Strategic Tips for Young Investors

If you're a young investor, long-term financial goals like saving for retirement may seem very distant. But even if you're at the onset of your career, it's important to begin saving for your financial goals as soon as possible. Here are some strategic tips from T. Rowe Price financial planners to help you get started.

Pay yourself first: Those who say they'll save or invest after taking care of other expenses often find that there's nothing left over. To make it easier to pay yourself first, enroll in your company's 401(k) plan or sign up for an "automatic asset builder" program in which money from your paycheck or bank account—often as little as $50 per month—can be automatically invested for you.

Start early: Due to the effects of compounding, starting early can have significant long-term benefits. For example, someone who saves $100 per month for 10 years in a tax-deferred account and then stops contributing would accumulate more by age 65 than someone who waits 10 years before starting, and then invests $100 per month for the subsequent 33 years. Of course, someone who saved $100 per month for the entire 43 years would do best, ending up with more than $329,000.

Look for free money: When evaluating job opportunities, check out the availability of a 401(k) plan, when you would be eligible to participate, and whether the company will match some of your contributions. The "free money" from a company match can make a significant contribution to your retirement nest egg.

Balance long- and short-term goals: Although thinking about a retirement that's 30 to 40 years away can be difficult when other needs seem more pressing, it's important to make saving for retirement an equal—if not more important—priority. Strive to save at least 10% to 15% of your income for retirement, with any additional savings earmarked for short-term goals such as a car, vacation, or house.

Saving for both long- and short-term goals means you'll have money for major expenditures, while also helping to ensure your financial future.

A T. Rowe Price analysis suggests that saving at least 15% of your salary each year for retirement as soon as you start working, and then maintaining at least that percentage throughout your career, can put you on a path toward a financially secure retirement.

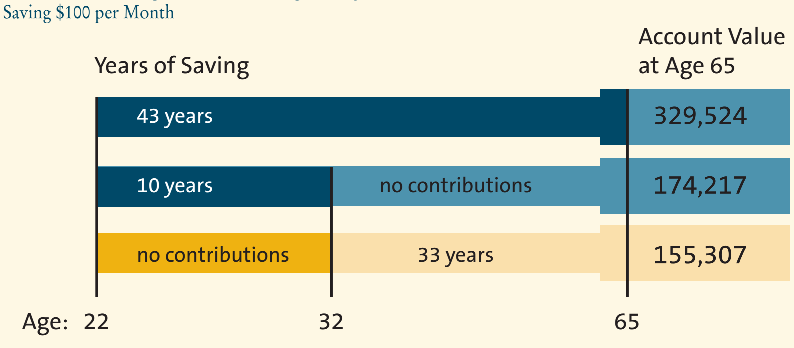
Consider IRA investments: For single tax filers with earned income of less than $122,000 for 2011 ($125,000 for 2012), investing in a Roth IRA can help you start building a retirement nest egg. The Roth IRA tends to be a better choice for younger investors than Traditional IRAs (whether deductible or nondeductible) because of how the tax benefit works.

With a Roth IRA, you receive no tax deduction on your contributions, but you pay no taxes (assuming certain conditions are met) on the much larger amount you are likely to have accumulated when you begin withdrawing from your Roth IRA decades from now. Since you could be in a higher tax bracket at retirement than you are early in your career, the tax-free withdrawals become that much more valuable.

With a nondeductible Traditional IRA, only the earnings in the account are taxed when withdrawn. With a deductible Traditional IRA, your contributions are tax-deductible in the year you make them, but then taxes must be paid on the assets at withdrawal. If you don't need tax benefits now, the potential for future tax-free withdrawals may make the Roth IRA the better choice.

Invest in equities for long-term growth potential: For your retirement portfolio, invest up to 90% in equities, assuming you can tolerate market downturns. Historically, investments in stocks have provided more long-term growth opportunities than bonds and short-term investments. Since younger investors have a longer period of time to overcome market setbacks, it is usually prudent for them to invest a significant portion of their portfolio in stocks. This percentage can be decreased as you get older.

The Advantage of Starting Early
Saving $100 per Month



Starting early is key to accumulating retirement savings. A 22 year old who invests $100 per month for 10 years and then stops investing could accumulate more than someone who delays saving for 10 years and then contributes until age 65, even though the investor who delayed contributed more than three times as much ($39,600) as the investor who started early and then stopped ($12,000). Of course, the investor who contributes for the full 43 years ends up with a significantly higher account value at retirement.

These amounts assume $100 invested each month in a tax-deferred account and an 7% annual rate of return.

Budget for unexpected expenses: To make sure you don't spend more than you earn, in addition to budgeting for fixed expenses (housing, utilities) and flexible expenses (restaurants, recreation), you also need to plan for unexpected expenses such as car repairs or health care costs. Often, those in financial trouble find that although they were not living beyond their means, they were unprepared for unexpected expenses. Suddenly they are overspending and must start borrowing.

Get the insurance you need: One way to protect yourself against very large unexpected expenses is to purchase insurance. While most people wouldn't think of going without car insurance, other types of insurance also provide a safety net and don't necessarily cost a lot. Renter's insurance provides liability coverage as well as protection for your possessions. Health insurance is also important, even if it's only a catastrophic policy to tide you over until you are eligible for an employer's group plan.

Pay off your credit cards: The ideal way to use credit cards is to pay them off, in full, every month. Credit cards are usually the most expensive source of borrowed money. The interest you pay on your credit card purchases can add significantly to the cost of an item—money that could be directed toward your retirement or other savings goals instead. Paying your credit card and other bills on time can eliminate penalty fees and also enhance your credit profile.