Healthy Financial Habits

Yes, even dentists need these.

By Richard A. Green, DDS, MBA

How did you go bankrupt? "Two ways. Gradually, then suddenly."
– Ernest Hemingway

Developing healthy financial habits is the surest way to grow your wealth.

The simple truth is financially successful people tend to think and behave in specific ways. They develop habits that separate them from those who struggle with money issues their entire lives. While what I am going to say is common sense—based on long-ago-learned basic math, busy people with immense responsibility…like dentists…can learn from one of Ben Franklin's proverbs: "If you would be wealthy, think of saving, as well as getting." The admonition of a not so famous man, yet one very influential in my life, my Grandfather Green would often say, "learn first to be responsible with little and in time you may find yourself responsible for much!"

Beginning can be the hardest part of the journey; *Learning to Live On Less Than You Make* – my definition for *Financial Freedom,* can occur at any age. Start living the definition of *Financial Freedom* and you change your relationship with money. It can engage you in the *power of compounding*. This change in your relationship with money can change the conversations you have with your patients. When a patient needs you and the work of your mind and hands more than you need their money, it changes the relationship and the conversation.

The residual benefits of beginning *compounding* early are well documented while action based on this knowledge is often unrealized by many. This inaction can seriously get in the way of accomplishing *Financial Independence*, which I define for a dentist as that point in your life when the return on your investable assets, replace the cash flow from the work of your mind and hands. *Financial Independence* is influenced by many factors, some we will be able to talk about in this article. Some factors have been written about and fill many books. I will include some observations within this article for your consideration of why now is the time to start if you haven't already done so!

- ✓ **Save part of your income.**

Human beings can be creatures of habit. Many people live from one paycheck to the next, because they have a habit of spending everything they earn. Financially successful people develop a habit of putting aside a percentage of their income every time they are paid. Each time you earn money you have a choice of saving and/or investing a portion.

Financially successful people put aside at least 10 percent, preferably 20 percent, for wealth accumulation. I call this "paying yourself first"…before you pay your bills and then start spending all the leftover earnings.

They invest a percentage in *tax-deferred investments* as well as *after-tax investments*. The benefit to investing in both *after-tax* and *tax-deferred investments* is ultimately choice. *Tax-deferred investments* often have high penalties for using them before appropriate timelines; this can be helpful when developing your savings discipline and present a difficulty if a life event (major health issue) places you in a situation where you require extra funds, before the *tax-deferred investments* are available without penalty. This is where *after-tax investing* can give you the benefit of choice in situations like an untimely "whack on the side of the head." (I'll talk more about this later.)

Of course, saving (*tax-deferred* and *after-tax*) requires earning more income in your business, so your practice has the option of offering a *tax-deferred retirement plan* to the whole team, doctor included. As well as, an appropriate personal income, which creates adequate funds for *after-tax saving and investment* along with funds to spend on your household, debt financing, contributions, and lifestyle essentials. Being able to accomplish this may mean decreasing your discretionary spending as you begin to shape new habits. You aren't going to know until you examine your personal situation…know yourself from the inside and out when it comes to money.

We are all shaped by our attitudes and beliefs around money and these attitudes and beliefs, if unexamined, can often get in our way, as we attempt to encourage ourselves and others to be *positive choice-makers* in the area of dental health. It is always easier to encourage others when we ourselves are actively practicing and demonstrating *positive choice making*.

People who are financially successful have an attitude about money that motivates them to be deliberate about investing and preserving money long term. As your money begins to accrue, you may be tempted to spend it. Resist the urge.

- ✓ **Control and Eliminate Debt**

Make a habit of listing how much you owe and to whom with a grand total amount. As you make a habit of tracking your debt each and every month, set a goal to eliminate all your debts.

The habit of tracking your debts and setting a goal to eventually eliminate them will cause you to pay closer attention to how much your monthly payments are for reducing the loan amounts. You'll be less inclined to accumulate new debt, as well as motivated to pay off what you presently owe sooner than the normal repayment schedule. These behaviors can lead you to creating an annual Net Worth Statement to track your progress in Wealth Accumulation.

- ✓ **Control Your Expenses**

Make a habit of budgeting your income. Your spending plan for how you will use your earned income before you receive it, can include the amount of money you:

- Intend to save automatically,
- Need to cover household line items,
- Need to make your debt payments,
- Intend to contribute, and
- Desire to provide opportunity for family vacations.

