EPISODE 1067

[ASK FARNOOSH]

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FT: Welcome to So Money, everybody. It is Friday, July 10th, 2020. Stores and restaurants and camps are reopening here in New Jersey. I’m still keeping it indoors though, guys. I’m not really feeling the need to go to Lululemon right now and I'm most concerned about schools. How are schools going to reopen in the fall? Because ultimately, that is what supports the economy, right? We need our schools to be open, so our children can be engaged, learning so that mom and dad can work and bring home the money. Why doesn’t anyone understand this? You want to tell me why we’re not throwing money at schools and not bailing out schools. They’re already underfunded. This idea of sending my son to school a couple days a week, let’s just homeschool them because then I at least know what my days look like every single day. But then who’s going to pay for that?

There was a really great article in the New York Times, a couple of articles about the importance of steering our attention to schools and supporting teachers and faculty so that we can reopen schools in a safe way. It’s never going to be 100% safe but we need to think more about this. I don’t want bars open. I want schools open. But that, of course, is going to take more money, more planning, more strategy.

All right, moving on, I did something a little wild and crazy recently. I, wait for it, moved some money around in my retirement portfolio. Yes, I didn't just set it and forget it. I didn't just do nothing as the advice has been over the last several months as we’ve seen the market really just do flips and become a roller coaster ride. We don't know where things are headed, and so I was worried but I also knew not to let my fears make any stupid moves. But what I did do and I do recommend this to everybody listening is take a look. Take a look under the hood and see where your money is being invested. At the very least, look at the allocation of your portfolio. You can do this if you’ve got a 401(k), if you’ve got an IRA or a brokerage account online. You can go and look at what is the mix.

I've been pretty aggressive in my portfolio. For many years, I've been 80% stocks and 20% bonds, fixed income cash. 80% stocks, I was okay with that for the last 11 years and I benefited from that. But now, I'm not 30 anymore. I'm not 35 anymore. I'm 40 and I want to be able to tap this money as early as 60. That gives me 20 more years. Is an 80% stock allocation really wise at this point, given that also we don't know what is happening this year and next year?

Now, I'm not investing for the short term obviously. I'm investing for the next two decades, plus. But 80% really made me stop and think I'm not comfortable with this, and there is a rule of thumb. You take 100, you subtract your age, and that is the ballpark in which you should be putting your money in the stock market. That is the exposure percentage-wise. The rest in these sort of safer havens, fixed income, bonds, cash.

I re-appropriated the money. I went from 80% to 60% stocks and increased, as a result, my exposure to things like bonds and cash. I feel really good about this. I'm going to write a piece about it for Bloomberg Opinion, I'm a new columnist there, about why I did this, which goes against a lot of what we're hearing which is do nothing. I had a reality check which was that I'm not getting younger. My time horizon is shrinking between now and when I want to tap this money.

What we experienced in the last 11 years, that crazy run-up in the stock market, that is less likely to happen again in our lifetime. What is more likely to happen in our lifetime is a pandemic, another pandemic. Recessions are cyclical. Recessions happen about every five years, some steeper than others. Given all of that historical reference, given my risk tolerance, given my age, given where I want to be in 20 years, I made a more conservative move and moved some money out of the market and moved it more towards fixed income, bonds, cash.

Call me crazy. This isn't really against the advice I've been giving. It's just that it is counter to the general lies you hear out there which is like, “Don't worry. Don't do anything. The market's going to do its thing, and you're going to be fine in 20 years.” I want to be more than fine in 20 years. I've been working really hard investing my money and I want to have something spectacular to show for it when I go to retire. I don't want just okay returns, right?

Everybody, check your allocation. If you're approaching retirement, especially, I'm talking to my fans out there who are my parents' age. Mom and dad, if you're listening. I've recently had a conversation with them about this. I said, "How much of your money is in the stock market?" My dad said like, "75%." I said, "Maybe you want to think about dialing that back." It's not just your age, right? It's also a factor of where you are in your life, what are your goals. I am responsible for my family financially and I want to not just build wealth for our lifetime but I want to create generational wealth. Those are my goals. 80% stock exposure, I'm fortunate for that over the last 10 years. But looking ahead, I am moving towards being more conservative.

