EPISODE 605

[ASK FARNOOSH]

[0:00:32.4]

FT: You're listening to So Money everyone, welcome back or welcome for the first time. I have to say, I'm really just – I like start crying every time I go to iTunes because you all have been so generous and kind and giving with your reviews you know?

It's not easy staying in the top 10 or the top 20 of iTunes in your category as a podcaster but I check every day because I'm obsessed and we you know, sometimes are on the top 10, sometimes top five, sometimes top 20. I'll take it.

And reviews help so much, you have no idea. I mean, I think they do, it's not a coincidence I think when I get a couple of new reviews and I soar in the rankings. Of course, iTunes is very kind, always has us in the what's hot section.

You know, as an independent female podcaster, to be amongst such names as Wall Street Journal, Market Place, Bloomberg, it's a big deal, for me at least and I think it's a huge complement to our audience because clearly you're dedicated and you know, you're very kind with the feedback. I have to say, I mean, I don't know if I had – if I was listening to a lot of podcasts.

Would I have time to write a review? I think I would if I really loved it so it means so much to see that we have over 460 reviews and I don't really solicit them like I used to, I used to really – a lot in the beginning but I just feel like you know, I really appreciate so much already that you guys have done for me.

I guess if you want to write another review, that would be amazing but I'm not going to twist your arm. Anyway, just wanted to take a beat to say thank you for that because it is something that's – I wake up feeling very grateful for every single day and now that we have a chance to really talk on the Friday episode as I turn the tables and make it all about you, I really wanted to just say that and so thank you.

It's Friday and I am sans cohost today. I was supposed to have a cohost and our schedule has just got knotty and we were unable to record but just so you know, I am still very much interested in finding cohosts for these Friday episodes and rotating the hot seat with a listener who wants to share the mic with me and tackle some of these questions.

You can very easily get in touch, you can either email me with your intent and your hope to record with me, email me, farnoosh@farnoosh.tv. You can also go to somoneypodcast.com and on the right hand corner, click on the purple button that says Ask Farnoosh and let me know through that.

You can also ask me a question there too but you can also just let me know that you know "hey, can I cohost with you" and let me know a little bit about you, how to get in touch with you and we'll try to really make it happen.

I get a little bit more requests than I have Fridays available at the moment and so it may take a while but we do consider every single person who shows and expresses interest. Just want to let you know that that is still something that I'm very much looking forward to doing.

This week, we have a number of questions, just looking ahead at some of these questions about where to park our money and retirement. I think that, it is not a coincidence that we're looking at the economy and the political world and feeling a little uncertain and that's trickling down and impacting our savings behavior.

The reality right now is that we are saving more money than we have been in probably 10 years. Our average personal savings rate, household savings rate is five and a half percent which means for every dollar we're bringing home, we're pocketing, we're saving 5.5 pennies which may not sound like a lot but if you consider how much we were saving back in 2007 during the recession.

We are vastly improved, we were saving I think around 2% back then. It definitely skyrocketed to about 8% at one point because we were all in the thick of losing our jobs and losing money so we were really scared to part ways with our cash. It has since subsided but since January, since our new president has taken office, savings rates have increased and I do think there's a correlation between people feeling uncertain and therefore wanting to keep close tabs on their dollars.

Not putting it in the market, not putting it in real estate, not blowing it on stuff, spending is down, consumer confidence has been you know, trending a little bit lower. Honestly, I'm kind of in this camp too, I will admit, I'm a little nervous about what's around the corner, we don't know what's happening with healthcare costs for someone like me who is an entrepreneur.

I worry about these wild cards, where will our healthcare costs be, how much more will I have to pay, perhaps next year? I don't know. Where is the stock market going, who knows? We're looking at the Dow and thinking, we didn't even think we crossed 20,000, now we're at 21,600 in change and you know, some might say it's a little frothy, overvalued.

It's a term that's being thrown out there. Not to say that's a reason not to invest for the long haul but certainly if you're just watching the markets every day, it's nerve wracking, it can be. As a result, we're seeing not as many people investing.

