short time. Investigate the financial aid process to see if you'll qualify for aid and research your borrowing options.

Other items to keep in mind when developing an investment strategy include:

✔**Start investing as soon as possible.** This can have a huge impact on the amount you need to save on an annual basis. For instance, assume you intend to send your newborn to a public college that currently costs $27,000 per year, the average cost of a public university (Source: *Trends in College Pricing and Student Aid*, 2021), with expected increases of 3% per year. After 18 years, you would need $184,000 to pay for four years at a public university. If you start saving now, you'll need to save $4,913 per year to reach that goal in 18 years. Waiting until your child is age five increases your annual savings amount to $8,560 for 13 years. Start saving when your child is 10 and you'll need to save $17,299 a year for eight years, while the

*Continued on page 2*

## Frankly Speaking

Thanks to all for the Christmas cards and E-cards, in this a most difficult year. Specifically, to my clients & friends, children, grandchildren, cousins, babies, the Eagle Scout, decked out in their PJs & onesies, to newlyweds in Tuxes & Wedding gowns, all the pets: dogs—especially the terriers, cats and even rats. May you enjoy the Christmas Spirit all year and remain healthy while it is more difficult than ever to do so.

If we haven't reviewed your portfolio recently call to set a date for a session to discuss your risk tolerance and time horizon. To start an Estate Plan, (and you can't do this too early) please request templates. You're not alone if you could use my help. You must know others who should be dealing with me too. Please send me their contact information, for their sake.

***"In trading, you must be defensive and aggressive at the same time. If you are not aggressive, you are not going to make any money, and if you are not defensive, you are not going to keep it."*** -Ray Dalio ❍❍❍

## An Investment Plan

*Continued from page 1*

amount grows to $56,678 a year for three years if you wait until your child is age 15. *(These figures assume an after-tax rate of return of 8%. This example is for illustrative purposes only and is not intended to project the performance of any specific investment.)*

✔**Look for tax-advantaged ways to invest.** If your earnings are tax deferred or tax free, you could end up with a much larger balance than if you had to pay taxes on earnings over the years. Take a look at section 529 plans and Coverdell education savings accounts, both of which allow tax-free distributions as long as the proceeds are used for qualified education expenses. Investigate these options thoroughly, however, since various qualifications and restrictions apply.

✔**Select investments that allow periodic contributions.** You may want to make contributions on a weekly or monthly basis, so select investments that allow small contributions. You may also want the ability to automatically transfer funds from a checking or savings account to your college investments.

✔**Adjust your investment mix over time.** As your child gets closer to college age, start moving investments from more aggressive ones with higher return potential to more conservative ones that will help protect your principal. This can help protect your investments from a major downturn that may occur right before your child enters college.

✔**Review your progress annually.** Review your investments at least annually so you can make any necessary adjustments. You may decide to change investments or increase the amount you are saving on an annual basis.

Please call if you'd like help with your investment plan for your child's college education. ❍❍❍

## Assessing Your Risk Tolerance

While investors want the highest returns possible, returns compensate you for the risks you take — higher risks are generally rewarded with higher returns. Thus, you need to assess how much risk you are willing to take to obtain potentially higher returns.

However, this can be a difficult task. It is one thing to theoretically answer questions about how you would react in different circumstances and quite another to actually watch your investments drop in value. What you are trying to assess is your emotional tolerance for risk, or how much price volatility you are comfortable with. Some questions that can help you gauge your risk tolerance include:

✔**What long-term annual rate of return do you expect to earn on your investments?** Your answer will help determine the types of investments you need to choose to meet that target. Review historical rates of return as well as variations in those returns over a long time period to see if your estimates are reasonable. Expecting a high rate of return may mean you'll have to invest in asset classes you aren't comfortable with or that you may be frequently tempted to sell. A better alternative may be to lower your expectations and invest in assets you are comfortable owning.