This advice once you really hear it from me and you really understand why I did this is not contrary to what all the experts tell us to do that, but it is against sort of the blanket statements we hear that like, "Oh, just don't worry. Don't do anything. The market's going to do its thing." No, take a look. Make sure you're okay with your allocation. Don't honestly pull out of the market, which some people are doing. I don't understand that. I still believe in the stock market. It's just about how deep do I want to be in the stock market. All right. So I just wanted to share that for full disclosure. I think it's important to stay transparent.

Okay, let's go to iTunes and pick a reviewer of the week. I'm going to say thank you this week to lcpmr who gave five stars on July 7th, my mom's birthday. She said, "The absolute best financial series in 2020. The guests are knowledgeable, on point, and on message. The Black Wealth Matters series was groundbreaking. I'm a black woman who is grateful that Farnoosh used her platform for us. She clearly understands that setting aside a whole month to focus on an underserved portion of our country benefits us all. Farnoosh is a bona fide soul sister."

Oh, my gosh! I got goose bumps. Thank you so much for that review. I'm so proud of the series. If you've been listening to the show since the series ended, you know that the conversations with African Americans and black individuals continues. We had Rodneyse Bichotte on the show on Monday, July 6th. She is an assembly member in New York State, representing parts of Brooklyn, and she is just remarkable. The adversity that she's had to overcome is unbelievable. From an accident when she was 10 years old that nearly paralyzed her to getting her MBA, working for Barack Obama, and then coming back to New York and being the first Haitian-American woman ever elected in New York City. I mean, she is a force and someone to watch.

But anyway, thank you so much for this review. I learned so much from the Black Wealth Matters series. I'm actually writing a piece about that for NextAdvisor, and the learning continues. I would like to connect with you, lcpmr. The way to get in touch is to email me, farnoosh@somoneypodcast.com, and let me know you left the review. I'll send you a counter link where you can select a time for us to chat. Everybody listening, if you want a chance to connect with me for a 15-minute phone call, here is how it works. Go to iTunes. Leave your review, your honest feedback about the show. It could be good. It could be somewhat critical, whatever. I read everything. Every week, I pick one reviewer to receive a free 15-minute money session with me, so go for it.

Okay, heading out to the mailbag. We have several questions this week, some about where to park cash, where to invest, what to do with student loans. Okay, first up is Sarah. Sarah writes in on Instagram and says, "Hey, Farnoosh. I grew up in a household where money was tight and awkwardly never talked about. I'm in my early 30s now and I'm just now realizing money isn't scary. It's powerful. Here's my question; my husband and I, both 33-years-old, have just recently started making six figures between the two of us. We have no debt, great credit scores and we're saving up to buy a house in the nearish future. We have a good chunk in savings, about 40,000, and we're contributing lots each month for our future down payment. My question is how do we focus our output of money between saving for retirement, which we haven't really started, and buying a house? It's tough to know how to divide everything up in a productive way. Thanks in advance. Love your podcast."

Okay, Sarah. Well, first of all, congratulations crossing that six-figure threshold. Kudos to the two of you. Great job saving $40,000. I would like to know how far that $40,000 will stretch. If you lost your job tomorrow, or your husband dead, or the both of you dead, how far could that $40,000 go to cover all of your expenses without any income coming in? And not all of your expenses, right? Because if you're not working, you're not obviously spending on all the things. You're just focusing on the barebones.

I just interviewed a friend, Jully-Alma Taveras. She is also known as Investing Latina. She's my friend. We write together for Next Advisor. She has a column out there on how to come up with your survival number. The survival number you need every month to live; housing, food, transportation, the barebones. Times that by 6 to 9, and that's a healthy amount of savings to have in cash tucked aside somewhere in case of an emergency. Does that $40,000 fulfill that? If the answer is yes, then I'll tell you this much, you're done saving for a rainy day. Okay? Just check that off your list. If not, then you still have more work to do. Before you invest more for retirement, before you put money away for that down payment, I want you to beef up rainy day savings. Got that?

