

FINANCIAL PLANNING

Personal Finance Education from LPL Financial



Aim for Your Best Financial Life With a Plan

Steps to take in your 20s and 30s

POPE
Financial Planning



There's no better time to start pursuing your financial goals than right now. The earlier you start, the more time you have to work toward them. It's easier to manage your money and make progress toward your goals when you have a strategy. Financial planning can help you evaluate your unique money situations as they come up and make suitable decisions for your future.

It's Never Too Early to Develop Sound Financial Habits

Consider these facts and figures about the importance of financial planning for millennials¹:

- An estimated 3.75 million millennials owe on average \$20,000 to \$40,000 in student loan debt.
- Millennials have accumulated 34% less wealth compared to previous generations.
- Homeownership rates among millennials lag behind Gen X and Baby Boomers; roughly one-fourth of millennials believe they'll be "forever renters."
- Less than half of millennials believe they're on track to hit their retirement savings goals.

When you add in economic factors like high inflation and rising interest rates, which can make obtaining a mortgage more expensive, the financial challenges many millennials face to get ahead become even more ... well, challenging.

This overview will help you become familiar with the basics of financial planning and start taking control of your financial future. It offers you ways to improve your financial life, whether it's through budgeting, debt management, investing, retirement planning, or some other aspect of managing your financial life. And as you move ahead on the path to financial wellness, remember your LPL financial professional is always available to help.

Enjoy the journey!

1. SmartAsset "5 Financial Planning Tips for Millennials," April 12, 2023

Establish a Budget and Stick With It

During this time in your life, you're likely busy establishing yourself in your job or career, building new relationships, enjoying activities with friends and family, and generally figuring out how to navigate through new challenges and opportunities. There never seems to be enough time to focus on your financial life. However, a budget can help you achieve true financial wellness. The following 5-step process can help you create a budget that helps you work toward your financial goals.

1. Define your goals

Financial goals should be both short-term and long-term. Here are some examples of short-term goals:

- Save for a vacation
- Purchase the latest Apple Watch
- Upgrade your furniture
- Save for a wedding
- Start an emergency fund

Here are some examples of long-term goals:

- Buy a home (if you're renting)
- Pay off student loan debt
- Buy a franchise/start a business
- Build an emergency fund to cover three to six months of living expenses
- Retire early (or just start saving for retirement)

Make your goals measurable

Write down your financial goals and make sure they're measurable (include the actual dollar amounts and time frames for reaching the goals). Here are some examples of measurable financial goals:

- Build up a \$1,000 emergency fund in 10 months.
- Pay off \$3,000 credit card balance in 18 months.
- Contribute 8% to company retirement plan.
- Increase retirement contributions every January 1st by 1%.

If your goal is to build up a \$1,000 emergency fund in 10 months, your monthly goal is \$1,000 divided by 10, which equals a \$100 monthly contribution to the fund.

2. Know your income

Before you can establish a budget, you have to know exactly how much money you have coming in every month from your employer and other sources. Make sure to include only the money you actually receive (the exact amount of your net pay, not your gross pay before taxes and other deductions).

3. Total Your Monthly Expenses

You can't budget until you know how much money you're spending each month. When figuring out your monthly expense number, be sure to include the following:

- Groceries
- Student loan payment
- Credit card payment
- Cable/Wi-Fi/streaming apps
- Rent
- Car loan payment
- Cell phone plan
- Entertainment/eating out

Also remember to include expenses like doctor and dentist visits, insurance payments, haircuts, gifts, manicures and/or pedicures, and others. It's easier if you look at past bank and credit card statements to get a realistic picture of your spending.



4. Create a realistic budget

To take your first stab at a budget, add your monthly expenses from step 3 to the monthly goals you calculated in step 1. Then, subtract that total from your monthly income calculated in step 2. If the balance is positive, you've created a budget that works for your current lifestyle. Here's an example:

Monthly income (from Step 2)	\$3,750
Monthly living expenses (from Step 3).....	(\$2,900)
Monthly financial goals (from Step 1).....	(\$ 700)
<hr/>	
Total left over	\$ 150

If the balance is negative, you have some more work to do. That leads us to Step 5.

5. Revisit your goals and expenses

If the first swipe at your budget came out negative, rework the numbers and try again. For example, you can revisit expenses and decide which ones are top priority and need to stay in your budget and which you can do without. Are there apps you don't use or movie channels you don't watch? Also consider changing the amount of time needed to meet your financial goals. Or you can figure out a way to increase your income.

