Fidelity Viewpoints®: Raising Money-Smart Kids

TRANSCRIPT

SPEAKERS:

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SEGMENT 1: Start the Money Conversation

Jim Armstrong: Hello and welcome to Raising Money-Smart Kids. Thanks for being with us today. I'm Jim Armstrong with Fidelity.

Since you've started watching this webcast, it's pretty safe to assume that you share our interest in helping to raise kids, teenagers, and young adults who start off life on a strong financial footing, so that's exactly what our goal is today.

And we're thrilled to be joined by Fidelity's Randelle Lenoir. She helps lead an investor center, a Fidelity branch just outside of Chicago. That means she and her team really spend pretty much every working day working with investors just like you and me, helping build long-term financial plans. But her not so secret passion is to help kids get started off on good financial footing as well.

So, Randelle, thanks again for making time to be with us today.

Randelle Lenoir: It's great to be here, Jim.

JIM: So, this segment of the webcast is really going to focus on younger kids, grade school age kids, for example. So, I thought we'd start the conversation off with an experiment that people can even do with the little kids in their lives if they want. It's called the marshmallow test.

Basically, what it involves is a researcher putting a little kid, six or seven or eight years old, in a room alone with a big, fat, fresh marshmallow. And the researcher says, I'm going to leave you in this room. Don't touch the marshmallow. Don't eat it. When I come back, if you haven't eaten it, you'll get two marshmallows.

Then they leave the room and you sort of watch how the kids behave and it's this mix of genuine and heartbreaking right as these little kids try to stare the marshmallow down and others just jump right in and gobble it whole.

But what they're after, Randelle, is really trying to gauge self-control, right?

RANDELLE: Right. I mean, this is a fun experiment and it's a great way to start the conversation about money with younger kids. Self-control is a way to teach delayed gratification or working and waiting for that big thing that you want. And it's similar to savings. Parents can explain when you save your money, you can earn interest which is extra money on top of what you started with. It can also relate to spending, right, so you can explain that you can spend the money now for something small or you can save your money to buy something bigger later.

JIM: Delayed gratification is quite a concept, absolutely, and I think underneath all of it, Randelle, is this idea of money having value, right?

RANDELLE: Right. You need to have the value conversation before you get into the money conversation because money is just a thing until you establish what it stands for first. So, here's an exercise that you can try at home. Maybe ask your kids to put a value on that drawing that they made. Ask them how much money they think their favorite toy costs. You can move on to a toothbrush, a book, things like that. That will help them begin to make that connection between money and everyday objects in their world.

JIM: Yeah. I love that idea, Randelle, because that connection, I think, is lost in a lot of ways these days. I'm thinking for example, my wife and I buy things online. So, if my kids are watching, they see us go to a website, type a couple keystrokes, and then a day or two later, the things show up on our front door. There's no—there's no connection for the kids to see how money is actually involved in that transaction.

RANDELLE: Right. These days, teaching kids how money works is not as easy as rolling coins on your kitchen counter and bringing them to the bank, right, but that might still be a great place to start. Maybe you can take the money in their piggybank and then show them how to deposit it into the bank. But you really can't graduate to the more complicated concepts of money without first understanding the literal nickels and dimes, right.

And also, to continue that exercise above, take the objects that your kids might find value in and put price tags on them. Give them some real money. Let them pretend to make purchases. Count out the money. Help them count out change. Give them a budget and ask them what they can buy with it. So, your kids will begin to understand that value piece that I talked about earlier.

And this helps lay the foundation for the tough stuff like digital money. I think it's really helpful to explain how the invisible transfer of money works. That is a big part of how money is transacted now. Think about it. I mean, you work. The money goes from your employer to your bank account. The money goes from your bank account to pay bills, to purchase gas, to buy groceries, so on and so forth. So, all of that happens without you ever touching your money these days.

JIM: Right. Exactly. It's all digital, right? It just—you never actually touch the dollars.

One thing I did with both of my sons is show them how to write a check which feels super old school. I mean, I barely write them anymore, but I wanted to show them how that process works. And then also with my younger guy, he was in the back seat last summer or the summer before I guess. I went to an ATM and he just—he told me that he really had no idea how it worked. He just thought it was a limitless supply of twenties that just keeps shooting out every time you ask for them, which of course he would think because he doesn't see that invisible transfer of my direct deposit going into the bank which allows me to take the money out.

