Creative

wealth maximization strategies*

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The Best Return-Boosting Strategy

MONTH	SCENARIO #3: 4% RETURN			SCENARIO #4: 15.84% RETURN		
	MONTHLY DEPOSIT: $1,600	4% RETURN MONTHLY EARNINGS	4% RETURN ENDING BALANCE	MONTHLY DEPOSIT: $1,500	15.84% RETURN MONTHLY EARNINGS	15.84% RETURN ENDING BALANCE
JAN	$1,600.00	$5.33	$1,605.33	$1,500.00	$19.80	$1,519.80
FEB	$1,600.00	$10.68	$3,216.02	$1,500.00	$39.86	$3,059.66
MAR	$1,600.00	$16.05	$4,832.07	$1,500.00	$60.19	$4,619.85
APR	$1,600.00	$21.44	$6,453.51	$1,500.00	$80.78	$6,200.63
MAY	$1,600.00	$26.85	$8,080.36	$1,500.00	$101.65	$7,802.28
JUN	$1,600.00	$32.27	$9,712.62	$1,500.00	$122.79	$9,425.07
JUL	$1,600.00	$37.71	$11,350.33	$1,500.00	$144.21	$11,069.28
AUG	$1,600.00	$43.17	$12,993.50	$1,500.00	$165.91	$12,735.19
SEP	$1,600.00	$48.65	$14,642.15	$1,500.00	$187.90	$14,423.10
OCT	$1,600.00	$54.14	$16,296.29	$1,500.00	$210.18	$16,133.28
NOV	$1,600.00	$59.65	$17,955.94	$1,500.00	$232.76	$17,866.04
DEC	$1,600.00	$65.19	**$19,621.13**	$1,500.00	$255.63	**$19,621.68**

When a financial professional says "Let's look at ways to increase the return on your savings," what comes to mind?

A. **Considering financial instruments with longer holding periods?**
B. **Increasing your investment risk?**
C. **Committing to a more active allocation strategy?**

Or…

D. **Getting a financial efficiency review?**

The setup gives it away. You should choose D every time. Improving your financial efficiency to "find" more dollars to save is almost always the best way to increase your returns (at least until you've built a sizable accumulation).

While you may conceptually assent to the superior results from a financial efficiency review, a mathematical analysis really hammers home the value. You just have to see the numbers.

The Math *(Oh My!)*

Scenario 1: Suppose you are currently saving $1,500 each month. Suppose also that your annual return on your savings is 4%, compounded monthly. (Standard disclaimer: This is a hypothetical situation, and the illustration does not assume the use of a specific financial instrument. It's just a numerical comparison; real-life results would likely vary.) This is a month-by-month progression of deposits and earnings.

Scenario 2: You make an adjustment to your allocation strategies that results in a 6% annual return; the earnings obviously increase. A 50% increase in return (from 4 to 6%) seems significant, but actual numbers are less impressive.

Over a year, the difference in return is slightly more than $200.

That's about $17 a month (also known as the price of an extra-large pizza with three toppings).

Scenario 3: What results might come from a review that cleans up some of your financial inefficiencies and "finds" additional savings? Could it be $50 a month, or maybe $100? Using the original 4% rate of return, let's *add $100 each month.* Obviously, bigger deposits will produce a higher ending balance.

Scenario 4: The difference between Scenario 1 and 3 is due almost entirely to adding $100 each month. But to illustrate the significance of bigger deposits, let's conclude with this calculation: What is the rate of return needed on $1,500/mo. deposits to equal the ending balance of $1,600/mo. earning 4%? Look at the return variable at the top of the table in Scenario 4.

This is the mind-blower: Scenario 2 would have to earn ***15.84%*** to equal the results of Scenario 3!

Between pursuing higher returns (Scenario 2) and increasing financial efficiency (Scenario 3), here are two relevant questions:

1. Which strategy is easier to execute?
2. Which strategy entails the least financial risk?

It is theoretically possible for either strategy to be the best answer to both questions. But for most households, the default choice should be to look first at becoming more financially efficient.

Can You Achieve Similar Results?

Financial efficiency in personal finance seeks to eliminate or minimize costly or overlapping expenses, and put more money under your control. Possible actions to accomplish this objective might include:

- Re-financing a mortgage
- Debt Consolidation
- Restructuring personal debt
- Adjusting deductibles on property and casualty insurance
- Evaluating allocations and employer matches in retirement plans
- Re-directing dividends or interest payments instead of compounding

Not all efficiency options may fit your situation, but it often takes only one or two to add up. In the example above, an extra $100 added to existing savings of $1,500 each month is an increase of less than 7%, which isn't much. So it's reasonable to think an assessment of your financial efficiency might yield similar results. And as the numbers show, increasing returns (usually through increased investment risk) to match finding an additional 7% to save, is usually a tougher challenge.

Granted, the returns from efficiency diminish as your accumulations get bigger. If you have $100,000 earning 4%, an increase to 6% is a $2,000 boost in earnings. Accomplishing the same increase with financial efficiency requires finding almost $200 each month, which might be a little harder (especially if you've already done a few financial "house-cleanings").

Having said this, finding ways to increase deposits remains a proven method for maximizing long-term accumulations while minimizing risk. And done right, a financial efficiency review is usually painless; the extra money that is saved doesn't diminish your lifestyle. It's money redeemed from waste. ❖

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