I want to say, it's still a good time to invest. In fact, when times are a little uncertain and when you're seeing dips in the market, that's actually a good time to get in. Get in low and of course if you have a long term trajectory, you have years and years, decades until retirement, you don't have to be worried about these fluctuations.

It's just power for the course. We have a lot of questions around all of this and our first is from an anonymous listener, a female who's left a question via Speak Pipe and we will play that right now and see what's on her money mind. Here we go.

[0:06:53.6]

FEMALE: Hi Farnoosh, my husband and I are 33 and 34 and have two small children, my husband just inherited about $100,000 and we are trying to decide the best way to invest this money. Would you recommend a CD, an index fund through Vanguard, or something else?

We are doing well financially and are on track with retirement, emergency savings and 529's. We don't expect to need access to this money within the next three to five years and want to put it somewhere that's low risk but also earning higher than 1% interest. Thanks so much for your feedback.

[0:07:28.9]

FT: Alright, thank you for your question. Just a recap, she and her husband are in there early 30's, they've got two kids and congratulations I guess right? $100,000 in inheritance. Trying to decide what to do. What to do with a huge lump sum of cash that you don't need right away, in this case she says, we won't need access to it in the next three to five years.

I don't think putting it in your savings account or your cheque account is ideal, you want to get a little bit more bang for your buck here, a little bit more returns and there are places where you can, believe it or not, get more than 1%. The caveat being that you were going to keep this money tied up for at least five years, if you'd go to a site like nerdwallet.com.

I used to work there and they have a really robust search engine for savings accounts, CD's, money market accounts, all sorts of savings vehicles, you type in your zip code, you type in how much money you want to save and how much time you've got and they will basically crank out a bunch of places online, offline where you can do that, you can park your cash and earn more than a percent, I actually did a little bit of –

Was curious so I went in and I just typed in my own zip code and I put in $100,000 like this woman with a three to five year horizon. There are a number of places where you can get over 2%. So, if you don't need this money, and you don't need to be liquid for at least five years, yeah, I'd say go look at something like a CD, maybe an index fund, maybe not.

I think you know, with a five year horizon an index fund, safer than a stock, an individual stock but you still are invested, you're exposed to volatility, more volatility than a CD, more risk than a CD and so I don't know if in five years you could recover from a real drop.

I think if you have 10 plus years then I think investing in something like an index fund, an ETF stock's, a little bit more manageable but I think for a shorter timeframe, a CD is probably a better way to go, a five year CD.

Look at nerd wallet. Also, bankrate.com has similar technology where they can find you, different kinds of accounts, based on your time price and your risk tolerance, how much money you're looking to park. Alright, good luck.

Another question from Nicole and this is also an audio question. I love audio questions, I love hearing from you so let's take it away Nicole

[0:10:05.2]

Nicole: Hi Farnoosh. My name's Nicole and I wanted to get your opinion of target date funds. The company I work for added them as an option, a little over a year ago, managed by Vanguard, fee expense is .1% which doesn't seem terrible for me since I do not spend a lot of time looking at it. I'd love just your opinion, thanks.

[0:10:36.0]

FT: Alright, target date funds is the thing, this is the question and so, I used to invest in target date funds when I had a 401(k) through my employer, they're very popular vehicles, offered through a variety of employer sponsored retirement accounts like 401(k)'s, 403(b)'s, it is often an option, on the one hand, there are advantages in that with a target date fund and let's just take a step back, what is a target date fund?

Target date funds are made up of a lot of different funds that represent different investment styles, different asset classes and they usually have a target date which is usually the name of the fund.

A target date that's like a 2020 fund or a 2040 fund, that date is when the fund assumes you're going to be ready to tap this cash when you're going to be "retiring" and so based on that date, the investments are adjusted with that in mind to be as risky or less risky or more risky.

The longer you have until retirement, let's say it's 2040, 2050, the allocation today, the exposure today in that index, in that target fund will probably be riskier than something that is like a 2020 fund, assuming you're going to be tapping this money a lot sooner and so you wouldn't want to be invested too heavily in a lot of stocks, a lot of aggressive stocks.

The other thing that's great about targeted funds is that, it adjusts. Today, if you're investing in a 2040 fund, it starts out a little bit more on the riskier side, as you approach 2040 it automatically adjusts, rebalances to adjust for risk, adjust for the time horizon.