The habit of creating a spending plan and knowing where your dollars go will likely motivate you to find ways to cut costs in order to increase the amount of discretionary money you have leftover after meeting your monthly financial obligations. A well thought out spending plan can help you avoid costly bank overdrafts and impulse credit card charges.

- ✓ **Set Goals and Deadlines**

Set goals and deadlines for achieving the financial success for which you are striving. You can make a habit of setting short-term and long-term goals for the amount of money you save and the amount of debt you eliminate. You can then find some way to celebrate your victories, large and small.

- ✓ **Schedule a regular time each month for financial planning.**

  Don't let life get in the way of creating a monthly plan and tracking its execution. Forming healthy financial habits requires discipline and effort. In the end, it comes down to being a ***proactive person of choice***. If you are mindful, you will move in the right direction. The sooner you start, the longer your investments can grow, and the more doubling periods you will experience.

- ✓ **The Rule of 72.**

  This rule states, if you divide the number 72 by the rate of return of your investment assets, you discover the number of years it will take for your investment assets to double, this assumes a constant rate of return. If you are 35 years old and reading this now, this is the take-home message: *The Rule of 72* teaches us that by waiting to get started until you are 42, you will have half of what you would have had at retirement age than if you had started saving at 35.

  Do the calculations yourself. A 35-year-old has 32 years to 67. In today's market place 6-8% growth in a conservative stock with a dividend yield of 2.5-3% could yield a total annual return of 10+% compounded. You play with the amount you can invest annually and see how, with the 35 or 42 year old starting dates, the 42 year old will have about 1/2 of the total amount available than the 35 year old has at 67 years of age Depending on the amount of money you can invest every year, some of the numbers you will come up with can sound like a lot of money. Yet, when adjusted for just an average 3% CPI Inflationary Factor, to arrive at an inflation adjusted dollar value, the purchasing power of those accumulated dollars will be less. Don't forget you will pay a tax up front (prior to investing) on *after-tax investments* and with *tax-deferred investments* you pay the income tax just before you get to use the money during your retirement years. When calculating your position of *Financial Independence,* the consideration of *CPI* and taxes are important to forecast, for they impact the amount of total invested dollars available to you to consume in retirement. Doing these calculations can alter your *Financial Independence Timeline*.

- ✓ **Another way to look at the *Power of Compounding***
  I remember beginning to read the Wall Street Journal (WSJ) and seeing some half and full-page ads for Mutual Funds bragging about their performance. Many of the graphs looked very similar. They would often start with a $10K investment and then show the projected value after thirty

or forty years. What I noticed was the slope of growth was very gradual the first fifteen to twenty years of investing and then it tended to become almost vertical over the next fifteen to twenty years! I was introduced to looking at the *Power of Compounding* from the point of view of consistently adding investment funds on a regular basis and watching what happened when the performance was measured by a ratio, which compared the annual internal earnings from the accumulated mutual fund in dollars and compared them as a multiple of the annual amount of capital added each year. This Ratio changed with a timeline, which was related to an average percentage return performance. If an average 10% Total Return could be accomplished by the mutual fund, it took approximately 8 years of putting in the same amount of money each year for the total invested amount to internally earn a dollar amount in the 8th year, which equaled the annual contribution. At that time the Ratio was considered 1:1 and the growth graph looked pretty flat. I began to see the *Magic of Compounding* when I notice it only took another 4 years at 10% to reach a Ratio of 2:1; when I contributed an amount equal to "X" the previously invested capital added "2X" to my mutual fund investment account. And then 3:1 appeared between the 14th and 15th year. The intervals of time shortened as the multiples in the Ratio increase; the *Magic of Compounding*! Remember the timeline is only altered by the amount of the average ROI – so if the average ROI is 12% the 3:1 Ratio appears in about the 13th year. A couple of basic principles of wealth accumulation became clear: First, everyone goes through the "flat" period of the curve, no one avoids it no matter how long you wait to get started, so start! Second, once you get to 3:1 you can really see the acceleration for often within another 5 years your Ratio is at 6:1 and you are seeing the Ratio advance by a factor of 1 annually. Can you imagine the smile on your face when you are at 10:1 – you are still putting in "X" and the corpus of your invested accumulation is putting in "10X" that year, due to the ROI – a different way to think about why now is a good time to get started, and a different way to look at *The Magic of Compounding*! For those who are a bit competitive and enjoy seeing your investment graph, representing wealth accumulation steepen, a phrase has grown from understanding the impact of the accelerating growth in the Ratio: ***The person who gets to 3:1 first wins!***

