Should You Buy a Car or Fund Your 401k?

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From the birth of the era of qualified plans (401k's, IRA's and alike) they have been touted as the premier way to secure a fantastic financial future. Since that birth over 30 years ago every financial planner in the country will tell you the same old advice. It goes something like this "Well Joe you should put money away for retirement and take advantage of your 401k at work and max out your contributions every year. You should also make sure you get the match from your employer if they are offering one to make your account grow even faster. Not only are you saving for retirement Joe but you are also going to get a nice tax deduction for your contribution so why wouldn't you fund your 401k?"

Well Joe let me tell you that advice that sounds so good and so simple is also a bunch of bunk! Let's break down all the flaws with this advice and then talk about a better alternative. First of all by funding your 401k you are giving control up of your money and entrusting it to Wall Street (where most of the money gets invested) and to Uncle Sam. Once the money is in the plan it is very difficult to access without penalty or tax. This is all by design so you won't touch the money. The government will tell you this is for your benefit so you keep it growing for retirement and don't spend it on something silly like a car. We are about to prove to you that in fact you are better off buying your car than funding that 401k but let's not go there just yet. Let's finish blowing this 401k myth out of the water.

On top of losing control who are you losing control to? Wall Street and they have robbed more people blind than can be counted. You are also giving up control to Uncle Sam. The only person that is a better stealer of money than Wall Street is your old Uncle Sam. I just have to mention two words to prove this point…Social Security and that should be enough proof. Are you comfortable giving these two entities control of your money? If not, read on McDuff!

Also let's talk about what the money does in the stock market. Does it grow at 8% compounded every year as you have been told? No, you get "average rate of return" meaning the money goes up and goes down by a certain percentage every year but don't worry because it averages out to 8% over all right? Have your 401k's gone up every year by 8%? I thought not. Have you ever lost 50% of your 401k money? If so how long does it take to get back? In the year 2008 the DJIA topped out around 14,200 before collapsing to just below 7,500. Now as I write this article the world is all excited about the market coming back up and the DJIA cracking above 15,000. So since 2008 your money (assuming you stayed invested and did not need the money or reallocate to another investment) is just a little over even. This is 5 years of little to no growth. Now my detractors will say that you bought more shares of your fund or stock when the market was low so you did just fine. Well that might be right but what happens if you were in distribution during those 5 years?

If you had to take money out to live on during that time because that is your retirement account than didn't you have to sell more shares to live on because the market was way down? So when the market finally rebounds do you have the same amount of shares you did before it started downward? The answer is no and when the next downward spiral hits (and they always do) you will be going through your funds at an accelerated pace.

That problem is called "reverse dollar cost averaging" and is rarely talked about by proponents of the stock market and mutual funds. This does not have to happen to your retirement funds if you take some simple steps to avoid this calamity.

How about the tax deduction you are taking isn't that a good thing for my family? Probably not and here is why: Do you think taxes are going up or down over the next 10 or 20 years? If you said up I agree with you completely and so does about 98% of the working population. So if you think they are going up why are you agreeing to postpone the tax (tax deferral) until later and pay by your own admission a higher rate? Also does it make sense to pay tax on a small seed or the bumper crop? This tax deferral benefits Uncle Sam and not you and your family. So let's assume you pay 30% tax today on $10,000 or $3,000 in taxes. Now the tax is done and you now can put those funds in an account that will never be taxed again (properly structured whole life policy and NOT an indexed universal policy) and where the growth is guaranteed every year. What you are doing now is not paying the $3,000 because you are putting the $10,000 into your 401k for an example. Now let's assume that $10,000 actually grows well inside of that 401k (slim chance) and becomes worth $60,000 by the time you retire. So now you take the money out and pay 30% of $60,000 or $18,000 to your old Uncle Sam. "Yes John but I will be retired and at a much lower tax bracket than I am now." Great so now if I want to pay less tax, I just have to make poverty wages and I will be all set. Sound good to you? Ok let's assume again you are only paying 15% instead of 30%. You now owe $9,000 on that money. So yes the percentage is less but the cash you pay is more.

I can go on here for another several pages on the rip off the 401k's have become for many reasons but let's talk about why you are better off buying your car rather than funding that 401k. Americans will spend more money on cars than they are able to put away for retirement. This will be one of the biggest single wealth drains they face over their lifetime and yet most people have no clue how to actually make money on a car. To understand this you must first understand that the power of banking or financing is one of the most little known ways to create wealth by the average American. Owners of banks get it but we as consumers don't…until now. Just understand for now that banking has been around for thousands of years for a reason. None of us know how to be a bank we just know how to pay a bank.

Let's take $25,000 for an example and let's assume you fund your 401k with that amount of money this year (assuming you could put in that much this is just for example). Not let's also assume that over the next 5 years that account grows by $8,000 or over 30% which I can assure you for 98% of the people reading this article is a Disneyland return especially if you are in mutual funds and in the market. However, for this example your account does very well.

Now in another part of your life you needed a car and since you had your money tied up in your 401k so you bought a $25,000 car and financed it with a bank over 5 years. Now it is 5 years later and you have paid off the car loan of $25,000 plus about $5,000 worth of interest for a grand total of $30,000 in cash you have laid out over that 5 year period. You have a $5,000 car to show for your $30,000 investment so you lost $25,000. So even if you made $8,000 in profit in your 401k in another part of your life you lost $25,000 so your net loss is $17,000 over a 5 year period. Now if your 401 does what it usually does which is nothing now how much is your loss? Could it be $25,000 and growing every day because of the car continuing to depreciate? What if your 401 drops 30% over the same five years? Now you have lost $33,000. It is not hard to see why it is so hard for us to get ahead in our financial lives.

So what if we just took the original $25,000 and used it to fund a properly designed life insurance policy before we bought our car. We could then borrow the $25,000 out of our life policy (to be fair you would not be able to borrow out the entire $25,000 from the first day so you might have to fund the policy with $30,000 to borrow out $25,000 but let's just say it was possible for this example.)

So now we borrow money from the insurance company and use our $25,000 as collateral and we buy our car for cash. Instead of letting the cash sit and die in the car we need to treat that money liked we borrowed it from the bank and simply make the same payment we would have paid a bank including the interest we would have paid a normal bank. So now 5 years later we have the $25,000 back into our policy plus the $5,000 worth of interest for a total of $30,000. We also received growth and hopefully dividends (growth is guaranteed but dividends are not) during that 5 years of let's say $5,000 for example that would mean we have $35,000 tax free in our life policy and we have our car that is paid for and we can keep or sell and repeat the process. This one simple move wiped out depreciation lost on cars and the interest usually paid to banks.

These results happen if you just make the payment and if you can't make the payment, unlike traditional lenders, you can defer the payment until you can afford to make them again. This is all discussed in depth both in my book "The Perpetual Wealth System" and in a 90 minute free training video both found at www.theperpetualwealthsystem.com take the time to get a handle on this concept and take back your financial future.

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...Published: November 7th, 2013 |