Let's assume that's all squared away. You're left with your down payment and retirement. The thing that I have learned about retirement savings is the best way to do it, the best way to approach it so that it's easy, so that it's done-done-done, is to make it automatic. If you have a 401 (k) at work, if your husband's got a retirement plan at work, automatically contribute I would say 10%, now that you're making money of every single paycheck into this diversified portfolio within the 401 (k) or the 403 (b) or whatever it's called at your company, and just do that. Get that started.

Now with whatever is left in savings every month, you can now work with this money to allocate that towards the down payment on your home. I would encourage you to not just save for the down payment, but also closing cost, because that is also part of the cash that you will need before you buy, and I would prefer that to not come from emergency savings. So whatever the price tag of the homes that you're looking at are, whatever range they're at. If it's like let's say $300,000, then you want to take about 2% to 3% of that and put that away in another account, and that's just closing costs. Okay? You may not have to pay as much as that at closing, but that is there for you in the event that you have to use it. As someone who just went through the process of buying a home, you need the down payment, you need the closing cost. And part of those closings costs will include the first couple of months of the mortgage. That's good. That gives you a little bit of a cushion when you move in, you're not immediately paying the mortgage. I mean, you are, but you've already paid it. You know what I mean? It's not that frenetic in the beginning where, "Yeah, I got to make sure that I hook up my bank account to my mortgage account and make sure that I make the first payment." It's all done at closing and probably for the next couple of months, maybe 3 months. That's always good. But have that money set aside.

So make sure emergency account is bulked up, 6 to 9 months tucked away. Once you got that done, automatically start contributing to your 401 (k) 10%. If you can already start doing this, do it. And then with the money that you have left, start to put some of that towards the down payment. Separate that from emergency so that you can just clearly see how it's growing and where you're at.

Next up is our friend Brian who says, "I find that I struggle, Farnoosh, in finding information on intermediate savings goals. I'm currently 21. I'll hopefully be getting married and make some other large purchases, like a home, a trip, I don't know, in the next 10 years." Yeah, who knows when they're traveling again, right? He says, "Do you have any advice or any suggestions of where to look to find more advice on intermediate savings? I've searched many blogs, websites, but find limited or very general information about intermediate savings goals."

All right, Brian, well you're very ambitious at 21. Looking to save for these intermediate goals. I applaud you. I would check out Morning Star. Their director of personal finance, Christine Benz, has written about this, and she gives some nice strategy around this. In general, the rule of thumb is for money that you don't need to access for at least 10 years, this is money that you may consider putting in something other than a savings account that's earning nominal interest, that maybe you can afford to take on some risk with this money, but not a ton. Because as we know, it sometimes takes markets longer than 10 years to recover. If you experience a huge downfall in the market within the first few months of pouring all these money into your portfolio, it could take a while for things to perk up again.

Questions you want to ask yourself. Do I want a guaranteed return on this money? If you know that you're getting married in the next 5 to 7 years and you don't want to risk this money, then you don't put it in the stock market. You do put it in something like a CD or just a high-yield savings account. You also want to be tax conscious if you do decide to put your money in stocks. There's going to be income tax potentially, capital gains tax maybe on any profits that you make when you withdraw the money. So keep that mind as you calculate the pros and cons.

Now back to Christine Benz, the director of personal finance at Morning Star. She says that historical returns suggests that if your time horizon is less than 10 years, stocks have been too unreliable. For goals that are 10 years away, she suggests opening a brokerage account having some of that portfolio be in low-fee funds, like index funds, ETFs, but do mix it up with bonds and other safer havens, fixed income. Diversification is always important, but when you have a shorter time horizon, we talked about allocation way in the beginning of this podcast. You may not want to be majority in stocks in this portfolio. You might want to be more like 30% or 40% stocks.

