

Financial Advice for New Grads

Five tips to share with the young people in your life.

Whether you're recommending a career in the plastics industry or touting the virtues of wearing sunscreen, graduation seems a natural time to share advice with any young people in your life. Because graduation often coincides with other life changes—including new jobs, moves, and sudden windfalls from generous relatives—it's also a great time to share financial guidance with any young graduates in your life. You no doubt have some tips of your own, but here are some of my best ideas for getting off to a good financial start.

1. Seize the Day

Although most new graduates aren't yet pulling down big salaries, the post-college years can actually be a great time to build a solid savings foundation. The young person in your life may have received some cash gifts upon graduation; urge him or her to save at least part of the windfall. And if they were accustomed to living on a shoestring while at school, new grads are apt to find it fairly easy to save part of each paycheck once they begin working, even if their income levels are still fairly low. The fact that many new graduates live at home for the first year or two after school provides an additional opportunity to sock away some cash. To help sell your new grad on the merits of saving, share a story about something exciting you were able to do or buy because you had saved money for the future rather than spending it right away.

2. Start Small, But Get Started

Young people might assume you need to have deep pockets to be an investor, but let the new grad in your life know that that's definitely not the case. Some terrific mutual funds will let you in the door for as little as \$500.

Even if market returns are fairly paltry over the next few decades, the benefits of getting an early start on investing can be substantial: The 21-year-old who starts saving \$1,000 a year and earns an annualized 5% on his money will have more than \$150,000 when he turns 65; were he to wait even five years to begin saving, he'd have only \$114,000 when it came time to retire.

3. Invest on Autopilot

Even investing veterans can attest to the fact that it's difficult to invest with discipline. As much as we all know that the goal is to buy low and sell high, it's a lot more fun to be an investor when everything's going up than when the market's in the tank. Investing on a regular schedule is a particularly big challenge for young people, who can find plenty of other ways to spend their hard-earned cash.

That's why I'm such a big fan of automatic investment plans, whereby you agree to invest a set amount every month. If your new graduate has landed a first job, urge him or her to take part in a 401(k) or any other defined-contribution plan—a familiar type of auto-invest plan. Because the participant's money is deducted from his or her paycheck on a pretax basis, contributions are particularly painless for young savers. A number of mutual fund companies also allow you into their funds with a relatively low minimum if you sign on for an automatic investment plan.

4. Use Credit Wisely

We've all heard about how banks bombard teenagers with credit card offers, and many college kids have been brandishing plastic for years. Those offers will only increase once the new graduate in your life lands a job, and the youngster will also likely be offered ever-higher credit limits. Because building and maintaining a good credit history will have an effect on almost everything your new grad might choose to do in this life—from buying a house or car to renting an apartment—graduation is a good time to review the dos and don'ts of managing credit.

Yes, a credit card can be handy in emergencies, and it makes sense for each person to establish a credit history in his or her own name. But keep it simple: A bank account and a single major credit card is all you really need to begin establishing a credit history. Urge the young person in your life to keep a running tally of any charges he or she makes and emphasize the importance of paying your balance in full each and every month. To drive the point home, discuss how credit cards can be “reverse savings accounts” if you carry a balance—that is, the interest rate you pay on your debt can easily wipe out the earnings from any money you manage to save or invest.

5. Know the Real Meaning of Prestige

Whether it's an iPod or an Izod (those alligators are back in style, you know), young people learn early on the value our society places on status symbols. But those status symbols can be illusory: The person driving that expensive car could be on the verge of bankruptcy, while the one in the 17-year-old station wagon could pay cash for 20 shiny new Mercedes.

Some people never learn this lesson, but you're on a slippery slope if you start defining yourself by your material possessions and the illusory "status" they confer. If you always need the newest, most expensive car, computer, or shoes (or whatever it is that floats your boat), you can easily set yourself up for financial disaster—or, at the very least, rob yourself of the chance to build real wealth.

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