

Should You Pay Off Debt or Save for Retirement? – Video Transcript

Should you pay off debt or invest through your employer-sponsored retirement savings plan?

That's an excellent question. Paying off debt and investing for your future are both very important financial goals. However, the answer is not an easy one – and what's right for one person may not be right for another.

There are several points to consider. Basically, the answer boils down to how your money can best be put to work for you.

Let's take a closer look at each point.

Point one is debt interest rate versus potential investment return.

When you make extra payments on a specific debt, you are essentially earning a return equal to the interest rate on that debt. For example, if you're paying a credit card with a 14% interest rate, you're basically getting the same benefit as if you invested that money and earned a 14% return on it.

That rate of return would be very difficult to match in your retirement savings portfolio on a long-term, steady basis. So if you're carrying a balance on a high-interest-rate credit card, your money may be best put to work paying down that balance.

On the other hand, if you're considering paying down a mortgage with a low interest rate, say 4%, versus investing extra money in your retirement account, the potential long-term returns earned on your account may outweigh the benefits of shaving a few years off of your mortgage.

Of course, there may be other reasons to pay off your mortgage, such as entering retirement debt-free – which is also a smart financial goal.

So the key is to think carefully about potential returns versus debt interest rates, in relation to your overall personal goals and circumstances.

The second point is whether you get employer matching contributions on money invested in your plan account.

Employer matching contributions are free money and increase the potential growth power in your account. If your employer offers a matching program, try to contribute at least enough to take full advantage of it.

But even if your plan does not offer an employer match, the tax benefits of plan participation and the long-term growth potential of even small investment amounts make contributing to your plan a smart financial move.

Which brings us to our last point: It doesn't have to be an all-or-nothing proposition. With a little budgeting and financial discipline, you may be able to both pay down debt *and* save for retirement through your employer-sponsored plan.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.