"We Need to Talk": Getting an Early Jump on Saving

By Judith Ward, T. Rowe Price Senior Financial Planner

Talking to your kids about money is a good idea at any age. But the discussion may be a bit more important as they begin their careers. While spending may be far more attractive than saving for many young adults, they may surprise you by listening to some advice on money.

As a parent, your natural instinct is to want your children to realize their full potential with rewarding careers and financially stable lives. If you've regularly discussed financial matters freely as they were growing up, you have a head start on approaching them about saving for their financial future.

A good place to begin is to make sure they understand "interest on interest"—the benefit of compounding—and how starting early and adding to their investments regularly could significantly ramp up their savings. You'll also want them to understand that although the compounding increases are modest at first, over time they could dramatically accelerate wealth accumulation.

Retirement Planning

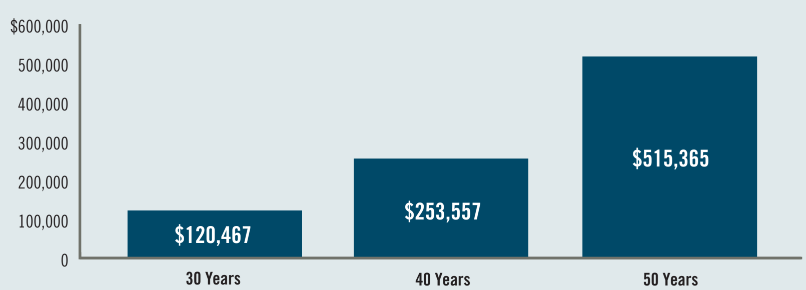
While getting a young adult to think about his retirement security may be a bit of a challenge, emphasize the benefits of opening a Roth IRA (individual retirement account) now—and how much money he could have when he retires. Contributions are made with after-tax income, and earnings are usually tax-free for withdrawals after age 59½. (See note below.)

If a young adult retiring in 40 years makes an initial contribution of $1,000 to a Roth IRA and adds $100 a month until retirement, he could have more than $250,000—all tax-free under certain conditions. (See chart this page.) That may get his attention!

You also could encourage your children by financially supporting their savings program—perhaps matching all or part of what they contribute—because they may not be enthusiastic about putting away some of their earnings for half a century or more. (However, the total amount invested in an IRA each year cannot exceed their earnings or that year's maximum contribution amount.)

Starting Small—Growing Big

Judith Ward, a T. Rowe Price senior financial planner, talks with her son, Justin, about how consistently saving over time can add up to a significant nest egg. For example, if a young adult makes an initial $1,000 contribution into a Roth IRA and adds $100 a month for 40 years, that could add up to more than $250,000—all tax-free.



Note: Chart is for illustrative purposes only and does not represent the performance of a specific security. It assumes an average annual return of 7%.

Video

My son and I talked about the value of saving early, and I suggested that my husband and I could help him get started. See "We Need to Talk," a video of this chat, at troweprice.com/startsaving.

Once a young adult understands how his money can grow, saving can be very exciting. It also can be a great way to begin his financial education. And chances are it will be rewarding for you as well, knowing that you can be giving your children a jump-start for their future.

Note: Withdrawals of Roth IRA contributions are always tax-free. After age 59½, Roth IRA withdrawals of earnings are tax-free if the account is five years old. Before age 59½, withdrawals of earnings are tax- and penalty-free if the account is five years old and the money is used for a first-time home purchase to a limit of $10,000.