Strategies For Wealth Building

For many people who are struggling from month to month financially, even the term “wealth building” seems alien. Yet when people spend less than they receive and make good decisions, they can, slowly over time, build up the value of what they own.

Wealth building is good for individuals, families and society because it improves people’s quality of life. Whatever goods and services you would like for yourself, your family or nation - better housing, higher quality medical care or anything else - they can be more nearly within reach if you engage effectively in wealth building.

The Three Rules

Many people act as if wealth building were very complex. In fact, an effective approach to wealth building can be summarized in three rules:

1. Start early.
2. Buy and hold.
3. Diversify.

Case Study: Charlayne, the Accidental Millionaire.

When Charlayne was getting started in her first job, she didn’t use any of her pay to play the lottery or head for the casino along with all her friends. “Come on,” they said. “It’s the only way you’ll ever be a millionaire.” She took note of the “Who Wants to Be a Millionaire?” show on television. But she was pretty sure she would never become a millionaire by hitting the lottery or answering game-show questions. Yet Charlayne became a millionaire. How?

Charlayne made an important decision when she began to work. With advice from the company’s benefits manager, she decided to have $20 withheld from each weekly paycheck and put into a mutual fund account. That wasn’t easy to do. Charlayne had many possible uses for an extra $20 each week. But the benefits manager persuaded her that putting $20 aside each week would be the best thing to do for her future.

Charlayne’s company matched the $20 deposit she made each week. This meant an immediate doubling of Charlayne’s weekly savings.

Over time, Charlayne didn’t exactly forget about her account, but she didn’t always monitor it closely. As printed statements arrived in the mail, generally showing that the value of her account was increasing, Charlayne became increasingly comfortable about her retirement plan.

There were times when Charlayne really would have liked to have the money she was saving. But she never considered trying to take her money out of the retirement account. Somehow she found a way to scrape through when there was a financial crisis.

When Charlayne retired, it became clear that her sustained program of investment had served her well. She had become a millionaire. Her retirement account was worth more than a million dollars. Steady payments from that account enabled Charlayne to travel and visit her grandchildren, go to movies or concerts when she wanted to, and live in comfort. She was even able to help with college expenses for next-generation members of her family.

Most people are skeptical when they’re told that matched weekly contributions of $20 could make them millionaires – but the math works. The chart on the next page shows how the money kept growing, in this case, until Charlayne became a millionaire. This example assumes an average return of 8.5 percent each year, calculated on the average yearly balance and compounded once per year.

Chart: Charlayne Becomes a Millionaire – Accidentally

Year	Beginning Balance	Addition to Principal	Return	Ending Balance
0	$0.00	$2,080.00	$88.40	$2,168.40
1	$2,168.40	$2,080.00	$272.71	$4,521.11
2	$4,521.11	$2,080.00	$472.69	$7,073.81
3	$7,073.81	$2,080.00	$689.67	$9,843.48
4	$9,843.48	$2,080.00	$925.10	$12,848.58
5	$12,848.58	$2,080.00	$1,180.53	$16,109.11
6	$16,109.11	$2,080.00	$1,457.67	$19,646.78
7	$19,646.78	$2,080.00	$1,758.38	$23,485.16
8	$23,485.16	$2,080.00	$2,084.64	$27,649.80
9	$27,649.80	$2,080.00	$2,438.63	$32,168.43
10	$32,168.43	$2,080.00	$2,822.72	$37,071.15
11	$37,071.15	$2,080.00	$3,239.45	$42,390.59
12	$42,390.59	$2,080.00	$3,691.60	$48,162.19
13	$48,162.19	$2,080.00	$4,182.19	$54,424.38
14	$54,424.38	$2,080.00	$4,714.47	$61,218.85
15	$61,218.85	$2,080.00	$5,292.00	$68,590.85
16	$68,590.85	$2,080.00	$5,918.62	$76,589.48
17	$76,589.48	$2,080.00	$6,598.51	$85,267.98
18	$85,267.98	$2,080.00	$7,336.18	$94,684.16
19	$94,684.16	$2,080.00	$8,136.55	$104,900.72
20	$104,900.72	$2,080.00	$9,004.96	$115,985.68
21	$115,985.68	$2,080.00	$9,947.18	$128,012.86
22	$128,012.86	$2,080.00	$10,969.49	$141,062.35
23	$141,062.35	$2,080.00	$12,078.70	$155,221.05
24	$155,221.05	$2,080.00	$13,282.19	$170,583.24
25	$170,583.24	$2,080.00	$14,587.98	$187,251.22

Year	Beginning Balance	Addition to Principal	Return	Ending Balance
26	$187,251.22	$2,080.00	$16,004.75	$205,335.97
27	$205,335.97	$2,080.00	$17,541.96	$224,957.93
28	$224,957.93	$2,080.00	19,209.82	$246,247.75
29	$246,247.75	$2,080.00	$21,019.46	$269,347.21
30	$269,347.21	$2,080.00	$22,982.91	$294,410.12
31	$294,410.12	$2,080.00	$25,113.26	$321,603.38
32	$321,603.38	$2,080.00	$27,424.69	$351,108.07
33	$351,108.07	$2,080.00	$29,932.59	$383,120.66
34	$383,120.66	$2,080.00	$32,653.66	$417,854.31
35	$417,854.31	$2,080.00	$35,606.02	$455,540.33
36	$455,540.33	$2,080.00	$38,809.33	$496,429.66
37	$496,429.66	$2,080.00	$42,284.92	$540,794.58
38	$540,794.58	$2,080.00	$46,055.94	$588,930.52
39	$588,930.52	$2,080.00	$50,147.49	$641,158.01
40	$641,158.01	$2,080.00	$54,586.83	$697,824.84
41	$697,824.84	$2,080.00	$59,403.51	$759,308.35
42	$759,308.35	$2,080.00	$64,629.61	$826,017.96
43	$826,017.96	$2,080.00	$70,299.93	$898,397.89
44	$898,397.89	$2,080.00	$76,452.22	$976,930.11
45	$976,930.11	$2,080.00	$83,127.46	$1,062,137.57

Call Charlayne lucky if you want to, but most people could do what she did. In getting her lifetime net wealth to $1 million by age 65, she followed the three rules:

1. **Start early.** Charlayne began saving when she turned 20, so she had 45 years in which her savings could grow.

