Strategies *for* teens *to invest early*

BY JESSICA PERRONE

Jessica Perrone, Founder of HerFinIQ.com, is a Summit mom and experienced investor who's on a mission to empower women and teen girls through Financial and Investing Education. Each month, she will answer questions she commonly receives on how to invest.

Question:

Dear Jessica, What are your thoughts on strategies for teens to invest early? - Kim, Summit NJ.

Dear Kim,
That's a timely question, especially with summer vacation in full swing, and if your teen has a summer job, they're bound to have extra money burning holes in their pockets!

First, consider talking with your new earner about the basic savings rules. An adult with various grown-up expenses is wise to allocate after-tax income: 50% to needs, 30% to wants, and 20% to savings. The "Jessica Perrone" savings rule for teens living at home without expenses is to save 50% of their after-tax income. So if your teen makes $4,000 as a barista at Starbucks this summer, they may want to consider putting away $2,000 of those earnings.
Now that we have the savings rules covered. How do we get these funds invested? I recommend researching or speaking with an investment professional about Roth IRAs as an investment option for these summer wages. A Roth IRA is an interesting way to build a teen's wealth early, especially because anyone with earned taxable income can contribute to a Roth IRA regardless of age.

Here are some of the rules:

- *The teen's wages from summer employment cannot be under the table. Meaning they need to work at a job where taxes are withheld.*
- *For 2021 and 2022, workers can contribute up to $6,000 a year to a Roth IRA.*
- *The contribution can only be as large as the individual's earned income.*
- *Parents can contribute to the teen's Roth IRA as long as it does not exceed the individual's earned income.*

I'm sure some of you have seen on social media the posts where if an individual starts investing early, they can be hypothetical millionaires by retirement. Let's look at two scenarios (for educational purposes only).

Scenario 1:

An individual starts maxing out yearly IRA contributions at the ***age of 15.***
Suppose a teen starts investing at age 15 by putting the max contribution of $6,000/year into their Roth IRA every year for 50 years. Now we'll add a 7% (rate of return) to the equation with annual compounding. In this scenario, **by the age of 65, the potential future balance could be as high as $2,786,658!**

Scenario 2:

An individual starts maxing out yearly IRA contributions at the ***age of 35.***
On the other hand, say the individual does not start contributing until age 35 (20 years later) if they max out their contribution each year and deposit $6,000/yr. into their Roth for 30 years at a 7% rate of return with annual compounding. **The potential future balance at the age of 65 would be $652,112.** That is a big difference!

As with all types of investment accounts, it is essential to do your research, but understanding your options is a great way to start! It can be fun and exciting for your teen to learn how to invest, and Roth IRAs are a great way to get an investing edge on retirement. But keep in mind there are also various levels of risk involved.

Some investment professionals say, "Let the kids make their investment mistakes young" with self-directed investment accounts hosted by a retail broker. Another option is to open the Roth IRA with a financial advisor so that the teen has a mentor they can call and discuss what is going on in the markets with.

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Be In Your Favor,
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