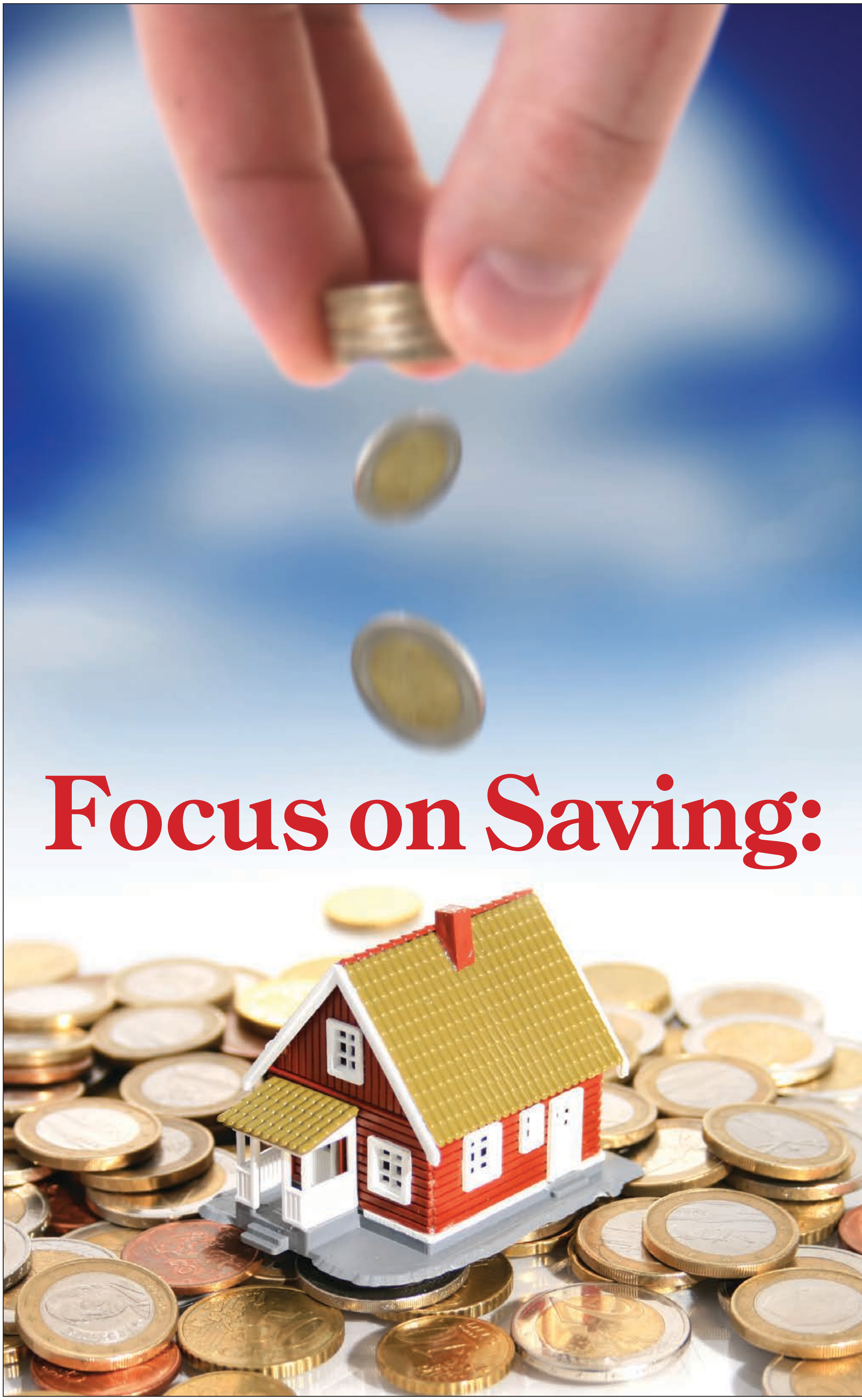

Focus on Saving: Ways to Save for a Down Payment and Build Financial Security

BY JANET THOMSON

According to Go Banking Rates 2015 survey, the biggest challenge for Americans is sticking to a budget. In fact, the study reveals that 62 percent of Americans have under $1,000 in savings. This is a startling discovery because the absence of a cash reserve means that during an emergency many people will have to rely on credit, family, friends or even their retirement accounts to cover life's unexpected incidents. Having a cash reserve or savings is a key component to determining financial health. Unfortunately, for many people, knowing where to start or taking advantage of resources available through avenues, like an employers' matching incentive retirement plan (which often goes untapped), could become a game changer for individuals struggling to save for the future. When you understand the importance of these incentives and other saving strategies, it drastically could change your financial trajectory. Dreaming of a new home in 2016? Here are some strategies you could implement to help get you a step closer to homeownership and build financial wealth and security.

First Steps to Saving for a Down Payment

For many people saving can be a real struggle. When you are living from paycheck to paycheck, putting away money for things like retirement and emergencies can be challenging because those funds are immediately used for rent, utilities and other monthly bills. First, figure out exactly how much you actually need to save for the down payment on your home. Ideally, you want to have 20 percent of the purchase price of the home in order to avoid Private Mortgage Insurance (PMI), which usually is required when your down payment is less than 20 percent. Although there are programs available requiring as little as two percent of the purchase price, or even zero down in some cases, soliciting the help of a qualified REALTOR® will help navigate you through this process. But for those individuals wanting to avoid paying the PMI premium, saving funds for this important life changing goal is an attainable and sustainable one. In fact, there are a lot of things people can do to save money. Once you have determined what you are saving money for, putting a strategic plan in action becomes doable because the end result could mean stability and security for your family.

