Title:
How to Have Financial Peace

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Summary:
One of the biggest contributors toward personal peace is financial peace. Sometimes it is assumed that financial peace is only for those with endless amounts of money. In actuality, you can be financially secure at almost any income level. Avoiding common financial mistakes is the first step. This article discusses some mistakes that many of us make and how to avoid them.

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Article Body:

One of the biggest contributors toward personal peace is financial peace. Sometimes it is assumed that financial peace is only for those with endless amounts of money. In actuality, you can be financially secure at almost any income level. Avoiding common financial mistakes is the first step. This article discusses some mistakes that many of us make and how to avoid them.

I'm Too Young to Settle Down

Not investing in a home or buying one too late in life is a mistake that more and more people are making. The reason it is a financial mistake is illustrated in the following example. Let's say Brittany makes $60,000 a year, is single and rents a home for $2000 dollars a month. When tax time comes, she has little or nothing in the way of deductions. In 2005 she would have had to pay $11,665 in federal taxes alone. If she had put that same rent payment toward a mortgage payment instead and purchased a $315,000 home with a 30 year fixed rate of 6.5%, her mortgage interest deduction would have been $20,236, saving her $5,059 in taxes in 2005.

Tax savings isn't the only reason to buy a home. Another reason is the investment it represents. Let's say Brittany did buy a $315,000 home in January of 2005 and its value increased 5% in one year. The 5% increase in value would give her $15,750 in equity by 2006 and she would have paid $3,657 toward principle as well. Let's add it up. Rent money saved, $24,000 + taxes saved, $5,059 + equity earned, $15,750 + principle purchased, $3,657 - interest paid, $20,236 = $28,230, or $2,352 per month saved by purchasing a home. Even if she put $1,000 into that home each month in the way of maintenance, she still would have saved over $1,300 per month in 2005 by buying a home.

But It Was On Sale!

Accumulating debt instead of savings is the next financial error to avoid. Unless debt can almost guarantee you a future return, such as investing in a business, education or your home, it is best to avoid altogether. Even purchasing automobiles with cash is better financially in the long run. As an example, let's look at a household that has a credit card balance of $10,000. Assuming a 15% interest rate, if they pay $150.00 per month on the card and don't put anything else on it, their total interest and principle paid to that card is $21,635 before it gets paid off. It will take them over 12 years to pay it off at this rate. They are paying $80 in interest a month for the "privilege" of having credit card debt.

There is even more to the debt picture, however. Debt is not just one sided, there are opportunity costs associated with debt. If they weren't putting $150 a month toward their credit card, they could instead be putting it into a savings account. Putting $150 a month into a savings account with a 4% rate of return compounded monthly for 12 years would grow to almost $28,000, which is $21,600 in principle and $6,400 in interest earned. So now the real cost of a credit card is the interest paid, $11,635 + the foregone interest from the savings account, $6,400 = $18,035 in 12 years or $125 per month of lost money.

Do You Accept VISA for my Mortgage Payment?

Not having any liquid savings is another area that can end up hurting you financially. The minimum amount to be saved is 3-6 months of living expenses. This will help to cover loss of income or medical emergencies that may arise. This money should only be tapped for major emergencies and not for things like vacations or weddings, which should be saved for in other accounts once the liquid savings has been established. When no short-term savings is available, the risk of bankruptcy increases. With the new bankruptcy laws it is becoming increasingly difficult to erase debt.

Liquid savings is especially important when you have a large income that is not standard across the industry, or when there is not a high demand for the type of work you do. In these situations, finding a new job with the same income may be difficult. This can leave you vulnerable to rushed decisions that can damage you financially for years to come. As an example, I have a friend who had made good money at a software company for 20 years. His income was quite high because he had been with the company for a long time. The company was eventually purchased and he was laid off. He and his family had just finished building and furnishing their dream home when it happened. While they didn't have massive amounts of debt, they didn't have any liquid savings either. In order to get out from under their house payment, they sold their home for much less than it was worth, they also emptied their 401(k) and both had to take low paying jobs just to make ends meet. Now, eight years later, they are just starting to crawl out from under it all, but without their dream home or a retirement account.

Natural Disaster...Here?

Little or no insurance is a mistake that many people make hoping they won't be hit by a natural disaster. Insurance is your best defense against financial ruin in such a situation. Sitting down and talking with an insurance agent is the first step. Make sure that the policy covers those things you are worried about. Set aside the money needed for the deductible on the policy if a disaster does occur. Other things to prepare for in a disaster is the possibility of being out of work for several weeks or months, high medical bills or being left without an automobile if it is also destroyed in the disaster. Liquid savings is the answer to these problems. Remember, just because the home or vehicle no longer exist doesn't mean that their payments have gone away.

I Have Plenty of Time to Save

Not saving for retirement is a mistake that is made all too often. If you do save, there is a good possibility it is not enough to retire on. The findings of the 2006 Retirement Confidence Survey put out by the Employee Benefit Research Institute suggested that many American workers are not prepared for retirement and will have to work far longer than they expect. As an example let's look at Jane who is 55 years old and currently makes $60,000. She hopes to retire at age 65 and has already put away $250,000. By the time she retires, her home will be paid for and she assumes she can live off 70% of her current income or $42,000. If she lives to 90, she will need to have income for 25 years. Let's assume her $250,000 grows at a rate of 7% until retirement and 6% once she starts taking the money out. We need to also account for inflation which averages about 3% per year. In order to have $42,000 per year for 25 years she will need $1,151,243 in her retirement account by age 65. That means she will have to start contributing $58,919 per year for the next 10 years to reach this goal. Obviously that isn't going to be possible. What is possible is for her to push back retirement to age 75 and save about $10,000 per year until then. Her goal retirement age of 65 is not going to be a possibility.

This is a start on the road to financial peace, steering clear of financial mistakes. Learning more about the different ways investment mistakes can hurt you in the long run is the first step in avoiding future problems. Next is to not make or stop making those mistakes. It may take some time to change your habits and actions, but it will pay well in the long run if you do.