

Retirement plan contributions: The strategy of time

As a retirement savings vehicle, the 401(k) plan offers a host of benefits. Contributions are tax deductible, and the earnings on your contributions grow tax deferred until you begin making withdrawals. What's more, the amount that you can contribute has been raised steadily. In 2007 you can set aside \$15,500, and if you are age 50 or older, \$20,500.

It's obvious, then, that most people recognize the importance of contributing to their company's retirement plan. But what many people may not realize is the importance of the timing of their contributions during their employment years.

A short story about the long term

Two friends, both 30 years old, are employed by the same company.

Faith starts making \$35 contributions to the company plan each week and continues to do so until she leaves the company ten years later (a total contribution of \$19,200). At that time she elects to keep her money in the plan, not withdrawing the money until 25 years later, when she reaches age 65.

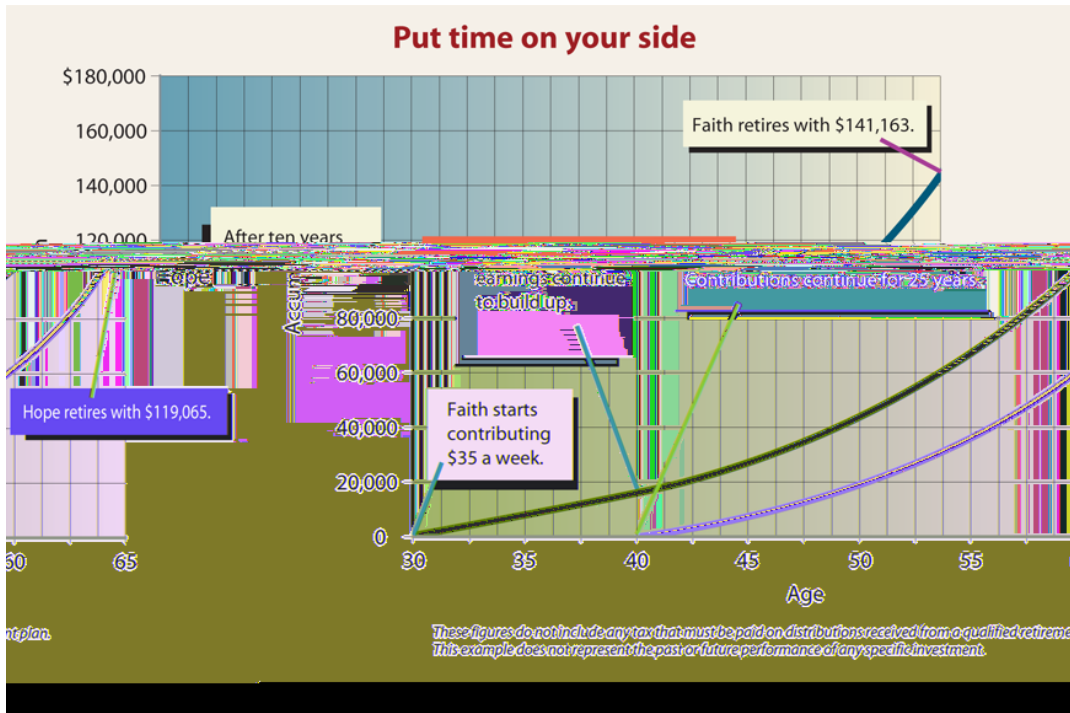
Hope initially makes no contributions to the plan. However, ten years later, just when Faith leaves the company, Hope decides to begin making contributions in the same amount (\$35). She continues to make contributions for 25 years, until she reaches age 65 (a total contribution of \$48,000).

Can you guess who has more in her retirement plan (assuming that they both earn 7% a year on their investments)? Would you be surprised to find out that, although Faith made contributions to the plan for only ten years to Hope's 25 years, Faith has \$22,098 more in her account?

Don't be. What you're seeing is the power of compound earnings. The benefit of ten extra years of tax-deferred earnings from her company retirement plan is the reason why Faith can put in less and come out with more in the end.

The bottom line

As the illustration below clearly demonstrates, it's not only how much you save, but it's also *when* you begin saving. Of course, saving and investing for retirement are important at any age. But time favors those who are now in their early working years, offering them a golden opportunity to secure a financially comfortable retirement for their golden years.



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Any developments occurring after January 15, 2007, are not reflected in this article.