She does actually recommend very specifically municipal bonds and bond funds. Why? Because they are often times free from federal tax. And in some cases, state and local tax. So that's getting pretty specific. Check out Christine's work at morningstar.com. In general, Morning Star is a great site. If you want more context, more information, more of the nitty-gritty behind what is in the various mutual funds that you're investing in, the ETFs, they do a lot of great market analysis, economic analysis. I've been referencing them for decades. So they're still around. That speaks for itself.

I know that if you go to any number of automated investing platforms, like Intelligent Investor from Schwab, Elevest, they will ask you about your goals and your time horizon and then create a portfolio for you that aligns with that. All right, good luck to you and thank for listening.

Okay. Meandra is up next, and she says, "Hey, Farnoosh. I just recently found your podcast during my financial journey, and I'm addicted. I listen to on my commute, while cooking dinner, doing household chores. Thank you for all your money and life wisdom."

Well, thanks, Meandra. And I'm happy to hear that you're still commuting and doing some routine things. "I'm reaching out for some advice," she says. "I've recently been on a financial journey with my husband to becoming debt free. We have student loan debt and a mortgage for our home, but no other debt. My student loans are at $55,000 at 6.4%. My husband's at 50,000 at 6.1%. We contribute to our employee match retirement programs and we have a four-month emergency savings account, but no other retirement accounts. This pause on student loan interest has made us question what we should do when the interest resumes. Should we refinance our public student loans for a lower interest rate separately or should we refinance together? We also wonder if we should use our extra money to pay down the debt or open a Roth IRA account. What are your thoughts?"

For this, first question that you have about what to do with your student loans. Yes, you should try to refinance. But I would try to just individually refinance. I think you can probably get better than 6% each of you. So explore that. The problem with refinancing together is now you're both on the hook for over $100,000 in debt. My only issue and concern with consolidating debt with you partner or debt that came into the marriage and wasn't something that you both created together in the relationship is that you're both going to be on the hook for this if there is a split.

Sometimes when you get divorced or you split up, like you just want to clean break. And this debt is going to be the thing that has to be constantly dealt with post-divorce. I assume you're both responsible, but what if one person isn't paying their fair share? Both of your names are on this debt, and if one person fails to contribute, it doesn't matter, the debt is due, and you're going to have to pay it. Otherwise, you will see your credit suffer.

So it's just cleaner, keep your credit profiles separate. The only time I might pause and say, "Hmm, maybe we should do this together," is if the insurance rate is significantly lower if you consolidate both together, versus just refinancing your 55,000 and his 50,000. So explore it. Talk to your bank and talk to other banks, shop around.

Now I would also like to see your emergency account closer to 6 to 9 months. So I would work on that in the meantime. Now that you're not paying your student loans, you have that provision to basically defer your payments until the end of September. If you've got the money lying around, I would use that to bulk up savings, and that's before adding money to the retirement account. You're already contributing to your 401 (k)s, that's great. All right. Good luck to you.

A question from Grant, last but not least, who just sold his house. It seems like he's moving, and he wants to know what should he do with his workplace 401 (k)? Should he cash out? Should he roll it over? "Just sold our house and we will be looking to buy again in 10 to 14 months," he said. So sounds like a lot of big moves going on in your life, Grant. You got a new house, got a new job. Your wife has a new job. Congrats to you. That's really awesome.

I think it would make sense to roll over your 401 (k), and you said you have a state retirement fund that has not vested yet. But whatever you have contributed, you could presumably roll that out into a new retirement account. If you want to keep everything streamlined, under one roof while you kind of figure out your next steps, that's smart. Not a bad idea. The mistake is to pull it out. Of course, cashing out is going to mean penalty, it's going to mean taxes, it's going to mean getting a very small amount at the end of the day from what is currently on that balance sheet. So rolling it over is the key. If you both already have new jobs with new retirement plan offerings, you can roll over your old accounts into these new accounts. Just don't cash it out, which we know can be expensive. But congrats to the both of you, and best wishes.

Keep the questions coming, every Friday, we're back at it with Ask Farnoosh. Thanks for tuning in everybody. I hope your weekend is so money.

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