Millennials: the Chart Every 25-Year-Old Needs to See

Description

There's a great story about the man who invented chess.

The inventor brought his chessboard to the emperor of China, who was so impressed that he offered to grant the man one wish. The inventor asked for one grain of rice on the first square of the board, two grains on the second square, four on the third, and so on.

It sounded like a modest proposal, so the emperor agreed. However, filling the chessboard's last 10 squares would have required 35 quintillion grains—enough to bury the entire planet under three feet of rice. The emperor was unimpressed and so had the inventor beheaded.

If you're 25 and under, you need to see this

Whether or not the story is true, it does illustrate the power of compound growth. When things grow exponentially, gains look tiny at first and then suddenly shoot off the charts.

The trick to making compound growth work is getting to the end of the chessboard. That's where the massive gains are. It's why, of Warren Buffett's $73 billion net worth, $72 billion was added after his 50th birthday and $70 billion came after his 60th.

Of course, few of us will ever be billionaires. However, the effects of compounding are profound, even for those of us with more modest means. Let me give you an example:

Two brothers, John and Hank, start a video blogging business at the age of 25. It's a success! So much so that there are a number of spin-offs—including "John Games," "Crashing Course," and "The Science Show."

Hank, the traditionally responsible brother, begins adding $5,000 to his tax-free savings account each year. He ploughs his money into a generic, low-cost equity index fund like the **iShares S&P/TSX 60 Index Fund** (TSX:XIU). This earns a 7% compounded annual return, about the stock market's historical average.

Hank sticks with that program for 10 years, but then inexplicably buys season tickets to the Calgary Flames. While he can certainly pick a winning hockey team, Hank can no longer afford to set aside any money.

His brother John parties hard and postpones saving until he turns 35, coincidentally the age in which Hank stopped. However, John sticks with his $5,000 per year TFSA contributions for an impressive three decades, investing in the same index fund, earning the same return.

At age 65 Hank's TFSA will be worth $563,700. John's will be worth only $505,400. John saved for 30 years versus Hank's 10. But because John started a mere 10 years later—a seemingly trivial detail when you're talking about a 40 year time frame—he ended up with a much smaller portfolio.

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Let's take things one step further. Suppose Hank isn't a sports fan and kept stashing away $5,000 per year. With an extra 30 years of saving, he would end up with $1,068,000.

Yikes! Hank finishes with more than twice as much money as poor John. Because John started to save only a decade later, he now has to stash away more than twice as much cash each year to catch up to Hank.

Is it doable? Yes, but it certainly is not easy.

This example illustrates the importance of saving early and often. What's strange is that many so-called experts are pushing the idea of *intentionally* not saving in your early working years. They argue that because your income is low, you should wait till later in your career to start putting money aside.

These folks are dumber than a box of rocks! That's because costs have a funny way of always going up. Second, few people are going to be able to transition from saving nothing into super-savers later in life. And of course, by delaying investment, you're sacrificing your biggest advantage—the wonder of compound growth.

The big money mistake that makes you look dumb

Now, what should you do if you're one of the tardy ones? First, send this article to anyone you know under the age of 25. This concept could literally make them a millionaire.

Second, don't panic. The best time to save was 20 years ago, but the second-best time is now. I've met a lot of people who have recovered from slow starts and did just fine money-wise.

However, the math is clear: procrastination is your enemy. Save now. Save a lot! That way you can make it to the end of the chessboard.

CATEGORY

1. Investing
2. Stocks for Beginners

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. TSX:XIU (iShares S&P/TSX 60 Index ETF)

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Date
2025/08/27
Date Created
2015/04/29
Author
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