

LEARNING MADE EASY



3rd Edition

Personal Finance in Your 20s & 30s

**for
dummies[®]**
A Wiley Brand



Reduce debt, spend less,
and avoid financial mistakes

Invest wisely and
accomplish your goals

Build your personal
financial plan

Eric Tyson, MBA

Bestselling author,
Investing For Dummies

Personal Finance in Your 20s & 30s

Building a Solid Personal Finance Foundation in Your 20s and 30s

You're finished with school and entering the workforce. You want to make sure you create a firm foundation for your personal finances. Keep the following in mind when you start:

- » **Get a checkup:** Just as you benefit from a health checkup, be sure to get a checkup on your finances to ensure you're making the most of your money and your financial decisions.
- » **Determine what you need with transaction and savings accounts and evaluate which banks and other financial firms offer accounts that best meet your needs.** Be on guard for high fees that erode your savings.
- » **Celebrate the savings habit.** The earlier in life you're able to save money regularly, the smaller the portion of your income you'll need to save to accomplish a given goal. Scrutinize your current spending so you know where your money is going and you can identify what to do about it.
- » **Be on the lookout for spending reduction opportunities.** Regularly saving money, especially on a modest income, is challenging. I present many ideas for reducing your spending, but ultimately, how you cut your spending is a matter of personal preference.
- » **Understand good and bad debt.** Debt can be a useful tool to enable the purchase of real estate or other valuable assets. Avoid consumer debt, such as on credit cards and auto loans. Consumer debt tends to be costly, and the interest isn't tax-deductible.

Managing Finances and Daily Living in Your Young-Adult Years

Getting a paycheck and having a job requires more responsibility. Be sure to consider these important points when you're encountering finances in your 20s and 30s:

- » **Know and manage your credit score.** Your *credit score* is a number that quantifies for lenders how likely you are to repay debts. Periodically access your credit reports, which you can do for free, and understand the steps you can take, as needed, to boost your credit score. Also take steps to protect your identity.
- » **Consider all options before deciding to rent or buy.** Renting and sharing living space can be both economical and fun if you avoid the pitfalls. Buying and owning may make sense if you see yourself staying put for an extended period of time.
- » **Communicate with your partner about money.** Money is often a source of friction in relationships. Thinking about money and planning how to manage it upfront with loved ones is usually time well spent.

Protecting Yourself and Your Income

Insurance plays a significant role in protecting your interests, including your health, your income, your property, and so on. Make sure you insure the following:

- » **Your health:** Though you may feel that you're not likely to need it, having health insurance is wise. With a properly designed plan, you can contain the cost and get needed coverage.
- » **Your income:** Even if you have no dependents, you surely depend on your income, so you should have long-term disability insurance. And if you have dependents, you may need life insurance, too.
- » **Your possessions:** Insurance on your car, home, and other valuable possessions protects those assets from loss and damage and protects you from lawsuits. Beware, though, of small-stuff policies that aren't worth buying.

Praise for Eric Tyson

“Eric Tyson is doing something important — namely, helping people at all income levels to take control of their financial futures. This book is a natural outgrowth of Tyson’s vision that he has nurtured for years. Like Henry Ford, he wants to make something that was previously accessible only to the wealthy accessible to middle-income Americans.”

— James C. Collins, coauthor of the national bestseller *Built to Last*; former lecturer in business, Stanford Graduate School of Business

“*Personal Finance For Dummies* is the perfect book for people who feel guilty about inadequately managing their money but are intimidated by all of the publications out there. It’s a painless way to learn how to take control.”

— National Public Radio’s *Sound Money*

“Eric Tyson . . . seems the perfect writer for a *For Dummies* book. He doesn’t tell you what to do or consider doing without explaining the whys and hows — and the booby traps to avoid — in plain English. . . . It will lead you through the thickets of your own finances as painlessly as I can imagine.”

— *Chicago Tribune*

“This book provides easy-to-understand personal financial information and advice for those without great wealth or knowledge in this area. Practitioners like Eric Tyson, who care about the well-being of middle-income people, are rare in today’s society.”