RANDELLE: Yeah, Jim. That's a great point. While checks and even paper money are being quickly replaced by new technologies like payment apps, it's still really important that they get that concept. So, be sure to explain things like checks, ATMs, and payment apps too.

JIM: How about, Randelle, this idea of kids having their own money, because at this age, grade school, right, they're getting money probably for birthdays, holidays, other special events, allowance money, for example. Any tips on how to help kids manage their own money at that level?

RANDELLE: So, great question. When a child has his or her own money, it's important to teach that they have some choices here. So, they can spend it. They can share it. They can save it. Let's talk about spending.

So, try going to a toy store with instructions. This is how much you have to spend and now decide what you want based on that. Is your kid going to spend all of that money to buy one item? Maybe talk about budgeting. Convince them to consider buying a smaller toy and save the rest of the money for something later like ice cream.

And I think it's also really important to let kids do their own transactions. There's really something about participating in the activity versus hearing it or just watching it that is so much more valuable.

JIM: And builds that sense of independence. I completely agree. One thing that my wife and I have to be careful of is taking the kids to the toy store, say they've got eight bucks, and the thing they want is ten. I have to consciously sort of back away and not fill the gap with the extra two dollars because in my mind at least, that's not teaching them about exactly what you just described.

How about the next thing though, giving or sharing? How would you help teach that?

RANDELLE: Yes. I love the kids—the concept of teaching kids the importance of charitable giving when they're little. So, for me, my parents used to give me a little change to put in my purse when I went to church on Sunday for offering, right? And then when I got a little older, I got money of my own. I began to set aside 10% and that was my practice of giving to my community. And that's still a concept that stays with me today and that concept translated to savings really easily for me earlier on.

JIM: That's great. It's great to be that disciplined. But I want to ask you a question about savings too and sort of how you can make that obvious to a kid. So, child of the 80's. I used to have a physical passbook that I would take to the teller and she or he would sort of print out how much interest I had earned that month and I would make five or six dollars which was a big deal back then.

That is less and less an option for people these days. How else can you show that to children?

RANDELLE: Well, I think it's still a good idea to show kids something physical. So, you can show them a printout of a bank account or you can walk them through an account online. Show them the beginning balances, the ending balances, how interest grew on your savings account. And this technical stuff is necessary but the most important thing is discipline, saving early and often, even if it's just a little bit, can really be habit forming. And that can help them grow into an adult who can successfully manage their money.

So, a suggestion here is every time they earn allowance, have them separate a portion, maybe 10%, for a savings account. And the same would go for birthdays, holidays, or any other gift. Teach them that they can spend some now but always try to save some for later.

Another suggestion is automate the process. I mean, automation is such a key tool to financial success, right? So, instead of giving them cash for an allowance, maybe setup a direct deposit from your account to theirs for their weekly allowance. And then they can setup an automated savings account.

JIM: Oh, I love that. And then potentially that starts the foundation of teaching them that digital money that you were talking about there and how that can continue to grow and certainly digital money is the way of the future, right? So, it's what our kids are going to be dealing with as they turn into adults.

Great, great tips, Randelle. Thank you again for taking the time to explain all this today.

RANDELLE: My pleasure.

Segment 2: Teach How Finances Work

JIM: Hello and thank you for joining us for Raising Money-Smart Kids. In this segment of the webcast, we're going to be talking about key financial concepts for teenagers. Randelle, thanks for agreeing to lend your expertise to this part of the conversation as well.

RANDELLE: It's great to be here, Jim.

JIM: Let's—look, let's dive right in, right. We've all been there. We've all been teenagers. And we all know that in theory at least, that's the time of our lives when we're supposed to be picking up all those crucial life skills that will serve us well whenever we transition to adulthood. However, I think a lot of us figured out the hard way that when we got to college or started working, it wasn't always very clear to us how to make the best financial choices. Maybe we didn't pick up the skills we needed when we were teenagers.

A million different ways to approach this topic, Randelle. How would you start off helping a parent help a child understand what they need to know?

RANDELLE: So, I think credit is a great place to start. Teens have a blank canvas for their credit history which means they haven't made any mistakes yet. And I would love to help people learn about using credit safely while they still have the benefit of hands-on guidance from their parents.

So, the only thing I was told growing up was to avoid credit cards, right. And then I went off to college and what do you think is the first thing that I did?

JIM: Got yourself a credit card.