Thinking about your goals can give perspective on how to approach financial planning. Once you have the bigger picture sketched out, you can fine tune the details of your action plan to work toward your goals.



Tactical tip

Set aside enough money in an emergency fund to cover an unexpected expense.

For example, your budget might be doing fine for several months before you suddenly need a \$750 car repair. It can be hard to get back on track once the emergency is over.

Keep in mind that emergency savings are just that – money to use for an emergency. It's critical to avoid using a credit card when an actual emergency comes up (and then have to pay interest when carrying a credit card balance). Use the emergency funds and then start to rebuild those funds again – that's what they're for!

Manage Credit Cards Wisely

Without a doubt, credit cards make life more convenient, but not necessarily easier – this is often your most expensive debt! If you use them too much, they can become the biggest obstacle to reaching your financial goals. When using credit cards, consider these valuable tips:



5 good habits to develop

1. Review your credit card statements regularly to keep your purchases in check
2. Pay your bill on time to avoid late fee charges
3. Pay off your full balance every month to avoid paying interest
4. Take advantage of rewards programs
5. Protect yourself against credit card fraud by putting a freeze on your credit bureau records



6 bad habits to avoid

1. Using a card to make ends meet
2. Using several cards at a time
3. Not researching other options before applying
4. Exceeding 25% of your credit line
5. Using rewards programs as an excuse to buy more stuff
6. Making large purchases unless you can pay off the balance quickly



Tactical tip

Many people carry balances on their credit card – many on more than one card. When that happens, it can feel almost impossible to pay it off. Where do you start? There are a couple of strategies to consider.

Snowball method

It's called the snowball method because your payoffs start small but get bigger over time. Pay off your smallest balance first. When it gets paid off, the next smallest debt becomes your focus, until you are credit card debt free. For many people, the satisfaction of seeing that first debt get paid off quickly makes the snowball method the best choice.

Avalanche method

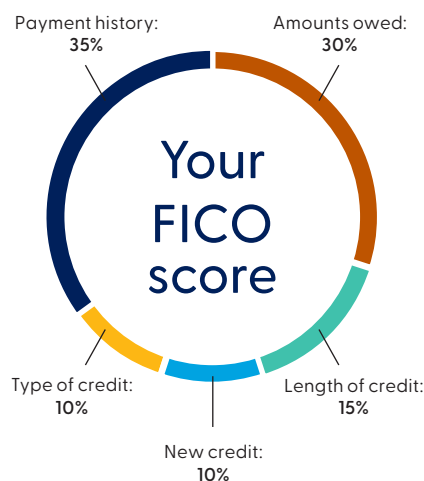
This is called the avalanche method because you are paying off the most expensive debt first – the debt with the highest interest rate. To use this payoff method, list all your debts in order of interest rate, from highest to lowest. The card with the highest rate on your list is the one to focus on first. When it gets paid off, move on to the debt with the second highest rate until you have zero credit card debt.

Maintain a Favorable Credit History

Your 3-digit “FICO” credit score is one of most important measures of your financial wellness. But what determines your score and how can you improve it? Your score is commonly used by creditors to determine your overall credit risk when you apply for a loan. Potential employers and landlords also often check your score.

The top three credit bureaus in the U.S. (Experian, TransUnion, and Equifax) calculate your FICO score. The better your credit score, the more likely you are to have your loan approved and receive lower interest rates. Generally, lenders regard scores of 670 and above as good credit risks.

To create your credit score, FICO looks at these five factors and weighs them by a certain percentage. If you're trying to improve your FICO score, focus on one or more of these areas:



5 factors contributing to your FICO score

Payment history: 35%

This component of your FICO score is the most heavily weighted. The best way to manage it is simple – pay your bills on time and get current on any past due accounts. If you can't, don't hesitate to talk to your lender and work something out.

Amounts owed: 30%

Since this component is also highly weighted, it's important to keep your credit card balances low as a percentage of your credit limit. Generally speaking, a balance of 30% or lower is considered best. For a card with a \$10,000 limit, make sure any balance you have is no more than \$3,000.

