10 Mistakes Nearly Everyone Makes When Trying to Get Financially Fit

By Jim Wang

WALLET HACKS

Welcome to the Wallet Hacks Family.

If you're reading this, you've already taken an important first step towards changing your relationship with money.

But it was just the first step and entering an email is just the beginning.

I've been writing about money for over ten years. I've been emailing and talking with folks like you for just as long. The difference between me and the other guys is that I'm not trying to sell you anything. I'm a regular person just like you … I'm just a few couple steps in front of you -- let me show you the way.

In order to change and make a better version of yourself, you'll need to **take action**. I'm willing to help you but I need you to take the next step.

Here's my pledge to you — if you're making one of these mistakes and you aren't quite sure how to fix it, **email me**.

I’ll work with you to get things fixed. I’m not a financial planner or adviser and I don’t give financial advice, I’m just a friend who has seen a lot of this stuff already and can offer some guidance and encouragement.

Mistakes are just opportunities to improve ourselves.

Let’s get started!

1. Not budgeting at all

Budgeting isn't fun but being broke is less fun.

If you aren't budgeting, then you don't know how much you're spending on what each month. You don't know if you're spending too much or spending too little.

Budgeting doesn't have to be a time consuming process.

There's one strategy that, if you use it, will get you 95% of the results with 5% of the effort — it's called Save First, Spend Second.

When you save first, you can spend all you want. Don't wait to spend your income and then save what's left, make saving the priority.

How do you do this? First, make any retirement savings you need directly from your paycheck. Your retirement savings comes first and by making it automatic and come directly from your paycheck, you prevent yourself from screwing it up. Contribute as much as you feel comfortable and at least enough to get any matching funds your employer offers.

Next, the balance will get deposited into your checking account after taxes are withheld and other payments are deducted. As it stands, your retirement savings are taken care of so you need to turn towards other savings needs. Transfer those funds out of your checking account to those savings goals – like a down payment on a house or new car.

If you have debts, those are goals too. Instead of, or in addition to, saving the money, use it to pay down those debts.

After that, the rest of the money left over is yours. Deduct your housing and other regular payments you might have and spend the rest on whatever you want. There's no need to track your spending because the whole point of tracking is to make sure you save money at the end. You've saved money in the beginning so your work is done.

Remember that the goal of budgeting is to make sure you are saving enough each month so you can achieve your goals. Whether it's retiring early, buying a house, or just living life to the fullest without worry; keeping an eye on your spending will get you there.

And when you have a budget, even a "good enough" one like paying yourself first, you ensure you're saving. That is no small thing. When you have your savings covered, you can spend money without regret.

That means no longer feeling guilty about that cup of coffee or that new piece of clothing. And no more worrying if last night out with your friends will broke your budget.

That is a freeing and healthy relationship with your money and it's achievable without spending hours tracking your spending.

2. Not planning for emergencies

Emergencies happen.

And usually at the worst times too.

Fortunately the fix is easy, it just takes time. You will need to establish and fund an emergency fund. In the event of an emergency, this fund will provide the cash you need to overcome that emergency. Whether it's something small, like a broken window, or something big, like job loss; an emergency fund steps in to shoulder the load.

But saving money is not enough.

You also need an emergency response plan for those potential emergencies.

An emergency response plan lists the steps you'll take when an emergency strikes. The goal is to separate the decision making from the stress of the emergency. If you're in a car accident, you'll be in shock and it'll be much harder to remember what to do. That's why insurance companies put a checklist on the back of your insurance card.

By having a checklist of steps, you separate the decision making from the stress. You don't make decisions under duress.

For example, let's say you own a house with a hot water heater that's 10 years old. Most hot water heaters have a useful life of 8-12 years before they fail. You know you're on borrowed time so as part of your emergency response plan you begin getting quotes for its replacement. When the water heater fails, you have a list of companies with relative recent pricing information. You can make an informed decision, not a panicked one because you had to schedule visits and get quotes while you and your kids take freezing cold showers.

The fund is most important, you can’t conjure money out of thin air, but the plan is equally important.

3. Not trying to eradicate debt

Many people do not take debt seriously. It doesn't matter if it's the commonly accepted "good" kind of a mortgage or the "evil" credit card kind.

Debt is a tax on your future.

It's a financial burden and a psychological one.

Some low interest rate debt, like a mortgage, can be managed if there are other qualitative and quantitative benefits. Carrying a large, low interest rate mortgage isn't financially pleasant but it's the cost of living in a home you call your own. It's less about the 4% and more about the ongoing payment, which is a tax on your future earnings.

As for high interest credit card debt, that's a debt you must eradicate. When you carry a balance on a credit card, everything becomes more expensive.