— Joel Hyatt, founder of Hyatt Legal Services, one of the nation’s largest general-practice personal legal service firms

More Bestselling *For Dummies* Titles by Eric Tyson

Investing For Dummies

A *Wall Street Journal* bestseller, this book walks you through how to build wealth in stocks, real estate, and small business as well as other investments. Also check out *Investing in Your 20s and 30s For Dummies*.

Mutual Funds For Dummies

This best-selling guide is now updated to include current fund and portfolio recommendations. Using the practical tips and techniques, you'll design a mutual fund investment plan suited to your income, lifestyle, and risk preferences.

Home Buying Kit For Dummies

America's #1 real-estate book includes coverage of online resources in addition to sound financial advice from Eric Tyson and frontline real-estate insights from industry veteran Ray Brown. Also available from America's best-selling real-estate team of Tyson and Brown: *House Selling For Dummies* and *Mortgages For Dummies* with Robert Griswold.

Real Estate Investing For Dummies

Real estate is a proven wealth-building investment, but many people don't know how to go about making and managing rental property investments. Real-estate and property management expert Robert Griswold and Eric Tyson cover the gamut of property investment options, strategies, and techniques.

Small Business For Dummies

Take control of your future, and make the leap from employee to entrepreneur with this enterprising guide. From drafting a business plan to managing costs, you'll profit from expert advice and real-world examples that cover every aspect of building your own business. Also check out Tyson's *Small Business Taxes For Dummies*.

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3rd Edition

by Eric Tyson, MBA

*Author of *Investing For Dummies* and *Mutual Funds For Dummies**

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Introduction

Your 20s and 30s are such an exciting time. During this period you're experiencing some dramatic changes in your life, exploring new endeavors, making your way in the world, trying new things, and meeting new people, while hopefully staying in touch with old friends and your family.

But as with anything else in life, your young-adult years can pose challenges as well. Some young people suffered layoffs and reduced employment incomes during the 2008 financial crisis and its aftermath and then again with the 2020 COVID-19 pandemic. Maybe you've experienced a failed relationship and a broken heart. You've likely had to deal with a difficult boss (or two) or a job (or two) you don't like — or perhaps you're in danger of losing your job.

And then there are the money issues. Most of you are out of the nest and out from under your parents' wings, and your 20s are when you experience firsthand earning your own money and paying your own expenses. This isn't true for all twenty-somethings, of course, because some young people still live at home or have some financial dependence on their folks — maybe that's why *they* bought you this book! No matter your living situation, your young adult years can be a challenging time, but this friendly guide can help make those years smoother and more rewarding financially.

About This Book

Based on my experiences teaching courses, counseling clients, writing articles and books, and corresponding with friends, family, and people through my website, I've discovered how important having healthy and strong personal finances is. With that in mind, I wrote this book to help you begin to lay a strong financial foundation. Your early adult years are the best time to start.

I've worked with and taught people from all financial situations, so I know the financial concerns and questions of real folks just like you. Believe it or not, I first became interested in money matters when, as a middle-school student, my father was laid off and received some retirement money. I worked with my dad as he made investing decisions with the money. A couple of years later, I won my high school's science fair with a project on what influences the stock market.

In my 20s, I worked hard to keep my living expenses low and save money so I could leave my job and pursue my entrepreneurial ideas. I accomplished that goal in my late 20s. My goal in writing this book is to give you lots of tools and information to help you get your personal finances in order so you, too, can achieve your goals and dreams.

I also wrote this book to protect you, to watch your back. Hucksters out to separate you from your hard-earned money know an easy mark when they see one, and being young and, therefore, less experienced makes you a target. You're also at increased risk of "being taken" because your generation spends so much time online where the rules and agenda of many sites and apps are murky or worse. The information and advice in this book can help you identify and steer around common pitfalls and bad deals before you suffer the consequences.

Foolish Assumptions

No matter what your current situation is — whether you're entering the job market right after school, graduating college with or without student loans, living with your parents, or living on your own — I thought of you as I wrote this book. I made some assumptions about you:

- » You want expert advice about important financial topics — such as getting a financial checkup, budgeting, paying off some debt, boosting your credit score, and investing — and you want answers quickly.
- » Or perhaps you want a crash course in personal finance and are looking for a book you can read cover to cover to help solidify major financial concepts and get you thinking about your finances in a holistic fashion.
- » Or maybe you're just tired of feeling financially frazzled and want to get better organized and on top of your money matters.

