Happiness Equals…

By Tracy Broeze, CFP

It's an interesting concept that financial planning has a lot to do with happiness, both current and future, and I'm always amazed at how different people are in this regard. Some people don't need much in the way of material wealth to define them as happy. Others choose more lavish lifestyles.

Neither end of the spectrum is necessarily wrong although you'll hear both sides criticizing the other. The frugal among us often point fingers and analyze cash leakage while justifying their own careful spending or lack thereof. The more extravagant disdain stinginess and prefer to live their short lives in what they perceive as greater comfort.

I think that each person should come up with his or her own definition of happiness and strive to apply it at every opportunity with a cautious and trusted third party to help balance the definition. This is where a financial planner can really make a difference.

The value of time and compounding can be dramatic so you will often hear your advisor saying to contribute early and often, no matter what amount you decide you can manage. Here's an example. If you contribute $100 per month for 5 years and earn a return of 5% per year, you will have $6800 at the end of 5 years. If you contribute $50 per month for 10 years and earn a return of 5% per year, you will have $7764. Same net invested, but an increased account value, all because of time. (Young people, pay attention!)

The reverse of the time value calculation above is also true. For example, in most cases, it is necessary to own a car but let's assume that you were convinced by the aggressive salesman to buy a more expensive car than you had planned on. Let's say you spent $5,000 more than you had budgeted for. If you had stuck to your plan and saved $5,000 and it earned 5% per year until retirement in 15 years, it would then be worth $10,394. That is what the 'up-selling' actually cost your retirement.

(Note: Neither of these calculations takes tax into account, but that's another topic!)

The amount that you decide you can manage to save or spend should take into account both current and future financial needs. Be 'in the moment' but make sure you also consider your future. The average life expectancy is higher than ever before and, statistically, we are more likely than ever to survive major health events even though they will probably disable us. So how short will your life really be? It's a question that no one else can answer for you.

I think that the best definition of happiness I have come across is this:

Happiness = Reality divided by Expectations

This was quoted recently in a popular book but was actually coined by Dr. Alden Cass as the economics of happiness. I don't think that there are many among us who would disagree that money provides, if not happiness, at least comfort. So, as my dear mother used to say, "If you don't work, you don't eat".

We can apply the economics of happiness in the following manner: If the reality is that your income <u>does not</u> exceed your expectations of what life should be like, then you will likely be unhappy, (and in debt). Conversely, if your income exceeds your expectations, you will likely be, well, let's say comfortable, and more likely to be happy. This is the secret of having a financially comfortable life now and retirement.

I am often asked how much should be set aside for retirement and I always reply: it depends on your expectations. Finding the balancing point between saving and spending, both now and in retirement, hinges on your personal reality and expectations. So ‘keep it real’ and talk to your financial planner.