Length of credit: 15%

The longer your track record of maintaining good credit and paying back loans and credit cards on time, the better. If you are younger, start building credit as soon as possible. Consider keeping current accounts open – even if you currently have a zero balance.

New credit: 10%

You should avoid opening too many new accounts to take advantage of special offers such as airline miles or cashbacks on purchases. Having too much credit capacity can actually make you more of a credit risk.

Type of credit: 10%

Managing a variety of loan types can get you a higher FICO score. Lenders will consider you an experienced borrower if you have, for example, a mortgage, a car loan, a couple credit cards and a student loan. If all you have is credit card debt, you will be considered inexperienced and score lower.



Tactical tip

One way to make sure your payments are on time is to set up automatic payments, or set up electronic reminders. If you've missed payments, get current and stay current! To learn more about how to improve your FICO score, go to myFICO.com.

Become an Investor

One of the biggest opportunities you have to build personal wealth and financial wellness is through investing. But how do you know you're ready to take the plunge? Since investing always includes some risk, it's important to have a solid financial foundation before you begin. Here are some key things to make sure you have covered to make sure you're ready.

- You have a steady income (sounds obvious, but it's important)
- You've built up your savings, including a 3-6 month emergency fund, before establishing an investment account
- You have money left over after meeting your financial obligations
- You've considered the effect of upcoming personal changes, such as marriage, children, or divorce, before investing

Investing and your financial goals

No matter what your financial goals may be, here's a quick look at the key types of investments available to help you achieve them.

Stocks

A stock (also known as "equity") is a type of security that signifies an ownership in the issuing corporation. This entitles the stockholder to that proportion of the corporation's assets and earnings. Stocks are bought and sold predominantly on stock exchanges and are the foundation of nearly every portfolio.

Stocks (and stock mutual funds and electronically traded funds, called ETFs) have a high return potential, but the potential risk can be high. They are typically considered as part of a long term financial goal, like retirement, where you have time on your side and can afford to be more aggressive and take more risk. They usually do not make sense for funding a short-term financial goal where safety and stability are more of a priority.

Cash equivalents

Cash equivalent investments are typically money market funds and can include U.S. Treasury Bills. They're known for consistent, lower returns with much lower risk that may make more sense for a shorter term financial goal such as saving for a wedding or vacations. As you get closer to retirement (generally within 5-10 years), cash equivalents may also become a bigger part of your retirement account portfolio if you are seeking much more safety at this life stage.

Bonds

Bonds are used by companies, municipalities, states, and sovereign governments to finance projects and operations. Owners of bonds are debtholders, or creditors, of the issuer. Bond details include the end date when the principal of the loan is due to be paid to the bond owner and usually includes the terms for interest payments made by the borrower.

Bonds (and bond mutual funds) may work best for funding a medium term financial goal (such as a down payment on a new home, a remodeling project, or having a child) where you can take on some risk, but less than stocks. In addition, as you get closer to retirement (within 10 years in general), bonds and bond funds may also become a bigger part of your retirement account portfolio if you are looking to reduce risk but still want some growth potential.

Diversify your investments

By diversifying your investments, you are managing the risk you will incur since you're not putting all your eggs in one basket. Different investments have different risks involved with them. For example, stock or bond mutual funds may be considered riskier than putting your money in a money market fund. However, mutual funds generally have higher return potential. By diversifying your portfolio, you can seek to reduce the amount of risk you are exposed to while increasing your potential returns.

Need help getting started?

Professional help is available if and when you need it. LPL Financial services professionals can give you hands-on personal guidance to help you determine your retirement goals and how you can work toward them. They can:

- Help you understand different types of investments and their place in a balanced investment portfolio.
- Discuss professionally managed investment strategies that may be of interest to you.
- Meet with you on a regular basis to track progress and adjust as necessary.
- Help you determine your financial goals, such as retirement, buying a home, funding a college education, starting your own business, or just getting better at budgeting and paying down credit card debt.
- Help you determine an appropriate investment strategy for your financial goals, based on your risk tolerance and timeframe.

Learning resources

Becoming an investor means making a commitment to increase your knowledge by subscribing to daily financial news reports such as the Wall Street Journal app (www.wsj.com), among many others available. You can also ask your LPL Financial services professional to sign you up to receive the LPL Research Weekly Insights report.



Tactical tip

It pays to start investing as early as you can!

