

Your Best Investment

Mary Rowland Personal Finance Column – September 2007

Question: What is the quickest way to improve your personal balance sheet and your net worth?

1. Invest in the stock market.
2. Buy a home.
3. Pay down debt.
4. Invest in foreign currency.

The correct answer is 3. No matter your age or financial situation, paying down debt is always your best investment. You get a guaranteed return of whatever the interest rate on your debt happens to be. If you owe credit card debt at 18 percent, you get an 18 percent return. Not maybe. Guaranteed!

For Younger Members Just Starting Out

What if you're just getting started, working to build your career and trying to save money for future goals? Build a good credit history. This history will be used to determine whether you get a job, get approval to rent an apartment, to buy a car or a home, as well as how much you will pay for each of these things.

The credit industry has grown, automated and consolidated. All your financial dealings are pulled together in one giant computer database and you are assigned a score that is used to determine whether you can rent an apartment or get a mortgage.

Of course, the score includes how you handle credit and how reliably you pay your bills. But it also includes seemingly random factors such as how much education you have, how often you change jobs and how often you change addresses. This means that rather than looking at your individual history, you get thrown into a pot with other borrowers. You want to look like the ones who repay their bills.

Get two major credit cards. Be certain each card has a low interest rate as well as a grace period, which is the length of time you have to make your payment before interest is added. Decide how you will use the card. To keep tax records or business receipts? Aim to pay off the entire balance before the due date. Making only the minimum payment means you will rack up thousands of dollars in interest.

For Mid-Career Members

Suppose you are entering your prime working years, the most difficult stage of your life to keep credit under control. Demands on your cash are great at the same time you aim to sock away money for college and retirement.

You are entitled to one free credit report and credit score each year from each of the three credit bureaus. So much depends on your credit score that you must know yours and, if necessary, improve it. This can be tricky business because of the myriad online offers for a "free credit score" and for help in raising this score. Most of these offers come from scoundrels hoping to make money from your ignorance. Do not fall for it. Do not pay anyone to "watch" your credit or to send you alerts. These folks are preying on your fears.

Instead, keep abreast of important changes yourself by going to a free online information service like gerridetweiler.blogspot.com. I've known Gerri, author of several credit handbooks, for more than ten years. She is an honest consumer advocate who works to help people avoid scams and schemes.

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If you carry a debt overload, pay it down, beginning with the highest interest rate card. If necessary, get help from a reputable credit counseling service to schedule payments. If your credit history seems hopeless, consider a secured credit card, which means that you deposit money in a bank and borrow your own money and repay yourself for the strict purpose of rebuilding your credit.

For Pre-Retired and Retired Members

Maybe you are approaching your golden years and your financial life is perfect: You are debt-free. Pension income will total 70 percent of your full salary. In your dreams!

Retirement is supposed to be a stress-free time to enjoy our years of hard work. But then children's college bills come in higher than expected. A family health problem soaks up the money we've set aside. Or an expensive mid-life divorce topples us.

Don't despair. You still have time to turn things around. Aim to pay off all your credit cards, home equity loans, car loans and the like as well as your mortgage before you retire. That gives you the flexibility in using your monthly income for necessities.

Take a look at how much equity you have in your home and decide how you will use it. Does it make sense to sell your primary residence and take advantage of the \$500,000 tax-free gain you get under current tax laws? Or to take out a reverse mortgage to draw the equity out of your house for living expenses?

Your credit goal should be to reduce the number of credit cards you hold to only two or three general purpose bank cards. Charge as little as possible and pay off the balance each month. At this point in your life, you still need a good credit history and a good credit score to give you flexibility should you want to borrow money to start a business, for example.

Conclusion

Whatever your stage of life, you must use credit—whether you like it or not—in order to establish yourself as a responsible person who can be trusted. But remember that credit can be a double-edged sword: It can give you the freedom to buy something now even though you don't have the money yet. But it might also mean that you will be paying for the take-out Chinese you ate in college when you're 45 years old with three kids.

Mary Rowland is a nationally known business and finance writer. The former personal finance columnist for The New York Times and former co-host of a nationally syndicated radio show, Ms. Rowland is the author of several investment books and speaks regularly to consumers and financial planners about investing and personal finance.