Why It's Never Too Early to Save for Retirement

Here's How to Get Started

Retirement may seem like a far-away milestone, especially if you're still early in your career. With 20, 30, or even 40 years between now and your retirement date, it feels like a problem best left to your future, more established self.

But studies show that most Americans don't have enough money to retire comfortably. According to a recent survey[1], only 14% of Americans have $100,000 or more stowed away for retirement. And 24% of people 65 or older have nothing saved for retirement. The earlier you start saving for retirement, the better off you'll be. Let's look at why it's a good idea to start saving for retirement as soon as possible, ways to calculate your retirement savings goal, obstacles you may face when saving for retirement, and the kinds of bank accounts you can use to keep—and grow—your savings.

The Perks of Saving for Retirement Young

When you start saving for retirement early, you benefit from two major factors: time and compounded interest. Let's break it down.

- **Time.** If you start saving in your 20s and retire in your 60s, you have roughly 40 years of savings to tap into. But there's another benefit to time: your earning potential. The theory goes that for most people, your salary will naturally increase with age and experience. So even if you start small in your 20s, you can increase your savings in your 30s, 40s, and 50s to eventually have a comfortable nest egg.

- **Compound interest.** Most financial advisors will tell you to use a specific type of account to save for retirement (more on those later). Retirement accounts rely on compound interest to help grow your savings, usually through a diverse portfolio of investments. The longer your money is invested, the more you'll earn on your investment over time.

Compound interest.

The process of earning interest on a principal amount and then, in turn, earning additional interest on top of that.

Curious to learn more about saving for retirement?

How Much Should I Save for Retirement?

Since everyone's financial situation is slightly different (and the future is unknown), it's difficult to recommend an exact retirement savings goal. Generally, experts recommend saving 10 to 15% of your annual income pre-tax[2] each year.

Let's look at an example. Let's say a person earns $75,000 a year. Using this recommendation, they should aim to save between $7,500 and $11,250 a year.

Experts recommend that higher earners aim to save closer to 15%, whereas lower earners can stick closer to 10%.

Want to get a more exact number? Try this retirement calculator

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Common Obstacles When Saving for Retirement

As a young saver, several cognitive distortions (or actual obstacles) may make retirement savings feel unnecessary or challenging. Let's review some of the most common reasons people may not save as much (or at all) for retirement.

Financial Hardship

Saving may be the last thing on your mind if you're experiencing financial hardship, like the loss of a job or a medical emergency. Saving for retirement can also feel extra challenging if you struggle to make ends meet. While it may be beneficial to examine your overall spending and saving habits, there are two important things to remember:

First, if you miss a year or two of saving because you need the money to go elsewhere, it won't ruin your retirement plans.

And second, remember that any amount of money towards retirement is progress. If you can still set aside a smaller amount and then increase your savings when you've recovered, then that's better than throwing in the towel.

Prioritizing Other Investments

We get it—retirement can seem far, far away. So far away that it feels less important compared to other financial milestones, like a downpayment on a house or a small business loan. One survey[3] found that a fifth of their participants were not saving for retirement for this exact reason. While financial priorities change over time, retirement is a long game. It's best to continue contributing to your retirement fund, even if you have to cut back occasionally to accommodate other goals. Like when you hit a financial bump in the road, any saving is still saving.

Wishful Thinking

Humans are terrible at looking at the big picture or very far ahead. Especially when we're young and vibrant, and it feels like nothing can stop us. The trouble is, we won't be young and vibrant forever. Waiting to save until the last minute is a poor saving strategy and may put you in a difficult financial position later.

Leaning on a "Safety Net"

Some people hope and/or assume that their retirement will be covered by inheritance, the sale of a house, or social safety nets like Social Security or a pension. But there's no way to know if you'll receive a financial windfall or if it will be enough to pay for your retirement. And the availability of public programs like Social Security is tenuous at best. It's a good idea not to rely on these to fund your entire retirement but rather to supplement what you've already saved.

How to Save for Retirement

There are very specific types of accounts that you can use for retirement. These accounts have a few key attributes:

- **Tax-advantaged.** These accounts have certain tax benefits, such as tax deferrals.

- **Limited access.** Unlike a traditional savings account or a high-interest money market account (HIMMA), these long-term saving accounts limit access to your funds until you reach a certain age.

- **Contribution limits.** You can only contribute up to a certain amount each year, and each account type has a specific limit.

Most retirement types, whether employer-sponsored or self-funded, offer two options:

- **Traditional.** This account is both tax-deductible and tax-deferred. This means that your contribution is subtracted from your overall taxable income, which can help you save money at tax time, and you don't pay taxes on your earnings until you withdraw the funds post-retirement.

- **Roth.** A Roth account uses taxed income to build your fund. However, when you're ready to remove your funds, you won't owe any taxes because you will have paid them already.

Here are some of the most common types of retirement funds.

Employer-Sponsored Retirement Fund

If your employer offers a retirement fund (often called a 401(k)), you can automatically deposit a percentage of your pay into your retirement fund with every paycheck. It's an easy way to save because it happens automatically, and you can customize your deposits. An additional benefit of an employer-sponsored fund is an employee match: The employer may offer to "match" your contribution up to a certain amount.

Here's an example. Let's say you get paid $75,000 a year, and your employer offers up to a 4% match on your 401(k). That's $3,000 extra a year toward retirement if you take the highest match, making it a total of $6,000 annually. Maxing out your employer's match is always recommended since it's considered "free money" that doesn't count towards your contribution limit.

An IRA

An IRA is a self-managed, self-funded retirement account held at a major financial institution. The funds are tax-deductible and tax-free until withdrawal.

There are two major differences between an IRA and a 401(k): An IRA offers a wider variety of investment options, so you can curate your portfolio exactly how you want. However, IRAs have much smaller contribution limits than 401(k)s.

Take a look at Keesler Federal's IRA options

Your IRA Options

There are two primary types of IRAs that can be used as a tool to build your retirement fund:

- **Traditional IRA[4]:** Available to anyone who earns, or whose spouse filing jointly earns taxable compensation, until the age of 70 ½. There is no earning limit to utilize a Traditional IRA, and you must start withdrawing funds at age 70 ½. Withdrawals made after age 59 ½ are taxed as regular income, and withdrawals made before this age are subject to taxes and a 10% penalty fee.

- **Roth IRA:** Available to anyone who earns or whose spouse earns taxable compensation, no matter the age. In order to use a Roth IRA, you must earn less than $153,000 filing single, or less than $218,000 filing jointly[5]. Contributions are not tax deductible, and funds can be withdrawn tax-free after age 59 ½ as long as the account has been open for at least 5 years. If funds are drawn before age 59 ½, these withdrawals will be taxed and subject to a 10% penalty fee.

Saving for retirement is an important financial goal that will set you up for life down the road, whatever that may look like. Learn more about how to save for retirement here. And if you need a little extra help, Keesler Federal's financial advisors are here to support you. Learn more

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Sources

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