For those of us who like to set it and forget it, like sounds like Nicole says she doesn't spend a lot of time looking at her investments, this is not a bad option. With that mentality comes risks right? You never want to set it really and forget it. You want to be able to check in, you want to be a little bit more vigilant about your investments, you know, maybe not checking them every day or every week.

But quarterly, looking at the investments and even before you invest in something like a target date fund, it's important to know what the mix comprises of. What are the different investments, are you comfortable with them.

You should look up these individual investments online through a site like Morning Star or Yahoo Finance or the site for that fund itself and look at the history of performance. I have read that some critics don't like target date funds because they generalize and they say that a lot of these funds just throw in some really weak low performing funds, mixing them in with some higher performing funds.

But sneaking these other lower performing funds in just to keep it alive and getting people to pay for them even if they are not the best within their asset class. So do some due diligence. Don't assume that you're getting a fantastic mix of funds. Yes, there is the benefit of having that target date and it readjusts automatically and it risk adjusts automatically but you still want to be aware of how your money is being invested.

And so that would just be the one thing and of course, these funds come with various fees and so you want to be aware of what are those fees. There's obviously the fee that you pay your financial adviser but there is also the fee for investing in a particular fund and that fee compounds annually. So do the math there is it really worth it? Maybe you are better off just being in an index fund for the next 25 years which typically carry much lower fees, okay?

That was a little nerdy of me going through that but that's why I guess you come here, you come for the fun, you also come for the nerdiness of going through the technicalities of things like target date funds. Eve wants to know:

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EVE: What percentage of a six figure income do I suggest go towards investing in things like stocks, real estate, savings, retirement and so forth?

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FT: So what's the investment hierarchy, I actually wrote about this for Mint.com and it was not respective of how much money you are making and I honestly think that no matter how much you're making, these rules of thumb are applicable to all. If you have a lot of money and not a lot of expenses then maybe you have more room to invest but I think at minimum everyone should be looking to invest 10% of their take home pay in a long term investment portfolio.

Intended for retirement that might be a 401(k), that might be a 403(b) for others, that's might be if you don't have access to an employer sponsored account, it might be a brokerage account or a Roth IRA or an IRA, whatever, something aggressive where you're in the stock market smartly for a long term period, I think up to 10% maybe even more than that like 15% if you are playing some catch up.

If you haven't been saving at all for retirement and you're 40 years old and you're like, "Oh my god, oops, I got to play catch up" I think something like 15% is better. I actually read an article in the New York Times last weekend I think it was in the op ed section or in the business section, Sunday Times, a man who for his entire life has written about retirement and how much to save wrote a piece.

An opinion piece that was like, "You know I was kind of conservative about how much I had said that we should save because now I am actually going through the whole retirement phase and regretting how much I actually save". He saves probably 10% and now he's saying save, whatever you think you should save tack on another 15% or increase that savings rate by 15% because you just never know what else is going to come your way.

That will be a financial distraction, that you just will need more money for whether that's health care or your home that's falling apart because you haven't been maintaining it for the last 20 years because you have been spending money on your kid's college or what have you. So check out that article. It was in the New York Times Sunday section about the title was like, "What I wish I had said about retirement savings" or "The advice that I never gave".

It's really insightful especially coming from somebody who is in it now who can speak from within the trenches but anyway, I had said I had written for Mint.com about your hierarchy of investing needs and the first is obviously have a rainy day account and it's not really investing your money. That's just saving your money in the event that you lose your job, you have to crash together some expenses because you weren't expecting –

I don't know, a health care bill or your car maintenance or whatever, some sort of access to cash so you don't have to dip into credit. Cash that can foreseeably cover your expenses, your necessary expenses for at minimum six months and that money you are just putting in a liquid account. You don't worry about interest rate on that, just something that you have access to quickly and then after that it's retirement savings or retirement investing.

Through your work, 401(k) plan, 403(b), an IRA then you might look at something like a 529 plan. If you've got kids and wondering about college savings and then if you've got money left over and you still want to invest and then you look at maybe opening up a brokerage account, creating a diversified portfolio there and then if you've got even more money, you could look at alternative investments like retirement, like real estate.

