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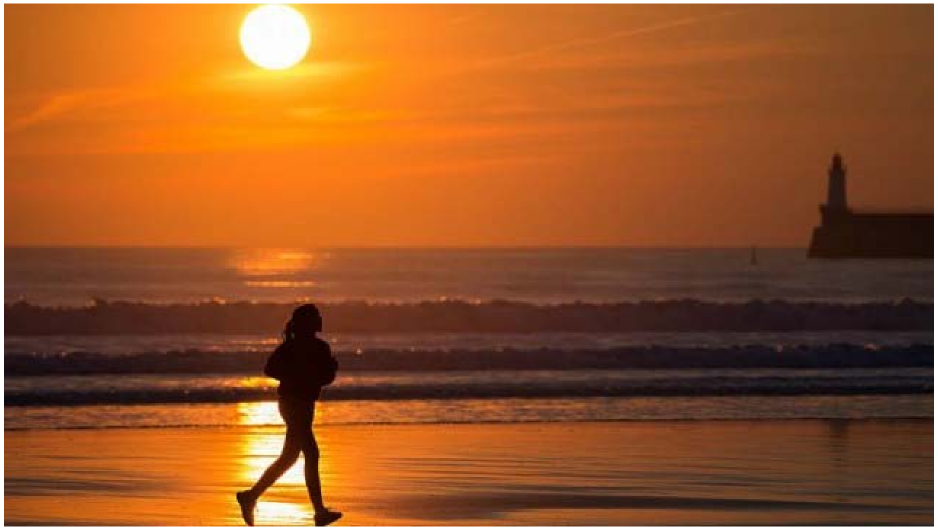
Why millennials should be thinking about retirement today

BY LISA OSOFSKY, OPINION CONTRIBUTOR - 02/05/17 12:00 PM EST



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Realtors say there are three factors that affect property value: location, location, location. My message to young Americans building their retirement savings: compounding, compounding, compounding!

They should use the power of compounding to their advantage and think about how they can save in today's uncertain environment in order to create a stable tomorrow, utilizing tax-favored strategies to help them get there.

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Retirement planning has always been a key area of wealth management, and it requires a holistic approach connecting it to cash flow, investment allocations, estate strategies, and insurance protection—all with the goal of ensuring someone's financial house is in order.

I frequently analogize wealth management to a house, where all these planning areas are under one roof, but at different points in your life, you spend more time in one room than another. Many young Americans don't spend enough time in the retirement planning room, since it appears too far into the future to be relevant. That is far from the truth.

Because of the power of compounding over time, even small amounts saved in someone's early years can lead to material amounts accumulated when they reach retirement. The growth on the saved amounts combined with the growth on the growth, month after month, is where the compounding really makes an impact.

For example, if a working 25-year-old were to contribute just $50 per month into a 401(k) plan until age 60, assuming a 5 percent average return, they would accumulate $57,000. If they can stretch that savings to $100 per month, it turns into $114,000.

Compare that to waiting until they're 35 to start the same savings plan. The $50 per month savings only grows to $30,000 and the $100 grows to $60,000. By starting 10 years earlier, they'd have almost twice as much saved.

There needs to be a shift in mindset, particularly among millennials. A survey of 1,900 Americans ages 18 to 35 revealed that this generation of young people spends more on coffee than retirement savings.

It also comes down to prioritizing. Many people compute their available savings by looking at their take home pay, subtracting their fixed expenses, backing out some discretionary spending for entertainment and vacations, and then whatever is left is set aside for savings. That usually equates to little or none.

How about this approach? First set aside a fixed amount for savings each month and then back out your fixed and discretionary spending. Pay for the future first.

The most common way to save for the future is through a 401(k) plan for

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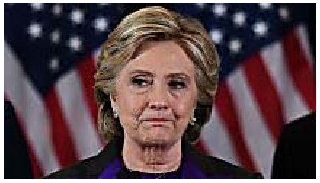

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employees, or an an individual retirement account (IRA) or other type of self-employed plan for freelance workers. These are excellent tools to save for retirement, since monies invested in them grow tax-deferred, so the power of compounding is not reduced by taxes on the earnings each year. The Roth version of these plans, if someone qualifies, is generally even better since the earnings grow tax-free, not just tax-deferred, and may never be taxed.

Many employers now offer automatic enrollment in a 401(k) plan where an employee has to elect-out if they don't want to participate. It essentially forces young Americans to save for their retirement.

The Plan Sponsor Council of America recently released its 59th annual survey of profit sharing and 401(k) plans, and respondents reported that nearly 60 percent of plans now have an automatic enrollment feature. In addition, many employers provide a matching contribution into the 401(k), so that puts even more money in the plan for compounding.

Unlike their grandparents, young Americans today rarely see employer-funded pension plans, so the bulk of the responsibility for setting money aside and paying for their future first is in their hands. According to a recent poll, 48 percent of all Americans aged 18 to 30 have zero in retirement savings and no access to a traditional pension.

We can change this statistic. The opportunity to save for retirement is there for the taking, but young Americans need to better understand how their money can compound over time, how they can set aside savings first before spending, and how participating in their 401(k) plan can help them build a war chest toward retirement.

It may seem too far away to care, but if they can start early and use that long time horizon to their advantage, they can enjoy their later years and look forward to when they retire, retire, retire.

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The views of contributors are their own and are not the views of The Hill.

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