EMPOWER 40: MASTERING YOUR MONEY STORY IN YOUR FORTIES

Book 3

Investment Mastery in Your Midlife: Why Boring is Better

Life Story
FINANCIAL

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Once you’ve empowered yourself to earn more so that you can save more, it’s time to take action and invest that savings towards retirement and other long-term goals.

In a 2023 survey (1), Fidelity found 32% of women cite fear of risk as a barrier to investing. As a result, they tend to be more hesitant to begin investing or to keep contributing. Unfortunately, this fear deters many women from taking control of their financial destinies.

Investing is not an exclusive club reserved for the financially savvy or the risk-takers; it's a powerful tool that can help women secure their financial future and achieve their goals.

(1) Fidelity Investments® 2023 Women’s History Month Survey

COMPOUND INTEREST

While it can be easy to put off investing when you're younger out of fear or because it's not important, making it a priority in your forties can really add up before retirement because of the power of compound interest.

Why You Should Harness the Power of Compound Interest

In my experience, most investors focus on getting higher returns. But what's even more important is to take advantage of compound interest through regular investing. It's a basic model for growth potential. Why?

The more consistently you invest and the longer period over which you do it, the greater the opportunity to create long-term value. The sum of your money can snowball into more money because it's earning interest on itself.

Here's a hypothetical example to illustrate the concept:

Annual Salary: $100,000
Retirement Savings: $50,000
12% of Annual Salary: $1,000/mo

27 Years Later @ 6% average return..... $1,005,586

Let's say you're 40 years old earning a $100,000 annual salary with just $50,000 saved for retirement.

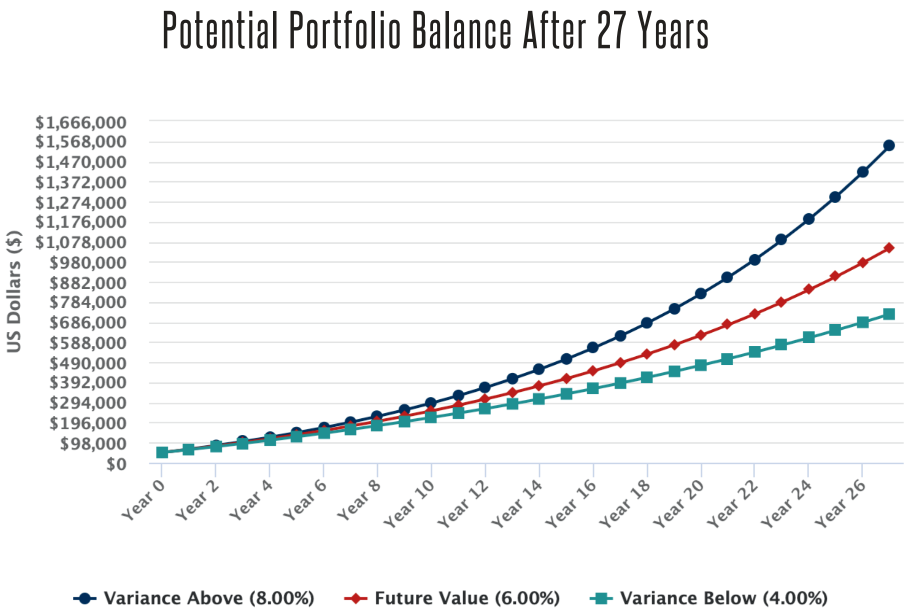
What happens if you start investing 12% of your annual salary, which is $1,000 a month, to your 401(k) plan or other tax-deferred retirement savings account?

If you did that for 27 years to retire at Social Security's full retirement age of 67, earning a fairly modest 6% average return, you could end up with a $1,005,586 portfolio at retirement.

That's right—you could be a millionaire!

Here ‘s the illustration of those results in a chart using the U.S. Securities and Exchange Commission’s (SEC) compound interest calculator. (2)

The middle line shows an overall average 6% return ending in a portfolio balance of $1,005,586. It also shows 2% return variables of 4% at the low end ending with a portfolio balance of $709,179, and 8% at the high end with $1,447,612.



Perhaps even more important than performance, this chart illustrates the power of compound interest from consistently investing over the 27-year time period.

Because of course, as you’re earning more you can save more, leading to more money that can compound over the years!

You can visit Investor.gov to use the compound interest calculator.

(2) Per the SEC, you should understand that slight adjustments in any of those variables can affect the outcome. Resetting the calculator to provide different figures will show you different scenarios.

HOW TO CREATE A LASTING INVESTING HABIT

Can you see why compound interest and systematic investing are such powerful drivers for investment growth potential?