The younger you are when you start investing, the more time you have to benefit from what is known as compounding. Compounding happens when your money – your initial investment – starts earning interest, dividends, and/or capital gains (when stock or mutual fund prices go up). Those earnings get added to your initial investment, and start earning interest, too. So now you're earning interest on interest – that's compounding.

Here's a hypothetical example: Let's say you start with \$1,000 in an investment account, and it earns \$100 in the first year. The next year, you earn interest on \$1,100 (your original \$1,000 plus the first \$100 it earned), and end the year with \$1,210 (\$1,100 + \$110 more interest earned) ... and that just keeps going.

Take Full Advantage of Your Workplace Retirement Plan

One of the easiest ways to become an investor is by participating in your employer's workplace retirement plan, if there is one. For most people, there may not be a better opportunity to pursue financial wellness than this.

Automatic savings

With a plan such as a 401(k), you pay yourself first – a core financial principal. Money is deposited from your pay to your account without you even having to think about it. It doesn't get much easier than that.

Tax savings

The amount you contribute to your retirement account reduces your taxable income, which lowers your tax bill. Let's take an example of a worker earning \$50,000, who is in the 22% tax bracket and saves \$5,000 in their retirement account each year (10% of salary). They are reducing their tax bill by \$1,100 each year ($\$5,000 \times .22$). Income tax won't be due on this money until it is withdrawn from the account.

Tax-deferred compounding

There's that word again: compounding. As your retirement account grows, you pay no taxes on any earnings until you begin to withdraw your money at retirement. Compared to taxable savings accounts, investments with earnings that are tax-deferred have the potential to grow even faster when they are not being reduced by taxes each year.

Free money from the employer match

If you can't max out your workplace retirement plan, you should try to save enough to get the full employer match (subject to your plan's vesting rules). A common employer match of 50 cents for each dollar you save in the plan up to 6% of pay is a 50% return on your investment. A dollar-for-dollar 401(k) match doubles your money. That's a pretty excellent return!

Your money goes where you go

If you leave your employer for any reason, you can take your vested balance and roll it into an IRA or a new employer's plan (if allowed). Other options include leaving your money in the 401(k) if allowed, or taking a cash distribution, which is a taxable event and may be subject to penalties if you are younger than 59½.

Account management made easy

Your plan's recordkeeper provides you with comprehensive account access where you can view your balance, perform transactions, and talk to a call center representative for guidance. On top of that, you can view retirement planning education materials and calculators, and likely even model various saving scenarios and assumptions to help gauge your progress toward retirement readiness.

Traditional or Roth savings option?

Your retirement accounts have unique tax implications. A traditional 401(k) uses pre-tax dollars, lowering your tax burden while you work. However, you'll pay income taxes when you withdraw money from your account during retirement. On the other hand, a Roth 401(k) contribution comes from money you have earned that has already been taxed. You'll pay zero taxes on qualified withdrawals from this account when you're retired.

In general, a Roth option may be a more favorable savings strategy for younger adults. At this stage in your career, you're likely earning less today than you will in the future (there is an income cap for Roth accounts above which you can't contribute). That means you're in a lower tax bracket and paying lower taxes now. Of course, no one knows what the tax brackets will be in the future, so you could decide to diversify your contributions evenly between traditional and Roth (many employers offer this option to their employees). Depending on your circumstances, you can always decide to go heavier toward one option versus the other in the future.

About target date funds

Your workplace retirement plan offers a number of appropriate investment options to choose from. That usually includes individual mutual funds representing all the major asset classes, as well as pre-mixed portfolios that you can match up with your own personal tolerance for risk and timeline to retirement. Another option likely available to you is a target date fund. A target date fund is a mutual fund that invests with the assumption that investors will need to start withdrawing money from the fund at a specified time in the future. A professional fund manager monitors the fund and makes adjustments to the underlying investments as needed for the time frame.

The primary feature of a target date fund is that the fund adjusts its risk level over time. When the target date is still far away (2055, for example), target date funds invest more of their total assets in higher-risk investments like stocks, with little or no exposure to more conservative investments. As the target date approaches, the fund gradually shifts its asset allocation away from stocks and other risky assets in favor of bonds and other conservative, income-producing investments.