If you have a $5,000 credit card balance at 10% and you make a $100 payment each month (if the minimum payment is 2%), it will take you 65 months to pay it off and you'll have made nearly $1500 in interest payments. That's if you don't add any more to the balance.

You might think that an extra $1500 over 5.4 years isn't that bad, it's about $23 a month, but remember that *you are not getting anything for that money*. It's just interest.

Put that $1500 into retirement savings and, growing at a conservative 7%, it will become $5804 in 20 years. Would you rather have nearly six thousand dollars more in your savings or just give it away?

Double your monthly debt payment to just $200 and it'll take 29 months and only cost you $630. That's $865 in interest savings.

Pay $300 a month and it'll take only 19 months and cost you $406 — that's $1089 in interest savings.

If you need inspiration or ideas, check out my **Pinterest board loaded with stories of people paying off massive debts**.

4. Not saving for retirement

Can you guess the biggest problem with retirement savings?

People just aren't saving.

The **16th Annual Transamerica Retirement Survey** revealed that the median retirement savings among workers is just $63,000. While 22% have over $250,000 in retirement accounts, 23% have less than $25,000!

It's not asset allocation (though 20% of respondents didn't know what they were invested in).

It's not what account to invest in (though 30% had no idea what a Roth 401k was).

It's that people aren't saving enough.

If you aren't sure where to start, here's a quick lesson in how to save for retirement.

1. If your employer offers a 401(k) with a match, contribute as much as you need for the match funds.
2. If you don't have an **emergency fund**, start saving towards that.
3. If they don't, contribute to the maximum on a Roth IRA ($5,500 in 2015).
4. Next, contribute to your employer's 401(k) up to the maximum ($18,000 in 2015).
5. If you have a HSA (health savings account), contribute to that up to the maximum ($3,350 for singles, $6650 for families in 2015).
6. If you still have savings left over, big thumbs up to you because you'll have contributed over $23,500 to your retirement.

As for what to invest in, keep things simple. Start with a simple 120 minus age allocation for stocks. If you're 30 years old, that's 90% equities and 10% bonds. Buy inexpensive index funds from Vanguard and work on something else.

When you have time, you can start researching a different allocation but for now 120 minus age will get you where you need to go.

The only other thing to pay very close attention to is fees. You can't predict the performance of a fund but you can predict the fees and the more you pay, the less you keep. Index funds are notoriously cheap. The Vanguard 500 Index Fund (VFINX) has an expense ratio of just 0.17%. Most actively managed funds have expense ratios above 1%.

In a $100,000 portfolio over 20 years gaining 4% annually, an annual fee of 0.75% will cost you almost $30,000. But that's not the whole story. If you were able to invest those fees you paid, it would itself have earned an extra $12,000. (**see this SEC report on expenses and fees**)

As you go to review your investment options, keep a very close eye on the fees of the fund.

5. Focusing too much on small wins

Frugality gets a bad name because most people writing about it focus on tiny microscopic wins. That's what happens when you have so many people writing about it, no one talks about the common stuff and everyone starts focusing on squeezing out a few more cents from that tube of toothpaste.

But the small wins take a lot of time and aren't justifiable.

Instead, focus on big wins. There are a handful of things you should be spending your time on. If you get them right, you can skip every tiny win in the book. If you get them wrong, those tiny wins won't get you back in the black.

What are some big wins? Capital spending, such as buying a car or house, and capital income, like your career and your investments.

Let's take your career as an example… what's the equivalent of focusing on small wins? If there's more you can do to further your career, like taking classes or additional training, you should focus on those. Instead, what a lot of people try to do is try to find ways to earn supplemental income in the short term.

Taking a class or getting a certification won't increase your income immediately, but it has the potential to increase your value to your employer. You should be focusing on that, not on a side hustle that can earn you a few dollars… and I love side hustles. The risk of side hustles is that you take your eye off the long term.

There are exceptions to this — if there are no clear cut opportunities, then a side hustle makes sense. If you aren't in love with your career and are looking for another track, then working on a side hustle makes sense. If you're looking for extra short term income to save for a goal or pay down debt, then working on a side hustle makes sense.

But if you have the choice between working on your primary career or starting a side business from scratch, it’s often better to work on your career.

6. Spending too much time “investing”

There’s a natural compulsion to try to “beat the market.”

But **86% of active fund managers don’t beat their own benchmarks**.

If professionals can’t do it, how could you? What advantage do you have in the market? You don’t have an informational/news advantage, you don’t have an experience advantage, and you don’t have a cost advantage. It’ll be tough.

But I get it. You want to trade. You want to do the research, you want to pick the companies, and you want to try to beat the market. It’s totally natural.