If so, get started by making contributions to your employer retirement plan directly from your paycheck or scheduling automatic transfers from your checking to an investment account. The more automatic you make it, the more likely it'll be become a habit.

You'll get so used to the money coming out that you'll stop noticing it's "gone." And as you incrementally increase how much you're saving, you'll naturally learn to prioritize your spending and cut out the things that aren't important to you.

If you feel like it's too late to start investing in your forties, consider this:

Your salary is probably much higher than it was in your twenties.

Which means you likely have more money you can commit to saving.

And you still have 15+ years of runway to invest it properly and benefit from long-term compounding.

WHERE TO STASH EXTRA CASH

If you're ready to put your extra cash to work, here are my suggestions for where it should go.

Katie finally moved on from living paycheck-to-paycheck. She had an emergency fund, and her checking account was steadily growing. She was feeling motivated to invest more, but wasn't sure how since her 12% contribution (plus her employer's 4% match) meant her 401(k) was maxed out each year.

CONTRIBUTE UP TO YOUR EMPLOYER'S MATCH

- Make sure you're contributing at least enough to maximize the amount of any match offered by your employer—it's *free* money and nobody should turn that down!
- I recommend doing this even if you're still paying off your consumer debt.

EMERGENCY FUND

- If you have a spouse or partner and you're both working, three months of living expenses (it doesn't need to match your income) may be enough in case of an emergency.
- If you're single or the sole income earner for your family, you may want to set aside six months of living expenses.
- If you're a high-income earner or an entrepreneur, you may want to set aside as much as 18 months of living expenses to have some job mobility or can take advantage of business opportunities.

HEALTHCARE SAVINGS

- If you have a Health Savings Account (HSA), only available under a high-deductible healthcare plan (HDHP), you can make a pre-tax contribution of up to the current year's maximum ($4,150 for an individual or $8,300 for a family in 2024).
- If you can pay your health expenses from cash and leave your HSA to grow, you can use the funds tax-free in retirement for qualified healthcare expenses.

WHERE TO STASH EXTRA CASH

RETIREMENT SAVINGS

- You can contribute up to the current year's maximum to your employer's 401(k), 403(b) or 457 plan ($23,000 in 2024).
- You can contribute up to the current year's maximum ($16,000 in 2024) in a SIMPLE 401(k) or SIMPLE IRA plan. If you set up a SEP IRA plan for your business, you can contribute up to the max ($69,000 in 2024).
- You might be able to contribute up to the current year max to a Roth IRA for tax-free distributions in retirement ($7,000 in 2024).
- Note: Eligibility is phased out for higher income earners, so make sure to double check first.

EDUCATION SAVINGS*

- If you or your kids plan to attend college or a trade school, you can invest in a 529 plan* for tax-free earnings when distributions are used for a qualified educational expense.
- You may be eligible for a state income tax deduction or credit if you contribute to a plan sponsored by your state.
- **I believe it's more important to save for your retirement versus paying for your kids' college if you have limited funds. Why? There are no loans or financial aid options to fund retirement, and (hopefully) your retirement will last more years than college.*

OTHER INVESTMENT SAVINGS

- If you've maxed out what you can save in tax-deferred and tax-free accounts but can save even more, consider investing in a taxable brokerage account.
- Are you charitably inclined? If so, consider utilizing a Donor Advised Fund. You can contribute stocks, cryptocurrency or cash and deduct it from your taxes.

Katie decided to hire a financial planner to learn how much she should put away for a travel-focused retirement and where else to save, like to her health savings account.

She also opened a taxable investment account and used the automatic investment plan feature to make monthly transfers from her checking account on payday—meaning she's saving it before spending it!

