Young Investors: Follow These 5 Steps To Start Building Wealth

Description

My biggest regret today at age 26 was not finding a clear-cut, defined path to building wealth and growing my net worth as a new investor. I made a lot of mistakes when I was 20 (weed stocks, penny stocks, expensive mutual funds, etc) that set me back a bit.

Fortunately, I had time on my side and was able to recover by age 22 back on the path to financial freedom. However, I still would have loved some sort of a short, clear guide on how to get there. Today, I'll be writing that guide, so you can follow it and start investing today.

Step 1: Build an emergency fund

You should only invest what you can afford to have locked up and unable to spend for a long time. This means you should have six months' worth of cash tucked away for a rainy day. Doing so will prevent you from taking on high-interest debt or cashing out investments to stay afloat during a crisis.

Step 2: Pay off high interest debt

It makes no sense to invest when the return on your investments hardly pays off the interest rate on your debt. Things like credit card debt can have annual interest rates of 19.99% or more. When the average stock market return is only 10%, it becomes absolutely important to eliminate this debt before you invest.

Step 3: Pick a broker and open a TFSA

Canada has a variety of self-serve online brokerages. Compare them side-by-side, taking note of their fees and features. When you've found the right one, open up a Tax-Free Savings Account (TFSA). Depending on the year you turned 18, you'll probably have a decent amount of contribution room. Max it out!

Step 4: Choose your asset allocation

Your asset allocation defines the ratio of stocks vs bonds in your portfolio. As a general rule, stocks return more, but bonds are less volatile and drop less during a crash. The proportion will depend on your desired return, time horizon, and risk tolerance. Common allocations include 90/10, 80/20, and 60/40 stocks vs bonds.

Step 5: Choose your assets

For most DIY investors, I recommend using exchange-traded funds (ETFs) that track a broad stock or bond index. Stock picking is time-consuming, exhausting, and prone to under-performing passive investing over a long time. Most people cannot consistently beat the market. So pick a globally diversified, low-fee ETF portfolio and call it a day!

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