If you have that itch, paper trade. If you do well for a year, carve out a little cash from your investments and scratch that itch.

If you learn you aren’t, put your investments in an asset allocation you feel comfortable with and spend all this extra leisure time you’ll have!

Oh and before we leave the idea of spending too much time on investing, Fidelity reviewed which investors did the best and the answer will surprise you… they were the ones who forgot they had an account at Fidelity. It’s an **anecdote** shared on Bloomberg Radio where Barry Ritholtz, of **The Big Picture**, spoke with James O’Shaughnessy of O’Shaughnessy Asset Management. O’Shaughnessy shared the story.

Fascinating huh?

7. Not estate planning

If you have no major fixed assets (like a house) and no dependents, estate planning isn't a priority. When you begin accumulating assets or get married, and especially if you have kids, estate planning is absolutely crucial.

Proper estate planning will ensure your wishes are executed and done so in a quick fashion. When you don't have a Will, things can drag on for a very long time and the state may make decisions you wouldn't agree with.

The bare minimum of estate planning includes a Last Will and Testament, Power of Attorney, and a Living Will. The Last Will and Testament is the all-encompassing document that explains your wishes, such as how your assets are distributed, who will execute it, where children go, etc. Power of Attorney gives someone the ability to act on your behalf and comes with a Health Care POA, for medical decisions, and a Financial POA, for financial decisions. Lastly, the Living Will, also known as a directive to physicians or health care directive, covers end of life medical care when you can't communicate your decisions.

Estate planning doesn't have to be expensive. Just as software has made tax preparation easier, software has made estate planning very straightforward for most scenarios. There's no reason not to have an estate plan.

8. Not having enough insurance

Insurance is one of those things we pay for and hope we never have to use.

Two insurances we often forget are disability insurance and life insurance.

Disability insurance is insurance for when something happens and you're unable to work. Its most often overlooked because we don't anticipate ever being disabled. The best place to get disability insurance is through your employer. If your employer doesn't offer it, you can seek out third party insurers who offer disability insurance. Lastly, if you qualify, Social Security offers disability benefits as a last resort backup.

Life insurance is another insurance you'll want to consider getting, especially if you have children. Life insurance has its own collection of issues because of how many of its products are marketed. Personally, I think insurance and investing should be separated so I recommend term life insurance. Term life insurance is a straightforward "pay premiums, get this death benefit." When you buy a $300,000 30-year term life insurance policy, you pay premiums and your family gets $300,000 if you die within 30 years. No investing component, it's strictly insurance.

One last insurance policy to consider is an umbrella policy. Umbrella insurance kicks in when all others drop out. It's like a backup insurance for when another insurance, like auto or homeowner's, hits the limit. Umbrella insurance is often very inexpensive, relative to the coverage amount, and can protect you against catastrophe.

9. Not maintaining good credit

Your credit score is almost unreasonably important in your life. From renting an apartment to getting a cell phone, your credit score is being used to give the Yay or Nay.

Fortunately, it's not difficult to maintain a good credit score. Remember that your credit score is a measure of how likely you will default on a loan. Lower score means higher risk.

To maintain a good score, you just need to be responsible with credit. It's as simple as that.

Make sure you pay your bills on time, don't open a lot of credit cards, and don't use a high percentage of your available credit. Those three tips will get you 90% of the way towards maintaining a good score.

You will also want to review your credit report every year, which you can do for free by requesting a report through **AnnualCreditReport.com** for each of the three credit bureaus (Experian, Equifax, TransUnion). Review your reports for errors and fix them as soon as possible. You don't want to discover and try to fix errors when you're applying for a mortgage loan, so stay on top of it.

If yours has taken a few dings and you're looking for ways to increase it, review our Grand Goal Guide for **How to Increase Your Credit Score**. It'll hold some strategies you can use to fix errors and

10. Not establishing long term goals

A long term goal is any goal you wish to achieve in five years or longer. Don't fixate on the number 5, that's not important, it's the idea that you should have some long term goals for yourself and your family.

A long term goal might be "buying a house in 5 years" — break down that 5 year goal into 1 year milestones and what you'll need to do to set yourself up to achieve that goal. If you decide that you want to get a 10% down payment and you're aiming to buy a $300,000 house, you'll want to save $30,000 over five years. That's $6,000 a year in savings – or $500 a month. Now you have a long term goal (down payment) along with shorter milestones of $500 per month.

As you may have recognized, retirement is a super long term goal, often decades into the future, but it's the same logic. Break down the long term goal into shorter intermediate ones and then work on those. It's hard to picture life in 20 or 40 years, but five is within reach.

I hope you enjoyed this guide!

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Thanks!

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