✔**What length of time are you investing for?** Some investments such as stocks should only be purchased for long time horizons. Using them for short-term purposes may increase the risk in your portfolio, since you may be forced to sell during a market downturn.

✔**How long are you willing to sustain a loss before selling?** The market volatility of the past several years will give you some indication of how comfortable you are holding investments with losses.

✔**What types of investment do you own now and how comfortable are you with those investments?** Make sure you understand the basics of any investments you own, including the historical rate of return, the largest one-year loss, and the risks the investment is subject to. If you don't understand an investment or are not comfortable owning it, you may be tempted to sell at an inopportune time. Over time, your comfort level with risk should increase as you better understand how risk impacts different investments.

✔**Have you reassessed your financial goals recently?** Periodically, your financial plan may need to be revamped. Otherwise, you may find you won't have sufficient resources in the future to meet your goals. Based on your current investment values, determine what needs to be done to meet your financial goals. You may need to save more, change or eliminate some goals, or delay your retirement date.

✔**Do you understand ways to reduce the risk in your portfolio?** While all investments are subject to risk, there are some risk reduction strategies you should consider for your portfolio. These strategies include diversifying your portfolio, staying in the market through different market cycles, and investing consistently.

Please call if you'd like help assessing your risk tolerance. ❍❍❍

# Start Budgeting

Almost no one enjoys the process of analyzing and budgeting expenditures, but inefficient and wasted expenditures can be major impediments to accomplishing your financial goals. It is difficult to manage your money if you don't know how much you have or where it is going. Consider these steps when developing your budget:

**1. Identify how you are spending your income.** Review an annual period so you determine regular monthly expenses as well as irregular, periodic expenses, such as insurance premiums, tuition, and gifts. Much of the information can be found by examining canceled checks, credit card receipts, and tax returns. Total expenses in categories that make sense for your lifestyle. If you can't account for more than 5% of your income, take a closer look at your cash purchases. Keep a journal tracking every penny you spend for at least a month.

**2. Evaluate your expenditures.** If you find it tough to find money to save, critically review your expenditures. Consider these tips:

- Find ways to save at least 10% of your income. Almost all expenditure categories offer potential for savings. With essential expenses with fixed amounts, such as your mortgage, taxes, and insurance, you may be able to refinance your mortgage, find strategies to help reduce taxes, or comparison shop your insurance to reduce premiums. Essential expenses that vary in amount, such as food, medical care, and utilities, can usually be reduced by altering your spending or living habits. For instance, you can actively shop for food with coupons, exercise to get in better health, or put energy saving light bulbs in the house. Discretionary expenses, such as entertainment, dining out, clothing, travel, and charitable contributions, typically offer the most potential for spending reductions. Dining out four times a week? Reduce it to two, go to less expensive places, and save the difference.
- Limit the use of your credit cards, especially if you're not paying the balance in full every month. Not only do credit card balances carry high interest charges, but credit cards tend to encourage impulse spending. Use cash or a debit card, which automatically deducts purchases from your bank account.
- Resolve not to purchase impulse items or items over a certain dollar amount on your first shopping trip. Go home, think about it for a couple days, and then go back to purchase the item. Often, you'll decide you don't really need it.
- Delay the purchase of large items. For example, instead of purchasing a new car every two or three years, keep your car for four or five years.
- If you're really serious about reducing expenses, consider moving to a less expensive house. Not only will you reduce your mortgage payment, but you will save on other costs.

**3. Prepare a budget to guide future spending.** You may want to start by setting a budget for a couple months, tracking your expenses closely over that time period. You can then fine tune your budget for an annual period. Some tips to consider include:

- Don't include income in your budget that is uncertain, such as year-end bonuses, tax refunds, or gains on investments. When you receive that money, just put it aside for saving.
- Set up enough expenditure categories to give you a good feel for your spending patterns, but not so many that it becomes difficult and time consuming to monitor your progress.
- Make your budget flexible enough to handle unforeseen expenditures. Nothing goes exactly as planned, and your budget should be able to deal with emergencies. Be sure to include large, periodic expenditures, such as insurance premiums or tuition.
- Don't be so rigid that your family is afraid to spend any money. Everyone in the family should have a reasonable allowance.
- Find ways to make the savings component of your budget happen automatically. Get the money out of your bank account and into an investment account before you have a chance to spend it.