This book is basic enough to help a novice get his or her arms around thorny financial issues. But readers who are a bit more advanced in financial matters will be challenged, as well, to think about their finances in a new way and identify areas for improvement.

Icons Used in This Book

The icons in this book help you find information you need:



TIP

This target flags strategy recommendations for making the most of your money.



REMEMBER

This icon points out information that you definitely want to remember.



WARNING

This icon marks things to avoid and points out common mistakes people make when managing their finances.



INVESTIGATE

This icon tells you when you should consider doing some additional research. Don't worry — I explain what to look for and what to look out for.

Beyond the Book

To view this book's Cheat Sheet, simply go to www.dummies.com and enter "Personal Finance in Your 20s and 30s For Dummies Cheat Sheet" in the Search box. There you'll get quick tips on understanding financial basics, managing day-to-day finances, and growing your money through basic investing.

Where to Go from Here

This book is organized so you can go wherever you want to find complete information. Want advice on minimizing your taxes, for example? Go to Part 2 for that. You can use the table of contents to find broad categories of information or the index to look up more specific topics.

If you're not sure where to go, you may want to start with Part 1. It gives you all the basic info you need to assess your financial situation and points to places where you can find more detailed information for improving it.

1

Getting Started with Personal Finance

IN THIS PART . . .

Evaluate your net worth, savings rate, credit health, investment portfolio, and insurance coverage.

Develop a savings mindset, as well as budgeting and saving strategies.

Conquer consumer debt and recognize the best uses for loans and the types of debt to avoid.

Get and understand your credit report and credit score.
Use your credit report and other tools to prevent identity theft.

IN THIS CHAPTER

- » Determining your net worth
- » Calculating your savings rate
- » Getting your credit score and keeping an eye on it
- » Growing your investment portfolio
- » Protecting yourself with insurance
- » Examining common money mistakes

Chapter 1

Your Financial Checkup

Where did your childhood years go? Was it that long ago that you were concerned with what exams you had coming up, what you might be doing over your summer break, and what kind of job you were interested in and qualified to do?

As a young adult, you wonder where you are going to live, how much a decent apartment will cost, and how much you will actually have left over after taxes and those other pesky deductions that are taken from your paycheck. How much will it cost to buy a home that you'll really want? What are the best ways to save and invest your money?

And then life throws you a curveball like the COVID-19 government-mandated shutdowns which turned plenty of young people's lives upside down in a way that few saw coming. Or perhaps an aging parent or other relative needs some help. How can you handle these situations personally and financially?

Those are some pretty big questions that even people 20 and 30 years older than you struggle to answer. You're wise to be thinking about these topics now. In this chapter, I help you start to answer those questions by showing you how to evaluate your net worth (addressing any debt, such as student loans, credit cards, or auto or other consumer loans). I also help you assess your savings rate, credit health, investment portfolio, and insurance coverage so you can develop and implement a winning plan tailored to your situation.

Calculating Your Financial Worth

Having a sense of what you own (your *assets*) and what you owe (your *liabilities*) is important because it provides some measure of your financial security and your ability to accomplish financial goals such as buying a desired car, buying a home, traveling, starting a business, or retiring someday.

In this section, I define net worth and then walk you through the relatively simple calculations of determining your own personal net worth.

Defining net worth

Your *net worth* is quite simply your *financial assets* (for example, checking, savings, and investment accounts) minus your *financial liabilities* (debts such as student loans and credit-card debt). In the following sections, I walk you through how to perform these calculations.



REMEMBER

When I discuss your monetary *net worth*, I'm not talking about personal possessions. Your car, clothing, television, computer, and other personal items all have some value, of course. If you needed to sell them, you could get something for them. But the reality is that you're unlikely to accumulate personal items with the expectation of later selling them to finance such personal goals as buying a home, starting a business, retiring, and so forth. After all, personal property declines rapidly in value after purchase and use.

