YOUR FINANCES
Saving For Retirement

6 Tips For Pumping Up Your 401(k)'s Balance

Key steps for building a nest egg include not stealing from yourself

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401(k) plans are about to celebrate the 40th anniversary of their enabling legislation. Chances are you've got access to one. But how can you get the most out of it? To maximize your retirement savings, follow these six 401(k) retirement planning tips.

"You only have one working career, one shot at building your retirement savings," said Judith Ward, a senior financial planner for T. Rowe Price. "You don't get a do-over. So you've got to make the most of the time you do have."

Start now. "Whatever you can do, do it now," Ward said.

Time is money, and the power of compounded earnings is one of your best tools for amassing retirement savings.

Suppose you are earning $40,000 a year at age 25. Let's say you win 5% annual pay raises until age 45, then 3% raises until you're 65, and that along the way you kick in 6% of your pay yearly. Further, let's say that your investments earn a 7% annual rate of return on average.

By age 65, your 401(k) retirement savings account will be worth a little more than $1 million, according to T. Rowe Price calculations.

But what happens if you wait until age 30, when your pay is $50,000, to start saving? You sabotage your own retirement planning. By age 65 your nest egg is only worth just over $825,000.

Save enough. "Many people agonize over their investment choices," Ward said. "But your deferral rate is the most important factor affecting your retirement savings total."

Many 401(k) plans' members set aside 3% of their pay. Instead, you should start with a contribution rate of 6%, Ward says. Aim for 15%.

Remember our example of a 25-year-old who saves 6% of his or her pay, ending with a balance of more than $1 million?

If he contributes 15% of his pay instead, he'll be sitting on a $2.6 million nest egg by retirement at age

65. Sweet!

Grab your company match. This is another way of aiming to save enough.

Fidelity Investments Vice President Meghan Murphy, a retirement planning expert, says a company match is like a pay raise. No sensible person would turn down a pay raise. So if your company is willing to match up to, say, 5% of your pay, you should contribute enough to win that full match as part of your retirement planning.

"The average match is 4.5%," Murphy said. "If you put in the same amount, your total is 9% of your pay, which will grow much more than 3% or 4%."

Increase your contribution rate. If you don't think you can afford to contribute 15% at first, start with less, then increase it over time.

Suppose that 25-year-old increases his contribution by one percentage point a year until reaching 15% at age 34, then sticking with a 15% annual contribution rate. His ending balance at age 65: $2.3 million.

"Those one-percentage-point increases are a pretty pain-free way to get your deferral up to a good number," Ward said.

Invest wisely. "Invest in age-appropriate funds," Ward said.

Target date funds can do that for you, Ward says, if you don't want to do your own research. The manager of a target date fund picks the stocks and bonds in its portfolio, and decides when to replace them with other securities over time. The fund manager adjusts the mix of stocks and bonds over the years as you approach your retirement target date, sometimes adjusting more even afterward.

The fund aims to become more conservative over time. It aims to dampen volatility as you approach and enter retirement. It does that by decreasing the percentage of stocks it owns and increasing the portion of bonds and cash in its portfolio.

Don't steal from yourself. That means don't take loans except for the most desperate emergencies.

To pay for things like car repairs and home maintenance, start a separate savings account, Murphy says. If you take the money from your 401(k) account, the money stops growing for your retirement. And you'll have to repay it with interest.