4 Keys to the Millennial Balancing Act of Paying Off Student Debt and Saving for Retirement

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The financial puzzle for millennials: What's the best way to pay off student debt while saving toward retirement? Here are four steps to a sustainable plan.

Millennials really like the idea of retiring early. In fact, when Charles Schwab surveyed 2,000 millennials aged 16–25, the average age at which they expect to retire is 60 years old. That is a whole seven years earlier than the current Social Security full retirement benefit eligibility for their age bracket and several years earlier than the average retirement age.

Moreover, based on the average millennial's saving patterns, this goal of retiring early is not entirely realistic. According to the National Institute on Retirement Security, approximately 66% of people aged 21–31 have nothing saved for retirement. Meanwhile, Fidelity found that as of the second quarter of 2018, the 33% of millennials (aged 21–37) with 401(k)s who *are* saving for retirement have an average balance of $25,500 and contribute 7.3% of their income. Although these young adults as a group are putting more money away for retirement than they were five years ago (when millennials had an average balance of $13,100 and contributed 5.9% of their income), it appears that most of them will not be on track to retire in their early 60s.

The other challenge facing this generation is the inordinate amount of student debt that they are shouldering. Essentially they face a perfect storm: large amounts of student debt and limited job prospects when they first graduated high school and college, along with unrealistic expectations and a lack of preparation regarding their future responsibilities.

What should millennials be aware of when saving for retirement?

According to research from LendEDU, more than 25% of millennials aged 22–37 spend more on coffee (Starbucks, anyone?) than they save for retirement. Unfortunately, this decision to put off saving for retirement may have drastic consequences in the future. Because although retirement may be decades away for millennials, they are not creating habits that lead to long–term financial success.

Moreover, due to the financial crisis, millennials already have an uphill battle to climb when it comes to saving for retirement. For instance, people aged

25–35 possess less wealth relative to their income than their baby boomer and Gen X forerunners did at those ages. Additionally, millennials need to be extra careful when planning for retirement in comparison with their predecessors because they can expect to live longer, meaning the money needs to last for a longer time.

Compound this with the fact that Social Security is underfunded and medical expenses in retirement are projected to cost hundreds of thousands of dollars, and millennials need to realize that they will have more responsibility for generating their own retirement security than prior generations. Here are the four things that every millennial should be thinking about.

1. The big dilemma: Should millennials pay off their student debt or save for retirement? Answer: Yes!

One of the biggest dilemmas that millennials face when planning for their financial futures is the choice between saving for retirement and paying off student debt. With outstanding student loan debt in America affecting 45 million borrowers and totalling approximately $1.6 trillion as of 2019, student loan debt is a huge obstacle when it comes to securing a sound financial future.

According to a 2018 study by the Center for Retirement Research at Boston College, millennials without student loans have saved nearly two times as much for retirement by age 30 as college graduates who have taken out student loans. This results in $18,200 in retirement savings for college graduates without loans at age 30, compared to $9,100 in retirement savings for college graduates with an average student loan balance of $16,230 at age 30.

Interestingly, even if the debt is small and the student loan payments are manageable, the existence of the debt can be enough to curb saving. In short, many millennials with student debt are prioritizing paying off the entirety of their student debt before saving for retirement, which is not always the smartest choice.

In fact, because student loan debt often has relatively low interest rates compared to other kinds of debt, it can be smarter to both pay off the debt and save for retirement by making the minimum payment on student loans every month while also contributing toward retirement savings. This way millennials can both pay off their student loans and benefit from the power of compounding through investing.

2. Millennials should consider refinancing their student loans.

Over 44 million Americans hold student debt, and many may benefit from refinancing that debt. Refinancing student debt means swapping federal or private student loans for a private loan with a lower interest rate. This helps millennials because refinancing student debt for a lower interest rate decreases the total amount of money they would pay over the lifetime of their loans. Some online lenders known for providing good deals to candidates with healthy credit scores are Social Finance Inc., CommonBond, and First Republic Bank. Even in this climate of rising interest rates, finance expert Robert Farrington confirmed in *Forbes* that certain millennials can still benefit from refinancing.

However, there are also cons to refinancing that millennials must weigh. For instance, federal loans allow borrowers to make smaller payments with more flexibility if they cannot make payments. Switching to a private program will remove that safety net.

Therefore, people who do decide to refinance with a private lender should make sure that they have a small safety net of their own in the form of an emergency fund that could cover all their bills, including student loans, for a year. Candidates should weigh benefits (like an interest rate reduction) against detriments (like income-based repayment) when deciding whether to refinance.

3. Millennials should contribute the maximum amount to their 401(k)s

In general, millennials should contribute the maximum amount of their income possible, ideally at least 10%, to a retirement account or 401(k). Although the exact number and percentage will differ from person to person, at the very least, millennials should insure that they are contributing enough to obtain the employer match as that is essentially doubling your money right away. And as they get raises and bonuses, those should be designated immediately to a retirement savings account. You won't spend it if you don't have it!

In 2020, workers under age 50 can contribute a maximum of $19,500 to 401(k)s and $6,000 to a Roth IRA or traditional IRA. And because millennials may be in the lower tax brackets, they may consider contributing to a Roth 401(k) (instead of the traditional) at their employer as that will enable them to build their Roth nest egg for the future. And the same goes for the IRA contributions, i.e., they should consider contributing to the Roth IRA so that they can build that Roth nest egg.

4. Millennials should plan to have 10 times their final salary in savings.

According to Fidelity, a good goal for millennials is to have 10 times their projected final salary in savings (assuming retirement at age 67). Assuming that a person saves 15% of their income annually beginning at age 25, invests more than 50% on average of their savings in stocks over their lifetime, retires at age 67, and plans to maintain their preretirement lifestyle in retirement, Fidelity suggests the timeline below.

- By age 30: Have the equivalent of your starting salary saved
- By age 40: Have three times your salary saved
- By age 50: Have six times your salary saved
- By age 60: Have eight times your salary saved
- By age 67: Have ten times your salary saved

Although every person is different when it comes to planning for retirement, Fidelity's basic plan provides a simple guide for millennials to go by.

In conclusion, millennials face many challenges on their path to a financially secure future. Although retiring at age 60 is not in the cards for many millennials at this time, realizing a financially stable retirement can be. In order to solidify the dream of a prosperous retirement, millennials must follow the simple steps set forth above and start planning and investing now for their financial future.

Debra Taylor, CPA/PFS, JD, CDFA, writes on tax and retirement planning for Horsesmouth, an independent organization providing unbiased insight into the critical issues facing financial advisors and their clients.