RANDELLE: I got a credit card. I remember it had a $2,000 limit. And I didn't know what I was doing. The problem with debt is that it can start out low and you think, no big deal, but then debt builds on itself and next thing you know, you're stuck paying it off for years.

JIM: And I think you can really understand a parent's impulse to say, if you can't afford it, don't buy it, end of story. But I think to your exact point, Randelle, that ignores the fact that when you use it responsibly, credit is a really, really valuable tool.

RANDELLE: Yeah, it is. And teens grow into young adults who may need to use credit for student loans or to buy a car, for example. Before they can sign up for credit cards or loans, they should understand how credit works. Teens may not understand that they have to pay back the principle amount, so the amount that they borrowed, and interest and maybe fees and monthly service charges on top of everything. So, borrowing money on credit has a cost.

JIM: Lots—right. Exactly. Lots of costs in there. Can you talk a little bit more about interest? I think that in particular probably trips some young adults up.

RANDELLE: Yeah. Later we'll talk about how compounding interest can be your friend when you're investing, but when you're borrowing, compounding can plunge you further into debt and teens don't always know this.

So, make sure they understand that carrying a debt in their credit card from month to month means that compounding is working against them.

Paying off your credit card in full each month is a way to help avoid this but it's not always possible. So, teach your teens that they should make at least the minimum payment each month so they can avoid late fees and avoid damage to their credit. And help them understand that they will have a credit score and a bad one means that they'll have trouble getting loans in the future or they may have to pay more for the money that they borrow in the future.

So, to make this simple, suggest automating that minimum payment each month and then encourage them to pay more as they have it. But they need to know that just paying the minimum can leave them in debt for years.

JIM: You know, one way I think that you can actually make this clear to teens in your life is just to show them a credit card statement of your own, maybe if you still get a paper statement, or pull it up online because they show you today sort of what you owe right now, what your interest rate is, what your minimum payment is, and then importantly, at the end, it shows you how much you owe if you only pay the minimum and how long it takes you and that can be really eye opening.

RANDELLE: Right. And here's an example. By paying just the minimum, a credit card balance of $1,000.00 at a 12% interest rate with a minimum required payment of $35.00 would take thirty-four months to pay off. So, your total payments would equal about $1,184.00, which means you'd pay $184.00 to borrow the money for nearly three years.

JIM: And by the way, 12% sounds pretty—like a pretty good rate. They get much higher than that.

RANDELLE: Yeah. I mean, the average rate for credit cards is 17% but it can be much higher. So, remind your kids that it can really pay to shop around for the lowest interest rate and even compare those annual fees too.

I also want to mention debit cards here because they can also be a great tool to help your teen manage their money and keep track of their spending. It's important to point out the difference between these cards to teens too because while we all know they look the same, they both look like plastic, they are very different.

JIM: Look, I think that's a great example that something as adults, we just take for granted, right. Intuitively, we get it, that they—that they function differently. But imagine sixteen, seventeen years old. You've got your first job. The difference between a debit and a credit card might not be intuitive.

RANDELLE: Right. And I'd explain it this way. Debit cards have made it so easy for teens to access their money, whether it's in a bank or it's in another account like a brokerage account. But they need to understand that that money comes out of their account. Very different from credit, right?

And if an account allows them to accidentally spend more than what they have, it could trigger an overdraft fee.

Many debit cards for teens, they also charge monthly and annual fees too, but a quick internet search can help you find a debit card that doesn't charge fees and maybe debit cards that also reimburse those ATM fees too.

JIM: Sounds good. I want to switch your attention now to a slightly thornier topic, right? Saving and budgeting. How would you approach that?

RANDELLE: Yeah, that's a tough one. Teens may have money coming into their hands more regularly at this point, right? Maybe they have an after school job. So, it's up to the adults in their lives to make sure that they see the options beyond just spending it all right now. And when it comes to savings, a little can make a difference. So, make sure your teenager understands this. Ten dollars a week after a year is more than five hundred dollars.

JIM: So, it's that—it's that concept of delayed gratification all over again, right?

How about budgeting, Randelle? I know that that's something that stumps even plenty of adults.

RANDELLE: Yeah. As a concept, yes, but that word, budget, can sound scary, so I have heard it described as a spending plan instead, or just think of it this way; it's a way to balance what's coming in, what's going out, and what you're going to do with the rest.

