

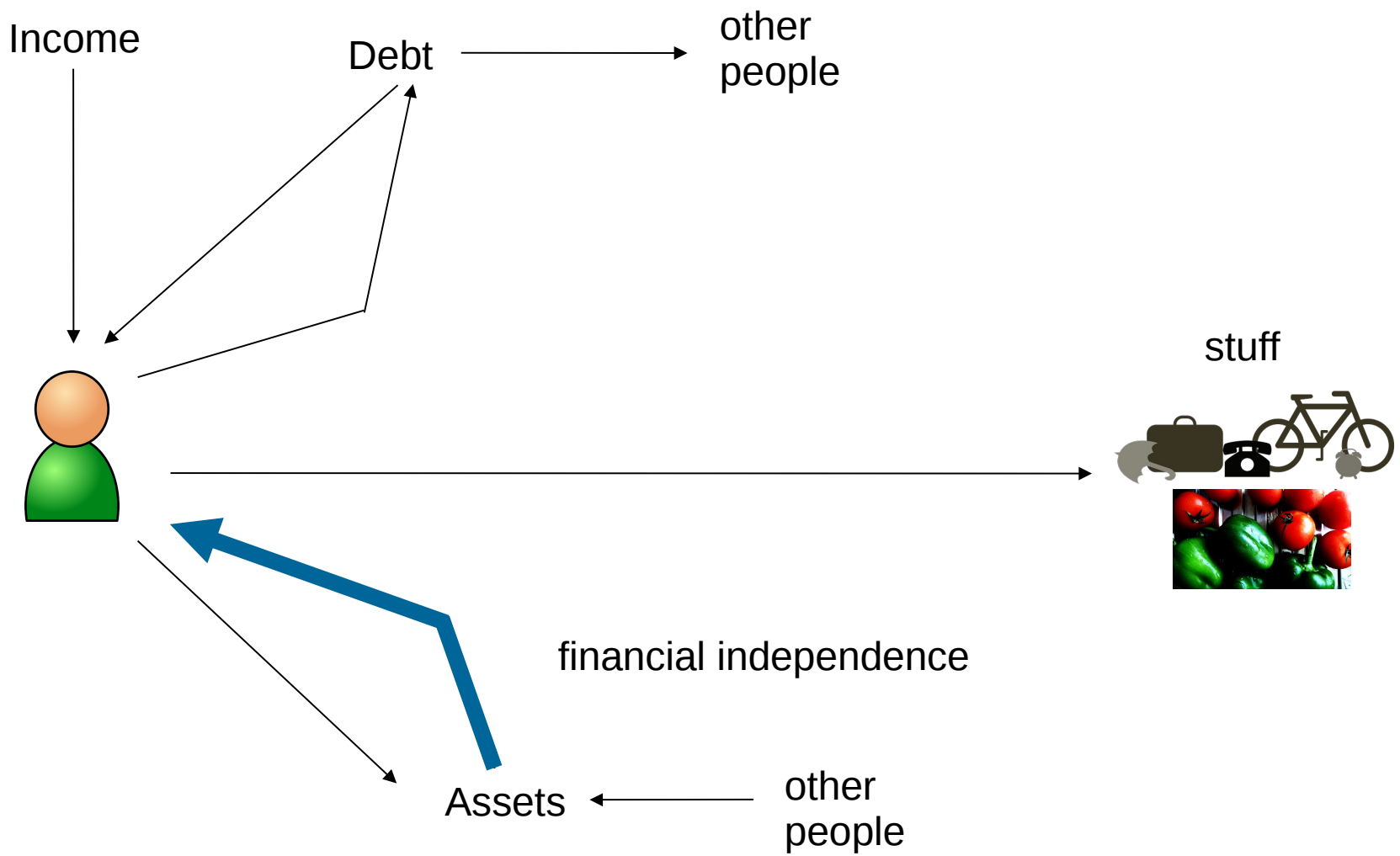
Saving and financial independence

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Learning objectives

- Define financial independence
- Describe spending and saving ratios
- Model path to financial independence
- Distinguish between needs and wants
- Describe benefits of financial independence

Money flows



Money flows over time

Quiz 1

How many years does it take to reach financial independence under these conditions?

Financial independence:

asset returns \geq spending

Control variables

- Rate of return
- Savings rate

Needs vs wants

Continuum: an example of shelter

Outside

Tent

Car

Mobile home

Shared room

Solo room, shared quarters

Solo apartment

Shared house

Solo house

Mansion

 Pay yourself first

 Lifestyle inflation

Quiz 2

If you have a 50% savings rate, how many years does it take to reach financial independence?

Model caveats

Time increasers

Some money in cash

Limitations of tax-advantaged savings vehicles

Variability of rate of return

Time decreasers

Your income is likely to grow

Rate is relatively conservative

Benefits of financial independence

Insulates from job market ups and downs

Reduce or eliminate financial anxiety

Enhanced ability to remain ethical in the face of financial incentives to do otherwise

Opens options for more rewarding but less remunerative occupations

Reduces downsides from taking risks on new ventures

Additional reading

The Millionaire Next Door: The Surprising Secrets
of America's Wealthy

by Thomas J. Stanley

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