Compounding not Confounding: Shoeing the Way to Savings

As both an aspiring businesswoman and the victim of an insatiable shoe fetish, it is essential that I save for the future. By initiating my savings as a teenager, I will avoid the uncomfortable situation of having to choose between paying rent or purchasing a pair of Manolo Blahniks. I recognize that shoe-frenzied females like me have hurled America into a downward cycle of over-consumption and negative savings rates. Luckily, however, I have had access to an economics education which has made me aware of the significant advantages of youth savings. I intend to reverse the American trend towards over-spending by investing early. By placing the capital I would have otherwise spent on shoes in long-term investments and compound savings accounts, I will ultimately enjoy a higher quality of life.

The earlier I begin to save, the greater the number of compounding periods my savings will undergo. Even an initially small deposit can grow into a large accumulation of capital if it is compounded enough times. By postponing my savings, I would decrease the number of compounding periods and thereby diminish the efficacy of compound interest. In order to compensate for my late start in savings, I would have to place a greater percentage of my disposable income into a compound account annually. For example, if, at the age of eighteen, I agreed to forfeit four pairs of Kate-Spade stiletto heels annually, I would have one thousand surplus dollars to invest in savings. Assuming my savings account had an annual return of 10%, and I continued to invest one thousand dollars each year, for five years, I would amass $489,504 in this account by the time I turned sixty-seven (Feinstein 29). If, however, I spent my twenties in reckless sandal, heel, slide, sneaker, boot and loafer consumption, I would have to contribute a much greater percentage of my disposable income annually in order to acquire the same overall amount of savings by the age of sixty-seven. In fact, even if I invested one thousand dollars each year from the age of twenty-eight to sixty seven into an account with identical annual returns, I would ultimately save only $486,852. Thus, in scenario one I put in a total of $5,000 and ended with a return of $489,504 after forty nine years of compounding. In scenario two, I put in a total of $40,000 and ended with a return of $486,852 after thirty nine years of compounding (Feinstein 31). By denying myself twenty pairs of designer shoes from the age of eighteen to twenty-three, I ultimately saved $37,652 more than the profligate twenty-something shoe-maniac of scenario two. Thus proving that time is money.

Diversification of savings will help me maximize the security of my investments. As with shoes, it is essential that I diversify my options. Municipal bonds, like work boots, are a low risk, low yield essential. They are issued by the government and therefore earn interest while being exempt from federal taxes. Much like work boots, municipal bonds are a durable, stable investment with a guaranteed returns (Stiglitz 347). Compound interest accounts are much like vintage Chanel satin pumps- they gain value each year. Another way in which to expand ones savings mechanisms is to invest in the stock market. This type of investment is much like buying a pair of Gucci platforms. Although risky in the short-run, cyclical fashion trends and national economic growth suggest that both platform shoes and diversified stock portfolios will ultimately bring positive returns (Siegel 41). Finally, Roth IRA accounts are much like a shoe-buffing kit. There is a price limitation on how much one can possibly spend on each commodity annually, and while Roth IRAs are tax deferred, shoe-buffing kits defer the taxing effects of overuse. Both Roth IRAs and shoe-buffing kits help people save money. Roth IRAs are tax exempt, and shoe-buffing kits allow their owners to get more wear out of their aging shoes. Thus in savings, as in shoes, it pays to have a variety of investments. Both the economy and the fashion industry are capable of fluctuation, which supports the concept of varying ones investments. In conclusion, diversifying my savings vehicles will allow me to establish a very secure economic portfolio and avoid excessive exposure to a single source of risk.

By beginning to save at a young age, I will develop healthy, life-long, financial habits. The small sums of money that I put into savings now will continue to compound until they have grown into a significant figure. By sacrificing the shoe purchases of today, I will benefit from greater returns in the future. The money I put in savings accounts now, will prevent me from being reduced to the "old woman who lived in her shoe" as the song goes. This small amount of capital, through compound interest and investment diversification, will raise my quality of life in the future.

Bibliography Emily Tiernan

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