So, you can do this exercise with your teen. Write down how much money they have coming in. Maybe it's from a part-time job, birthdays, holidays, gifts, allowance, whatever it might be. Then write down what they owe or what they spend regularly. Is there like a weekly pizza night where all of their friends use payment apps to pay each other? Are they chipping in for the family cell phone plan? Which, by the way, if they aren't, I think that's a great way to teach responsibility.

And then next, what are they saving for? Prom? Are they saving for a used car? Books or housing for college?

And if your teen has something longer-term that they're saving for, please be sure to watch part three of this video where we talk about investing.

But this is your spending plan. And it's not scary at all. It's simply meant to be a guide to help you reach your financial happy place. And it can and will change as life does.

JIM: Thank you for that, Randelle. Just great habits to get yourself into when you're a teenager that again, can help you navigate when life gets a little more complicated as you grow up. So, thanks for taking the time to explain all of that with us today.

RANDELLE: My pleasure.

Segment 3: Explore Investing

JIM: Hello and thanks for joining us for Raising Money-Smart Kids. In this segment of the webcast, we're going to talk about the topic of investing for teenagers and young adults. And Randelle, I would like to start off with a bit of an experiment I did with my older son a year or so ago. I set it up like this. I said, today I can give you $1 million, or I can give you a penny, but that penny doubles every day for a month. So, a million dollars today or a penny that tomorrow is two pennies and then four cents after that. Which do you think he chose?

RANDELLE: The million dollars.

JIM: Oh, right, in like a heartbeat. He's like, I want the million today, which of course makes sense. Most people would choose it. But when I showed him the math, he could see that the penny on day thirty was close to $5.3 million. That was my attempt to teach him about compounding and I hope it worked.

RANDELLE: I love that example too. It's a quick way to show how interest can build upon interest. So, of course, there are no investments that I know of that will double your money every day, but the point is, money can make money. Compounding is a process that happens over time to your savings and investments. It's such a crucial concept for young people to understand. So, make sure they're clear that savings generate interest and that interest can also earn interest, kind of like that penny in your example but a little less dramatic.

Unfortunately, interest rates have been so low for so long that this number usually isn't very impressive in savings accounts, but when you invest, that snowball effect of compounding can be quite powerful, especially over time. If you make gains on your initial investments, you may reinvest that and then make gains on gains on gains and so on and so forth.

JIM: I think you're exactly right. I mean, that's the point. And you've got time on your side when you're younger which I think is part of the reason we're even having this conversation today, right?

RANDELLE: Right. And a simple example here. $100.00 invested at 10% earns ten bucks the first year. Then the next year, you've got $110 earning interest for you. That makes eleven bucks. And then in year three, you're up to $133.00 total. And inching up to $150.00 by year four. And when the numbers get bigger and you have more time, that's when compounding really does its work.

JIM: And once you sort of lay that foundation, I'm curious for your take on how to explain investing to young adults, particularly I think the difference between investing and trading. I mean, investing is certainly for the long-term, long-term goals, whereas trading can be a lot more short-term.

RANDELLE: Yeah. And any conversation about investing and compounding with a teen or young adult, I always say, invest early, often, and you can start small.

Definitely make sure that they understand the difference between investing and trading, investing being more of that long-term thing and trading being more of that short-term.

I heard a great analogy that helps us understand how these two words are often confused and people use one to talk about the other. So, one of my coworkers recently gave me this.

Investing is like barbecue and trading is like grilling. When you barbecue something, you cook it on low, indirect heat for hours and hours and time is a key factor there, right?

When you grill, the process is quick and you'd better be paying attention. If you walk away for too long, you burn something, right? So, with grilling, your undivided attention is what matters.

Now, you take those concepts and apply it to investing and trading. In both cases, you buy shares of stocks, bonds, or other investments, and your goal is simple; you want to make more money than what you started with.

The major difference is how much time and attention you put into the process. So, with investing, you're going to typically keep your shares for a long period of time. That's where those terms buy and hold and long-term investing come from. With investing, you should have a general idea of what's going on in your accounts, but looking at your account every day or updating that app isn't really going to serve you well.

JIM: It doesn't help. It does not help.

RANDELLE: Not very much, right? But with trading, on the other hand, you need to be actively involved. Again, this is a short-term process.

I have heard people say to be a trader, you need to have the skill, will, and time to focus on those stocks. You need to be following the market daily, sometimes even hourly to keep up on the news constantly. Which CEO got fired? Which company is buying what other company? Is the market rocky? How do you feel about it? Right? It's just like grilling. You need to pay close attention to what's going on when you trade.