2. **Buy and hold.** Charlayne bought a tiny bit more in financial assets each payday with the small amount withheld from her pay. She never touched that account as it grew over the years. Most importantly, she did not withdraw her money and spend it even when times were tough.

3. **Diversify.** Charlayne's retirement account was invested in a broad variety of financial assets. It wasn't put into any one asset.

And that is how Charlayne became a millionaire. Let's look at the three rules she followed in more detail.

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Rule 1: The Importance of an Early Start

Rule 1 says "Start early." Money that's saved early so that it can work for a long time has a great deal of importance in overall wealth building. An early start works well because of the magic of compounding.

When you save money, you receive a return. In the case of bank accounts, that return is called interest. If you leave the interest in the account, that money also earns interest. In other words, you earn interest on interest. The longer this process goes on, the more it works for you.

Here is a different example that also shows the importance of an early start: Charlayne had a co-worker who didn't start early. Instead of starting to save at the beginning of his career, Marcus held off for 10 years. Then, like Charlayne, he saved $20 per week, and his company matched these deposits for the next 35 years. Marcus accumulated about $400,000 by saving as he did.

That's a lot of money. But because Charlayne started early, she became a millionaire and Marcus did not. This example shows how you need to get an early start in order to build significant wealth in a lifetime.

But even if you don't get an early start, then (like Marcus) you can still take big steps toward wealth building. You just have to save more (or settle for less) than if you had gotten off to an early start.

Rule 2: Buy and Hold

The second rule is "Buy and hold." This means that to build wealth over time, you have to hold on to your long-term savings. You can't be dipping into them frequently, or they won't compound over time in the same way.

To buy and hold, you have to have your finances in order. Here are three steps to consider:

- **Spend less than you receive.** You do this either by earning more or spending less. You can help yourself to spend less by keeping track of where your money is going; then you cut back in places where you can save small amounts. You take the small amounts you're saving and get them our of sight so you won't be tempted to spend what's there.

- **Make intelligent choices about financial institutions.** Here the goal is to open and maintain accounts at mainstream financial institutions such as banks, credit unions and brokerages. Then you can accomplish savings and budgeting goals that simply wouldn't be possible if you were still operating on a cash basis.

- **Manage your credit properly.** When you're managing your credit properly, you're limiting the number of credit cards you have. You're limiting your purchases to what you can payoff each month, without leaving a balance to accumulate interest that you'll also have to pay. As time goes by, your credit score goes up, making it possible for you to borrow when you have a good reason to borrow.

If you're doing all this, you can buy and hold with confidence. Remember the case of Charlayne, the accidental millionaire? Surprisingly, one of the smartest things she did with her retirement account was to neglect it. She just kept having money taken our of her paycheck and put into financial assets, no matter what.

That meant that when her financial assets declined in value because of the normal ups and downs of the market, she didn't change her strategy. Financial assets were then, at down-market times, relatively cheap, and her regular contributions bought more than they bought when financial assets were more expensive.

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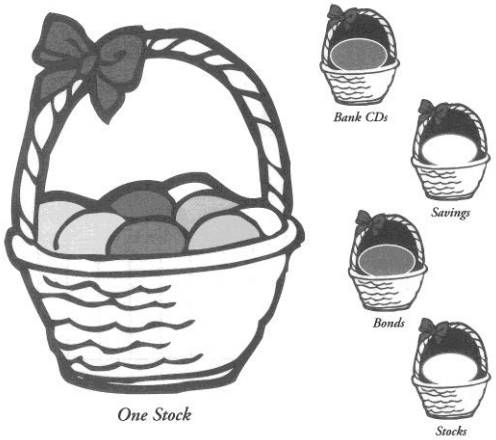
When financial markets went up, those inexpensively-bought financial assets became worth a whole lot more. Charlayne saw televised accounts of people who became rich overnight playing the stock market because the values of their financial assets had become so high. But she didn't think she could play that game, so she just left her retirement fund alone. She held onto it and kept most of the gains, though she was aware that markets were always going up and down.

Over time, Charlayne came out better than many people who worked much harder trying to make more. They tried to jump in and our of the markets with their retirement money. They tried to "buy low" and "sell high," but in the end didn't do as well as people like Charlayne who stuck with the dull rule, "buy and hold."

Rule 3: Diversify

Somebody probably once told you, "Don't put all your eggs in one basket." This saying hearkens back to the time when knocking over a single basket might wipe out a week's supply of eggs from the henhouse if you had put all the eggs in one basket (see Figure 3).

Don't Put All Your Eggs in One Basket



To diversify is to take on many small risks rather than one large risk. If you put all of your savings into a new start-up toy company, you could get rich if the company succeeded. Or you could lose all your money if the company failed. That's like having all your eggs in one basket. The same point would apply if you were approached by someone proposing that you invest in a business opportunity. If you put all your savings there, you would again be putting your money at risk.

Any time you take one large risk with your money, you're not diversifying. That's dangerous. It's far safer to spread risks out. This means holding a variety of financial assets rather than just one.

Prepare a Post It Pad on the 3 Rules. You MUST have at least 2 questions that you can ask the other groups on the material that you presented.