I don't know jewelry, art, a lot of people like to invest in all sorts of things just remember that with any alternative investment, you want to be smart about the exposure to risk. So you don't want to put all your money in the real estate basket. You put you know, I would say no more than five or 10% of your investment holdings in something that is on the very risky side. Alright, Vanessa's got a question and again it's about saving money:

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VANESSA: She has a personal credit union savings account and she contributes a said amount to it every paycheck, great job Vanessa, and now she wants to know should she additionally participate in her employer's 403(b) plan.

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FT: So my feeling on this Vanessa is that you are talking about apples and oranges. So you've got the apples, that's your savings account that's something that you're automatically contributing to that will come in handy in an emergency, awesome. A for that. Separately you want to save for a long term goal like retirement and by doing so, you can be more aggressive in something like a 403(b) plan.

Which invests your money in things like we talked earlier, target date funds also probably other kinds of mutual funds, index funds, ETF's, perhaps individual stocks. Through that plan, you want to create a diversified risk adjusted portfolio that speaks to your investment needs, your investment horizon and you can sometimes pair up with somebody that works on the inside of that plan and can help you navigate all the options.

And pick something really right for you and that is something that is completely separate. It could be more advantageous than opening up a brokerage account because maybe your employer will also match, dollar for dollar, sometimes employers match their employee's contributions and that's free money and you want to be able to take advantage of that to the utmost. So yeah, I think if you don't have anything for retirement yet start with your 403(b) plan at work.

And look at the types of investments, the fees and all of that and you can maybe compare that to say opening up an IRA, a Roth IRA. The thing about a 403(b) and a 401(k) as opposed to let's say an IRA is that you can invest much more in something like a 403(b), a 401(k) than an IRA every year. So if you like the plan and you want to save a lot of money go with that. If you don't have a lot to start with and you're not so crazy about the 403(b) plan at work.

Because the investments are not so great, fee heavy, something like a Roth IRA or a traditional IRA could be a good alternative, okay? Alright, last but not the least, Chris has a question:

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CHRIS: Also about Roth IRA's. He says that he wants to know if he is still eligible for a Roth if your bonus plus your income puts you over the income threshold. He says he makes about $72,000 a year in salary but with his bonus, the maximum bonus, it could tip over a $100,000. So will he be in a position to no longer be eligible to invest in a Roth IRA.

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FT: And so, what we know is that unlike a traditional IRA, a Roth IRA does come with an income limitation. So once you make over a certain amount of money, your contributions get modified down and then after certain income level you are totally phased out. If you are single Chris, you have to have a modified adjusted gross income of under $133,000 to be eligible to contribute to a Roth for this tax year.

And your contributions begin to get reduced at a $118,000. If you're married, your adjusted gross income must be less than $196,000 and your reductions began at $186,000. So it sounds like you may be able to contribute the full $5,500 this year and that's for 2017. You can invest up to $5,500 in a Roth IRA. If you are 50 or over, you can do a catch up contribution an additional $1,000 for a total of $6,500.

So I think the good news here is that you could still do it up to the max but as you make more, just be aware of these income limitations and every year they get adjusted or updated. Sometimes they stay the same, sometimes they get adjusted so just check with the IRS website, irs.gov just to keep abreast of all of that.

All right, thanks Chris, thanks Vanessa, thanks Eve, thank you Nicole and our anonymous listener who left a question through Speak Pipe. Good luck with your inheritance. I want to know what happens so please keep in touch and the same goes with all of you. Thanks so much for tuning in everyone. I hope you have a great weekend. I am headed off for the beach for two weeks. I'll be offline, well sort of, trying to.

It's my goal this year to really just relax, you know? Dip my feet in the pool maybe my whole body, trying to go for the full swim okay? Wish me luck and I wish you all a wonderful rest of your summer and I'll be back in two weeks, taking your questions as usual but in the meantime, we're do have some new episodes available for you and then we'll do some reruns. You know it's August, we've all got to take some time off but we'll be back with a bang before you know it.

Thanks so much and hope your weekend is So Money.

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