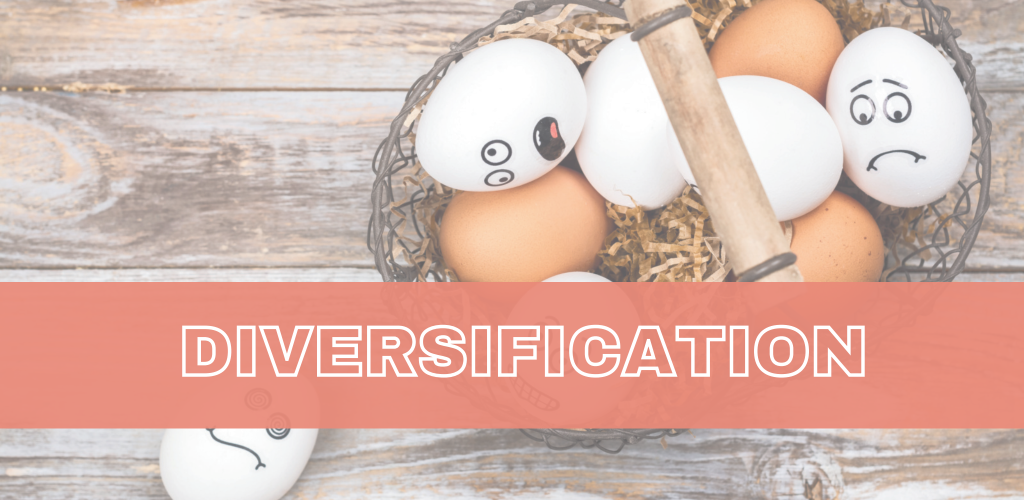
INVEST IN YOURSELF EVEN DURING A BREAK FROM THE WORKFORCE

SPOUSAL IRAS KEEP YOU SAVING EVEN IF YOU'RE NOT WORKING

Keep saving for retirement even if you take a break from your career to care for a child or an elderly family member. If you're married, you can **contribute to a spousal IRA.**

This way, you're still able to take advantage of the power of compound interest. A spousal IRAs ensures that both partners are saving for retirement, fostering a sense of independence for the non-worker and financial security for the entire family.

- A spousal IRA is a type of retirement account set up for the non-working spouse that's funded when the working spouse contributes to it.
- It's not a joint account; it's set up in the name of the non-working spouse.
- Couples need to file joint tax returns to contribute to a spousal IRA.



DIVERSIFICATION

Smart investing isn't hard and doesn't require an expert stockbroker who's clued into the hot stock tip of the day or a hedge fund manager offering a complicated, private opportunity to build wealth. Instead, invest wisely for the long-term with a well-diversified (and boring) portfolio. The experience should be like the tortoise during its race to win—slow and steady.

How Diversification Works

- Diversification spreads risk across different asset classes (stocks, bonds, real estate, commodities, etc.), sectors (tech, healthcare, energy, etc.), industries (in tech there's software, hardware, etc.) and geographic regions, instead of having all your eggs in one basket.
- **A well-diversified portfolio is likely to have at least one portion with a disappointing return, while others are stable or growing.**
- Diversification can reduce the chances that any single investment's poor performance will have an outsized impact on your overall portfolio. It can cushion the impact of losses by offsetting them with gains in other parts of the portfolio.
- Corporate workers who receive stock options or participate in an employer stock purchase plan often overlook diversification when they have a large concentration of company stock in their portfolio.

Here's how this looks. The asset class chart (or "quilt") below was created by Ben Carlson, CFA and portfolio manager for Ritholtz Wealth Management LLC to show how different asset classes performed over a 10-year period.

2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	10 Years
REITs 30.4%	REITs 2.4%	Small Cap 26.6%	EM 37.3%	Cash 1.7%	Large Cap 31.2%	Large Cap 18.3%	REITs 40.5%	Comdty 17.5%	Large Cap 26.2%	Large Cap 11.9%
Large Cap 13.5%	Large Cap 1.3%	Mid Cap 20.5%	Int'l Stocks 25.1%	Bonds 0.1%	REITs 28.9%	EM 17.0%	Comdty 31.1%	Cash 1.4%	Int'l Stocks 18.4%	Mid Cap 9.0%
Mid Cap 9.4%	Bonds 0.5%	Comdty 12.9%	Large Cap 21.7%	TIPS -1.4%	Mid Cap 25.8%	Mid Cap 13.5%	Large Cap 28.8%	**EW -11.5%**	Mid Cap 16.1%	Small Cap 8.6%
Bonds 6.0%	Cash -0.1%	Large Cap 12.0%	Mid Cap 15.9%	Large Cap -4.6%	Small Cap 22.6%	Small Cap 11.4%	Small Cap 26.8%	TIPS -12.2%	Small Cap 16.1%	REITs 7.4%
Small Cap 5.5%	Int'l Stocks -1.0%	EM 10.9%	Small Cap 13.1%	REITs -6.0%	Int'l Stocks 22.0%	TIPS 10.8%	Mid Cap 24.5%	Bonds -13.0%	REITs 11.8%	**EW 5.0%**
EW 4.0%	TIPS -1.8%	**EW 10.0%**	**EW 12.6%**	**EW -7.2%**	EM 18.2%	**EW 7.8%**	**EW 16.3%**	Mid Cap -13.3%	**EW 10.2%**	Int'l Stocks 4.2%
TIPS 3.6%	Small Cap -1.8%	REITs 8.6%	REITs 4.9%	Small Cap -8.6%	**EW 17.5%**	Int'l Stocks 7.6%	Int'l Stocks 11.5%	Int'l Stocks -14.4%	EM 9.0%	TIPS 2.3%
Cash -0.1%	Mid Cap -2.5%	TIPS 4.7%	Bonds 3.6%	Mid Cap -11.3%	Bonds 8.5%	Bonds 7.5%	TIPS 5.7%	Small Cap -16.1%	Bonds 5.7%	EM 1.8%
EM -3.9%	**EW -4.7%**	Bonds 2.4%	TIPS 2.9%	Comdty -13.1%	TIPS 8.4%	Cash 0.4%	Cash -0.1%	Large Cap -18.2%	Cash 4.9%	Bonds 1.8%
Int'l Stocks -6.2%	EM -16.2%	Int'l Stocks 1.4%	Comdty 0.7%	Int'l Stocks -13.8%	Comdty 7.6%	Comdty -4.1%	Bonds -1.8%	EM -20.6%	TIPS 3.8%	Cash 1.1%
Comdty -18.6%	Comdty -28.2%	Cash 0.1%	Cash 0.7%	EM -15.3%	Cash 2.0%	REITs -4.6%	EM -3.6%	REITs -26.2%	Comdty -9.9%	Comdty -1.9%