Figuring what you own: Financial assets

To calculate your financial assets, access your checking/savings, and investment account records, including retirement accounts and any other documentation that can help you. You may have only one or two accounts, and that's fine. The COVID-19 pandemic has proven the absolute need for emergency fund savings. Add up all the values of these accounts to find out what you own.

It's common for most young adults to be in the early stages of accumulating assets. This book helps you change and improve upon that.

In addition to excluding personal property and possessions because folks don't generally sell those to accomplish their personal and financial goals, I would also probably exclude your home as an asset if you happen to own one. (You can include it if you expect to downsize or to rent in retirement and live off of some of your home's equity.) Include investment real estate — that is, real estate that you own and rent out.

VALUING SOCIAL SECURITY AND PENSIONS

Now or in the years ahead, you may accumulate some retirement benefits based on your years of work. You may do so through the federal government's Social Security program and/or through an employer's pension plan.

When you work and earn money, your employer (or you if you're self-employed) pays taxes into Social Security, which earns you future Social Security retirement income benefits. Under current laws, which of course may change, you're eligible to receive full Social Security benefits at age 67. (You may collect a benefit reduced by 30 percent if you begin receiving your Social Security payments at age 62.)

In surveys, most young adults say that they're more likely to believe in things like UFOs than in actually getting money out of Social Security! Although being skeptical and questioning things is useful, such deep cynicism about Social Security isn't well founded. Those who are eligible to receive benefits (generally, folks who've paid Social Security taxes above relatively low threshold amounts over at least ten years in total) should get them. As a young adult, it's important for you to also know that some Social Security benefits, such as disability and survivorship benefits for your children under 18, are a part of your Social Security insurance coverage.

Some employers provide a retirement benefit known as a pension that's paid to you in retirement based on your years of service (employment) with the organization. Your employer puts aside money above and beyond your salary compensation into a separate account to fund your future pension payments. Pension plans are more common in public-sector organizations (governments, schools, and so on) and larger companies, especially those with labor unions. Pension plans are generally insured/guaranteed by government agency entities.

Now, I do have one exception to something that isn't generally thought of as a financial asset, which you may or may not want to include in this category. Some people have valuable collections of particular items, be they collectible coins, sports memorabilia, or whatever. You can count such collections as assets, but remember that they're only real assets if you'd be willing to sell them and use the proceeds toward one of your goals.

Determining what you owe: Financial liabilities

Most people accumulate debts and loans during periods in life when their expenditures exceed their income. I did that when I went through college. You may have

student loans, an auto loan, credit-card debts, or a medical or pet debt. Access any statements that document your loans and debts and figure out the grand total of what you owe.

Netting the difference

After you total your financial assets and your financial liabilities, you can subtract the latter from the former to arrive at your *net worth*:

$$\text{financial assets} - \text{financial liabilities} = \text{net worth}$$

Don't worry if you have a small or negative net worth (where you have more debt than assets). There's no point wringing your hands over the results — you can't change history. And, it doesn't matter how you compare with your peers even if we can accurately define exactly who your peers are. *This isn't a competition or test.*

But you can change the direction of your finances in the future and boost your net worth surprisingly fast to work toward accomplishing your personal goals. First, you have to figure your savings rate and how to increase it, which I discuss next.

Grasping the Importance of Your Savings Rate

To accomplish important personal and financial goals such as building an emergency fund, buying a home, starting a business, traveling, and someday retiring, most folks need to save money. Some exceptions do exist, such as those folks who have trust funds or inherit significant-enough sums that they don't need to save money from their work earnings. But the vast majority of people must save in order to accomplish their goals.

You can't effectively save for a long-term goal if you don't know what your savings rate is. When I worked as a financial counselor and taught adult-education money-management courses (which I now do online), I was struck by how few people knew the rate at which they were saving money. Most people can tell you how much they earned from their work over the past year, but few folks really know what portion of their employment income they were able to save. That's because to have an accurate idea of this percentage, you really need to do some analysis and calculations. The math isn't that complicated, but it does require some time and effort, especially if you haven't been tracking your spending or net worth over the past year. In the following sections, I explain a couple of different ways to calculate your savings rate over the past year.