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July 2001 - A Thought for Young People

I hope each of you reading this consider yourself young!

There were once two young people, trying to furnish their homes, get appliances, a living room and dinette sets, a television, a sound system, and a computer. Alas, when each of them priced these items, they discovered that the total was ten thousand dollars. They anguished with the thought that there was no way they could pay such a sum in cash, and so surely they wouldn't be able afford these things that surely they needed?

The first young person went home and found an offer from a credit card company, guaranteeing him a card with a \$10,000 limit, with an initial interest rate of only 3.9% for the first six months, and then 21% as a permanent rate. Excited, he called his friend! Now for only \$310 each month he could have everything he needed – right now! In 48 months he would be paid in full. \$310 was a lot of money to commit to every month, but it was possible, and compared to the thought of living without these essentials, it was a wonderful opportunity!

His young friend came home to the same offer in her mailbox, but she did not get as excited about it. She had always been taught to avoid debt, and although it would be hard to do without these items for now, especially when her friend had them, she was committed. So instead, she shopped sales and second-hand stores and found bargains as she could pay cash for them. She did want to have nice, new items when she could pay for them, so she saved the same \$310 each month that her friend paid to the credit card company.

At the end of four years, the young man had paid his credit card debt and was pleased with his accomplishment. Unfortunately, the computer, sound system, and television were hopelessly out of date, and the other items were out of style. So he sold them at a yard sale for a few hundred dollars, which he spent on a short vacation that surely he had earned, and used his credit card to replace them with new items. He would just keep making the same payments and would have the pleasure of having new and up-to-date items in his home!

He called his lady friend to see if she was finally going to get some current stylish things for her home, and was pleased to learn that she was willing to go shopping with him. They both picked out items that again totaled \$10,000. He paid with his credit card, and was surprised when she paid cash! When he asked how she had possibly come in to such a large sum of money, she smiled and said she had paid herself \$310 each month for four years into a savings account that paid her 4% interest, and that this had now accumulated to over \$16,000! So she could pay the \$10,000 cash, and have \$6,000 left over to put into a Roth retirement account that would accumulate for her tax-free. She put the retirement money into investments that had an average return of a just over 8% each year.

Another eight years passed. Each person kept following the habits they had formed. The young man got new items every four years on credit, made his payments on time, and was out of debt and had no savings at the end of each four year period. The young lady made do with used items for the first four years, and bought the same new items as her friend with cash every four years from then on. She consistently saved the same \$310 each month her friend paid the credit card company and put it in a short-term savings account earning 4% per year. She had over \$6,000 to invest in retirement savings each four years over and above the \$10,000 she spent on furniture, appliances, and the like at the end of each of these four year periods.

At the end of these additional eight years, making a total of twelve years since the initial decisions, the young man was surprised to learn that his friend had already accumulated over \$25,000 in her retirement account! (So if you read this and want to start her plan now, you could have \$25,000 saved in only 12 years with this plan. Compare that to the amount you have saved in the last 12 years!)

When 20 years had passed from the initial decision, he was replacing his items for the fifth time and still had no savings, while she now had over \$60,000 in long-term savings and had bought \$10,000 of the items of her choice every 4 years in addition!

At 30 years, she had over \$150,000, and yes, he still had no savings. At 40 years, she had over \$350,000, and at 50 years, she had over \$770,000!

By official U. S. Government statistics, only 5% of Americans age 65 or better have total savings of \$1,000 or more. The other 95% are totally reliant on Social Security and whatever pension they might be entitled to. Many of them had changed jobs enough they had no pension.

The difference is this: The 5% collect interest, and the 95% pay it. Over a lifetime, that initial decision to pay cash can make a \$770,000 difference. And even if you have only 12 years left to retirement, this simple example could help you save \$25,000 you wouldn't have otherwise.

If you'd like detailed numbers to prove my story true, they're free for the asking!