Each target date fund has a unique glide path, which describes how the asset mix in the fund changes over time. Some have what are called “to” glide paths, which means the fund will reach its most conservative asset mix right when it arrives at (or gets “to”) the target date. At that time these funds will typically be invested primarily in investments like bonds and money market funds. There are also target date funds that follow a “through” glide path approach, which means they will continue to pursue some level of exposure to stocks and riskier investments beyond (or “through”) the target date. Target date funds that have a “to” glide path approach are generally more conservative than those with a “through” glide path.

IRAs: A retirement plan option if you're self-employed

An individual retirement account (IRA), traditional or Roth, is a tax-deferred retirement savings account typically established by someone who is self-employed and doesn't have access to a workplace retirement plan like a 401(k). IRA accounts are held by custodians, such as banks or brokerages. Unlike 401(k)s, IRAs allow account holders to choose from a much larger universe of choices that include stocks, mutual funds, ETF funds, bonds, treasury bills, and certificates of deposit (CDs).

Like 401(k)s, contributions to traditional IRAs are generally tax deductible. Any earnings and returns are tax-deferred and you pay tax on qualified withdrawals in retirement.

Contributions to a Roth IRA are made with after-tax dollars, and qualified withdrawals are tax-free in retirement. The annual contribution limit for traditional and Roth IRAs changes every year.



Tactical tip

Your LPL financial professional can help you determine your retirement saving goals and how you can confidently pursue them. That includes helping you decide between a Roth and traditional contribution, creating and monitoring your investment strategy, and balancing your retirement savings goal with other financial goals.

Investing in mutual funds involves risk, including possible loss of principal. Fund value will fluctuate with market conditions and it may not achieve its investment objective.

Some Final Moves to Keep in Mind

Here are some additional components of financial planning to keep in mind to help you achieve financial wellness.

Execute essential legal documents

Having a plan for the unexpected will reduce stress and expensive repercussions during potential emergencies. Consider having the following legal documents drafted and executed by an attorney, so a trusted person can step in to assist in case of incapacity or early death:

Will

Outlines how property should be divided at your death and designates a person to handle the details; without one, courts will make decisions according to state law and not your wishes.

Living will (aka advanced directive)

Outlines preferences for treatment if you face a serious medical situation and need machines to help you stay alive.

Medical/health care power of attorney

Often part of a living will, it designates a person to make medical decisions for you if you are incapacitated.

Durable financial power of attorney

Designates a person to make financial decisions on your behalf if you are unable to do so at some point in time.

Review insurance coverage

Life insurance

In general, life insurance gets more expensive with age. Term insurance for a young, healthy person is relatively inexpensive and a good idea if you have debts that will need to be paid if you die unexpectedly or if you have a family to provide for.

Disability insurance

Your employer may offer disability insurance, which comes in handy if you get ill or injured and cannot work.

Property and casualty insurance

It's a good idea for younger adults to consider talking with an insurance professional to help them decide on the most effective car insurance coverage as well as whether an umbrella policy is needed. Renters should also purchase renter's insurance, as it can limit your liability if someone sues due to a personal injury or damaged property.

Consider partnering with a financial advisor or planner

Taking control of your finances is a big undertaking. Luckily, financial planners can help you develop a plan tailored to your unique circumstances. In addition, their knowledge and expertise can fill in gaps in your understanding.

You'll want to find out how they charge for their services before committing to one. Financial advisors and planners can charge in multiple ways. For example, some advisors charge per hour or have a fixed fee based on a specific service they are performing for you. Others charge a percentage of the assets they manage.

At this stage of life, you may not have a need for a comprehensive financial plan. Many planners offer customized services based on a specific need, such as reviewing your 401(k) plan and making investment allocation recommendations, or helping you create a cash flow management plan.

About LPL Financial

LPL Financial Holdings Inc. (Nasdaq: LPLA) is among the fastest growing wealth management firms in the U.S. As a leader in the financial advisor-mediated marketplace, LPL supports more than 28,000 financial advisors and the wealth management practices of 1,000 financial institutions, servicing and custodialing approximately \$1.6 trillion in brokerage and advisory assets on behalf of 8 million Americans. The firm provides a wide range of advisor affiliation models, investment solutions, fintech tools and practice management services, ensuring that advisors and institutions have the flexibility to choose the business model, services, and technology resources they need to run thriving businesses. For further information about LPL, please visit www.lplfinancial.com.

Sources: Investopedia; Smart Asset; Kiplinger; IRS.gov; Myfico.com.

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