According to Kimberlee Barrett-Johnson, financial advisor and President at Barrett-Johnson & Associates, if you are getting a raise at your place of employment, before committing to spending that money on your lifestyle, a better alternative is to immediately save the whole amount, less taxes, to a separate account. For example, you could set up the account with a monthly bank authorization. That way you are not tempted to use it for unnecessary or impulsive purchases. This will create a very positive and empowering money habit, and as you see your savings building, it encourages you to save even more.

Another way to jumpstart your savings is to use your tax refund. According to the irs.gov report, the average refund in 2014 was $3,034, and almost 88 percent of those refunds were directly deposited in the accounts of taxpayers. If you are expecting a refund, directing those monies to your housing fund account can significantly help boost your confidence and relationship surrounding saving money. Since you are not relying on this extra income to maintain your household, putting it away becomes easier, especially when you have a goal. In addition, you might want to consider investing your withholdings as a way to build towards a home down payment. By adjusting your withholdings, "you can avoid locking your money in a no-interest holding cell."

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Using Retirement and Investment Funds to Purchase a Home

Sometimes it makes sense to use monies that have been set aside for retirement towards a down payment on a home, says Barrett-Johnson. However, you want to carefully assess your individual circumstances to avoid any unintended consequences. In the right scenario, using something like your employer 401(k) plan for first time home buyers is a good option.

According to smartasset.com, borrowing directly from youself is a great way to leverage a 401(k) plan for a home down payment. When you take out a loan against your 401(k), you are paying back the principal and interest on the loan directly to yourself, instead of a third-party or bank. For individuals looking to purchase a home within five years, market based investments (like an S&P 500 index fund) might be worth considering.

However, "if the goal is less than three years, you probably don't want to be investing in market based accounts," says Barrett-Johnson. "You wouldn't want to pull money out of your investments at a time when the investment is taking a down turn, but five years is far out enough that it could make sense to invest in a mix of stocks and bonds, especially if you are dollar cost averaging." In other words, you are systematically investing the same amount of a particular investment on a regular schedule.