✓ **Some thoughts on *After-tax* or *Tax-deferred Investments* – it depends!** When I first met Dr. L.D. Pankey in 1968, I was 26 years old and from my point of view, I did not have two extra quarters to rub together. At that time, there were very few tax-deferred investment vehicles available to dentists. So, in an *after-tax environment*, Dr. Pankey's counsel was quite direct:

- Create a 3-6 month Emergency Fund –money to live on in the event of an emergency.
- Invest in yourself and your continuing education; you are at the *pivotal center* of your *"Economic Engine*" and you are worthy of continued investment, in learning and growing your skills, knowledge, business acumen, management understanding, and leadership.
- Create an Investment Savings Account and accumulate $15K – in today's dollars, a conservative estimate would be an equivalent of $105 -150K, so saving it will take time and discipline.
- Find a low expense ratio Mutual Fund Family of Funds like T. Rowe Price – now Vanguard and find 3-5 Individual Funds within the family and open Accounts in them.
- Start weekly or monthly investing and Dollar-Cost-Average your investments over time. As you establish that discipline be open to additional systems you can implement in "down markets" to increase your long-term yields/returns. Do not try to time the market by taking all your money out thinking you know just what the market is going to do. Rather develop a discipline and cash reserve to be an investor in down markets! (That is when the Investment Savings Account will be used, with a discipline.) Research abounds, which shows when you try to time the market, you more likely will miss the most powerful upswings, which over time account for the markets greatest gains for long-term investors. (More can be said about these disciplines at another time – start with the basics and develop your *Healthy Financial Habits* first.

All of the above was done in an ***after-tax investment venue***, from my 26th year until my 34th year, when I incorporated my practice into a "C" Corporation. At the time, the "C" Corporation was the best vehicle to create a *tax-deferred Pension and Profit Sharing Plan,* which allowed a $30K maximum contribution per year. (Much higher than the $7,500 Keogh Plan available for non-incorporated professionals.) Today there are many more choices and much higher maximums, which to me is a welcomed array of investment vehicles for professionals.

Over the past fifteen to twenty years *tax laws* have changed from time to time, which have either favored the *after-tax investmen*t or the *tax-deferred investment,* as a long-term retirement and Wealth Accumulation vehicle. At the present, I would recommend at least the first two items on Dr. Pankey's list to those who are beginning to shape *Healthy Financial Habits*. Use a *tax-deferred retirement investment vehicle* while you develop your *Healthy*

Financial Habits Discipline because it is harder for you to withdraw and spend the money you are trying to save. I would encourage you to invest in the *tax-deferred investment vehicles* to the maximum allowable in the letter of the law. With the present tax law, the difference between an *after-tax investment* and a *tax-deferred investment accumulation vehicle* over time, have been minimized. So, get started now. Do not let the vehicle get in the way! And as you gain strength in your *Healthy Financial Habits Discipline,* use both *after-tax investment* and *tax-deferred investment* vehicles to develop your Wealth Accumulation; these actions will create in you ***a person-of-choice perspective***.

✓ **Thoughts concerning long-term investing**
Just about all serious endeavors encourage a period of reflection and clarification concerning: Your *Philosophy*, Your *Process*, and Your *Discipline*; the same holds true for investing. I would encourage you to develop a *Philosophy* of a long-term investor. One who uses a *Process* to allocate investment capital on a percentage basis into selected investment vehicles. One who's *Discipline* routinely places a percentage of your business income (*tax-deferred*) and your personal income (*after-tax*) in investment grade assets on a regular basis. Because you are a long-term investor you will continue to invest in all markets and develop a *Process* and a *Discipline*, through experience, to invest more in periods of down markets and in that way increase your chances to buy low and sell high.