The money you have available for saving is a direct result of your spending habits. Use a budget to control your spending so you can maximize your savings. Please call if you need help with this process. ❍❍❍

# Avoid These 401(k) and IRA Mistakes

When it comes to saving for retirement, many people take a set-it-and-forget-it approach. But not paying attention to your 401(k) and IRA accounts could cause you to miss valuable savings opportunities. Avoid these seven mistakes:

✔ **Not contributing enough to get your full employer match**. If your employer matches your contributions to your 401(k) plan, you should try to stretch enough to at least meet their maximum match amount.

✔ **Neglecting to maximize your contributions**. While you may not be able save up to your 401(k) contribution limits (for most people, that's $20,500 in 2022 plus an additional $6,500 catch-up contribution for those over age 50), you should save as much as you are able. If there's any extra room in your budget, consider dedicating that money to retirement.

✔ **Playing it too safe by investing in an overly conservative way**. If you only choose safe investments like cash or CDs, you run the risk of inflation outpacing the low returns.

✔ **Not reviewing your investment allocation regularly**. Your asset allocations will inevitably need to change as you age. This means you should review your portfolio at least on an annual basis.

✔ **Not taking advantage of catch-up contribution options**. Once you turn 50 years old, you have the chance to catch up a bit and your maximum annual contributions go up another $6,500 for a 401(k) and $1,000 for your IRA.

✔ **Forgetting about old retirement accounts.** If you've changed jobs, there is a chance that you left an old 401(k) plan with your former employer's plan provider. Of course, the money is still yours, but it may not be doing as much for you as it could if you rolled it into an account you are actively managing now.

✔ **Taking too much of a do-it-yourself approach**. Managing your own retirement planning can be confusing if you do not have the knowledge and skills to make the best choices. Seeking the help or guidance of a financial professional can remove the doubt and emotion from your investment decisions and ensure you are on track for retirement. ❍❍❍



# Is Out-of-State Tuition Worth It?

Out-of-state colleges are significantly more expensive than going to a school in your home state. There are few factors to consider in deciding if it is worth it:

The first factor is cost. According to the College Board, the average costs of tuition for the 2021-22 school year is $10,740 for state residents at a public university and $27,560 for out-of-state residents (Source: *Trends in College Pricing and Student Aid 2021*).

The second factor is comfort. The transition from high school to college is a big one and being in a completely new city without a support system can be a daunting change. As a family, you should discuss how your student reacted to other changes in their life, such as switching to a new school or moving to a new town. Some will easily do well, while others will not. It is important to be honest with yourself as to what your real comfort level will be.

The third factor is your area of study. The expense may be worth it if you have a specialized area of study that is only available at an out-of-state school, or if a specific university's program is exceptional. ❍❍❍

# Financial Thoughts

Despite the coronavirus pandemic's impact in 2020, most retirement plan participants did not make trades, loan use fell, and only a small minority took withdrawals. Loan use declined by more than 20% in 2020. Only 13% of participants had an outstanding loan in 2020, compared to 16% in 2015. Due to the CARES Act, participants were allowed to withdraw up to $100,000 from their retirement plan without incurring a penalty through December 30, 2020. Only 5.7% of those with the option made withdrawals through coronavirus-related distributions (Source: Vanguard, June 2021).

In a recent study, account balances in defined-contribution plans increased by 30% in 2020. 56% of participants are men and have average and median account balances nearly 50% higher than women's account balances (Source: Vanguard, June 2021).

Approximately 45% of Financial Times Stock Exchange 100 index companies have some form of environmental, social, and governance measures within their executive pay (Source: London Business School, Centre for Corporate Governance, July 2021). ❍❍❍