Funds: EEM, VNQ, MDY, SPSM, SPY, EFA, TIP, AGG, DJP, BIL

Showing returns for the years 2014 to 2023, each color represents a different asset class with the highest annual return at the top. You can see there's a lot of fluctuation (or color) over time between the winners and losers.

Here's what Ben has to say: "I have no idea what this quilt will look like next year. The reason this is my favorite performance chart is that it perfectly illustrates how difficult it is to predict the winners and losers in the short run."

Katie and her financial planner came up with a plan to reduce her concentration in her telecomm company's stock. She sells her shares as soon as they vest and invests at least 50% of the proceeds into her well-diversified taxable investment account.

She feels good saving more for retirement while still enjoying the benefits of her hard work today!

DIVERSIFICATION MAY REDUCE VOLATILITY

A well-diversified portfolio can also reduce volatility*, which is the degree to which prices are fluctuating up and down for stocks, bonds, commodities or indexes.

Now, here's the nifty part: by having a more stable investment journey, you increase the chances of your money steadily growing over time. Reduced volatility means a smoother ride, and when your returns are more predictable, your money gets the opportunity to grow consistently. This is especially good news because consistent growth over the years and decades can add up to some serious wealth.

Think of it like this: When your investments experience fewer high and low swings, the compounding effect (where your money earns more money over time) can work its magic without too much disruption from the poor performers.

So, the longer you keep your money invested in a diverse and less volatile portfolio, the more money is available to slowly and steadily grow over the long-term, creating a stronger foundation for your financial future!

Are you investing but want to know how much to save for retirement? Download the fourth title in my *Empower40: Mastering Your Money Story in Your 40s* ebook series called *Scripting a Flexible Plan for Your Retirement Readiness*.

*Diversification and/or any investment strategy that may be discussed does not guarantee against investment losses, but are intended to help manage risk and return. If applicable, historical discussions and/or opinions are not predictive of future events. The content is presented in good faith and has been drawn from sources believed to be reliable. The content is not intended to be legal, tax or financial advice. Please consult a legal, tax or financial professional for information specific to your individual situation.

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Ready to Plan for the Next Chapter in Your Financial Life?

Michelle Francis

Next Steps

✓ Download the other eBooks in my *Empower40: Mastering Your Money Story in Your 40s* series.

✓ Subscribe to my newsletter for common sense money and finance tips delivered straight to your inbox each month.

✓ Follow my blog for practical advice to better manage your money and finances. I write about topics related to life and career changes, business ownership, taxes, investing and preparing for retirement (or just slowing down).

Get to Know Me!

I'm Michelle Francis, the founder of Life Story Financial. I'm a fiduciary, fee-only financial planner who will not only teach you the ins and outs of your finances but will help you identify the "why" behind your money. I'm passionate about helping women in their forties make better money decisions to gain financial independence.

My practice is fully independent, so I'm able to offer flexible pricing that includes flat-fee financial planning, an hourly fee for advice on a topic or two, and an asset-based fee for investments.

I'd love to talk to you about your top money questions and concerns. You can schedule a free, no-pressure introductory call with me today to learn more about how I can help you plan for the next chapter in your financial life.

Book Here

MICHELLE'S FAVORITE *Financial* THINGS

Be on the lookout for emails from me with even more ideas on how to transform your finances. They'll include links to some of my favorite resources, including articles, blog posts and videos. My goal is to keep you motivated by educating you on how to manage your money with confidence, support yourself financially and empower you to reach your goals.

> *Give a woman a dollar, and she can put it to good use. Teach her about how money really works, and she can change the world.*
>
> *-Linda Davis Taylor,*
> *CEO of Clifford Swan Investment Counselors*

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