One of the advantages of being my age is I have been observing the markets, in which I invest, for forty-six years. It has been proffered in investment books for years that most individuals will experience at least three 30% drops in the market in a lifetime. Well, when it first happened to my money, I was ready to take what money was left and run. Wise guidance encouraged me to stay and put some more in during the down period, along with my regular investment amount. (More on this in a future article)

Think about the recent ten-year period; the markets moved to a high and then retreated by more than 30%, followed by a recession and then followed by slow positive growth to an exceptional year in 2013 and now we are half way through 2014 and the growth has slowed, yet the market is attaining new highs, beyond the previously ten year highs. Growth expectations have been encouraged to lower percentages as we are reminded of the markets habit of "*regression to the mean*" as a factor of past behavior.

> The current market environment is colored by extended multi-day rallies. Then consolidation periods where each pullback is shallow and short lived. *What does it all mean?* One position of thought is the bullish bias continues. Just at a more tepid pace than the last few years. Yet when you appreciate how little the bank is paying you on your cash or the meager yields on bonds, you can begin to understand why investing in stocks continues to be the best game in town. Many of the so called, *"Rules of Investing and Portfolio Management"* from past decades, have been altered due to the impact of the Federal Reserve artificially holding down the interest rate over a long period of time. The risk to the value of bonds, if and when the interest rates return the market-determined rates, is significant. All of this has moved the investor into areas of higher risk for return, when considering previously defined portfolio management percentages for balancing stocks and bonds.
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> One thing, which has been shown time and time again, is *market timing does not work*. Most *Processes* and *Disciplines* would encourage staying in the market and finding a way to identify cash flow potential, through valued pricing and dividend yield. When I have watched individuals remove their funds from the market, they have extreme difficultly getting it back into the market and often they have missed appropriate re-entry points, creating lost opportunity more than saving money, especially when considered from a long-term perspective

Start Early Developing Healthy Financial Habits / Wealth Accumulation
Despite the general feeling of uncertainty and financial market ups and downs and back up we experienced in the last few years, regular saving via *after-tax* and *tax-deferred investments* has paid off for those investors with a long-term perspective. My full-time, past position as Director of Business Systems Development at The Pankey Institute (1994-2004) provided an opportunity to create and observe many responses to our *Financial Health Questionnaire* at our C-4 level. Often the responses revealed a wide range between those who had developed the discipline of regular saving and investing and those who had yet to get started. Postponing saving will leave a person woefully behind the curve at just about any point in their career. It can be a sad day when the awareness of the truth occurs, yet that waking up is better than burying your head in the sand.

During 1994 – 2004 at the Pankey Institute and in the past ten years continuing to work with dentists and teams as a Coach, Facilitator, Consultant, and Educator, I have been allowed the privilege to listen to professionals – some just getting started, some in their middle years, and some in the midst of practice transitions and major life transitions. Often I am asked to comment on their Financial

Statements and Personal Balance Sheets or Net Worth Statements and Retirement Assets. I observe a wide variance in the ability to accumulate wealth.

The results reflect a matter of choice and it has been their choices, which have shaped their present situation. At times, especially when the gift of time to "recover" is not as readily available, it can be difficult for me to remain silent. I find any words, which may imply a corrective action, can be received as being judgmental. Knowing what I know about the "*Magic of Compounding*" and witnessing a lack of response based on a person's outcomes can be disheartening.

While there is some need to be emphatic, my intent is not to make anyone feel guilty concerning the past or to look to others to rescue them. Rather, my intent is to encourage everyone to take the individually appropriate action now to self-correct your financial position over time. This is often easier said than done!

There are many forces that shape our attitudes about money, not the least of which is our own family of origin: attitudes, which can be real or perceived. These issues become very important in the life and work of a professional. They impact all aspects of communication with patients, team, suppliers, family, consultants, and advisors.

I would encourage some reading on the subject – any reading. You pick the book! There are a number of books: *The Richest Man in Babylon, The Millionaire Next Door, The Millionaire Mind, Money and the Meaning of Life by Needleman*, *The Number by Lee Eisenberg*, or for our Canadian friends – *Better Happy than Rich: Canadians, Money and the Meaning of Life* by Michael Adams. Go to www.amazon.com and pick one out for your reading. Start examining what is between your ears – your attitudes, beliefs, and operational directives connected with money.

I am a slow reader. If you are, don't let it be an excuse. Buy a book, read, and start investing on the same day! Do it even if you presently do not have the perfect retirement investment vehicle to invest in. Saving is about discipline. Save regularly starting now so you have something left over when your hands, back, or eyes give out!