JIM: I love that. That's a great way to help keep the two things separate as they should be, Randelle.

I know where some kids get confused and some adults, for that matter, is kind of getting overwhelmed with all the investment options they have, right? They know they want to have some long-term investments but they're not sure even where to begin. How do you help sort that out for young adults just starting out?

RANDELLE: Listen, there are many ways to invest and you might use one or maybe all of these ways. Here are a few topline, key points.

You have self-directed investing, retirement plans, and managed accounts. So, self-directed investing means you do it yourself. So, when you open an account like a brokerage account, you do the research and you make the decisions about where you want to put your money. And one way to dip your toe in is to buy fractional shares. This means you can buy a fraction of a stock or ETF based on the dollar amount that you want to spend. It's kind of like buying pizza by the slice rather than buying the whole pie.

And then there are employer retirement plans which go by names 401(k) or 403(b)s. It's important to talk to young adults about the importance of starting to fund their retirement as soon as they can, and especially when they work for an employer that will allow them to make contributions through their payroll. And many employers will offer a match which is essentially free money on top of the money that they're already putting in. So, don't let your kids miss out on that match.

And then finally, there are managed accounts. So, there are some accounts managed by professionals. There are accounts managed by algorithms called robo advisors. And there are hybrids of the two concepts as well.

JIM: Lots of choices there. I think—I'd love it if you could talk a little bit more, Randelle, about the value of having time on your side, because again, I think that's what brought a lot of people to this webcast is how can they get their kids started off early to take advantage of the long time horizon they have in front of them.

RANDELLE: Yeah, so I have the perfect example to illustrate what can happen over decades of investing. In fact, I love to show younger people this who are just starting out in the workforce just to see the look on their faces.

So, for younger people, lump sums can be scary. Saving a thousand dollars might seem intimidating or unreasonable for where they're at, but when you break it down to $20.00 a week, it suddenly feels more accessible. In over fifty-two weeks, you've actually exceeded your goal. So, onto the example.

You have Michelle and Joseph. They're both saving into their company's 401(k). Michelle is thirty-five and she contributes $5,000.00 a year. That amount includes what she puts in and her employers match. And at a hypothetical rate of return of 7% each year, Michelle accumulates close to $800,000.00 by the time that she's seventy.

JIM: So, pretty good.

RANDELLE: That's pretty good. That's pretty good. But listen to this. Michelle's coworker, Joseph, is twenty-five and he's also investing in his company's retirement plan. Same exact scenario except Joseph started investing ten years earlier than Michelle, so he has more time to benefit from that power of compounding which should allow his savings to more than double Michelle's, to more than $1.6 million.

Now, we understand not everyone can invest that much, but it's important to encourage young people to start early because they cannot get that time back. The earlier that you start investing, the more compounded returns you can hope to make.

JIM: So, the earlier part of the early and often makes sense. How do you do the often part? How do you have that make sense as well?

RANDELLE: Yeah. I talk to my customers about a simple but effective technique known as dollar cost averaging. It means investing the same dollar amount every week, month, or quarter. So, over time, the amount that you invest will buy more shares when the price of an investment or fund is low, and it'll buy fewer shares when the price is high.

The good thing is, if you invest in a 401(k), you're already using this strategy. So, dollar cost averaging works best when the markets are choppy because you get a lot of opportunities to buy more shares while they're cheap. And it's important to know that dollar cost averaging doesn't assure a profit or protect against any losses in a declining market, but it's a time tested strategy that can work well over the long run and it's easy to automate.

JIM: Randelle, in just a few minutes' time, you've been able to pack so much great information into this webcast. So, I just wanted to say thank you again for taking the time to be with us.

RANDELLE: Thank you for having me.

JIM: Absolutely. Absolutely.

And for the folks watching, we hope that this conversation is able to kickstart or support conversations in your own homes with the young people you care about, again, with the goal to help get them off on a solid financial footing.

If you feel like you need more information to continue the conversation, by all means, check out Fidelity's website or download our app, and you can do keyword searches on any of the topics we talked about here today to continue the conversation.

And of course, finally, if you yourself have questions about building your own financial plan or updating your current plan, by all means, give us a call and one of our representatives can talk to you about how to get that done.

Again, thanks for taking the time to be with us today and we hope to see you soon.

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