For example, if you had a monthly car payment of $400 and you are used to having that money going out of your cash flow each month, you could put those funds in an investment account with the goal of using it as your nest egg for a down payment on a home. Barrett-Johnson says that because you are dollar cost averaging, there will be some market fluctuation over that five-year time period. However, because of this five-year time factor, you could benefit from volatility. Basically, you purchase more shares when the prices are cheaper, and fewer shares are bought when prices are high. Essentially, when shares are going up and down this simply means that your average cost per shares is less than the average price per shares. And, if you are good at making money, this is a great way to take advantage of the natural volatility that the stock market has—buy more when it's cheaper and less when it's expensive.

Market based investments can be a great approach to building a financial nest egg, if you have the time and patience. However, Barrett-Johnson advises that when you get within two years of your five-year goal, start considering whether it's a good time to get out and move your money into something safer.

Practical Ways to Save for a Down Payment

When determining exactly how you plan to approach your house saving journey, go through your budget and identify some low hanging fruits—things that you could live without indefinitely or perhaps for just a short period of time while you are saving for this very important goal of homeownership. Instead of blowing your money on a lavish vacation, why not consider a staycation or day trip as alternatives. The money that you typically would spend on hotel accommodations or an exclusive resort could be used towards your goal of getting into a new home. In addition, you could turn off the cable bill and just use some online options like Netflix and Hulu for entertainment. Furthermore, looking into a cheaper telephone provider could also yield some extra savings.

Additionally, if you are spending an alarming amount of your hard earned cash eating out daily, then you are missing out on a great source of revenue that could be used to kick start your savings journey. Instead, take your lunch to work as opposed to eating out. When people begin to look at their lifestyle choices and make some changes, they can get excited, says Barrett-Johnson. Changes that are gradually incorporated can be more empowering as opposed to feeling deprived during this financial transition. Having the right attitude and mindset towards savings will help you become better off financially and get you closer to your goal of homeownership, which is an important step towards building wealth.

Building a Permanent Financial Wealth Mindset

Financial wealth and security doesn't end once you have reached your housing goal. After settling into your new home, dedicating money towards saving for retirement should be an essential goal. If you have a 401(k) plan or a simple IRA through an employer where there is a match, you should take advantage of this perk because it's free money that you don't want to leave on the table, advises Barrett-Johnson. Then, if you are eligible, Barrett-Johnson suggests contributing to a Roth IRA because it's a great place to save and has the nice counterpoint to a traditional IRA or 401(k) in that you have tax and investment diversification. According to vanguard.com, you want to start simple, which means looking at your age and income. Then compare the IRA rules and tax benefits. For example, with a Roth IRA you can contribute at any age. However, with a traditional IRA you must be under age 70 ½ in order to contribute. In addition, vanguard.com chart analysis goes on to show that for the 2015 and 2016 tax years, taxpayers under age 50 can contribute up to 5,500, and if you're over 50, that contribution amount increases to $6,500 for both a Roth IRA and traditional IRA respectively. Buying a home and educating children are some of the major life goals that people have. Often times, you have more time to save for retirement and usually you can take advantage of many market cycles as well as dollar cost averaging – "investing in equity and things that fluctuate can be a very tolerable way to build for the future," says Barrett-Johnson.

Determining Your Destiny

Although it can be tough to put aside money, there are many different ways to get the ball rolling. Setting up some practical strategies like having a certain amount each month to automatically transfer into a savings account, or using your yearly bonus as a jump start to building your savings are just two of many great options. In some instances, tapping into your 401(k) or IRA accounts will make the most sense. But, before going this route understand the tax implications and penalties associated with using funds from these accounts. In addition, if you are a savvy investor and have at least five years, market based investments could be more beneficial for reaching your housing goal. Regardless of the strategy or approach taken, you don't want to be house poor, because people are generally much happier when they are not money stressed, says Barrett-Johnson. The great thing about home ownership is that you begin to earn equity with each mortgage payment. Those payments goes toward reducing your debt and the equity in the home can be a very important first step to building wealth – "it's definitely a very good goal and often the first step on the path towards financial security for many people." ■

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