

Investing in Your 20s: How to Get Started

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You probably know that your investment strategy should depend, in large part, on your age. A twenty-something shouldn't have the same asset allocation as a forty-something, and a retired 70-year-old is going to be in a different position entirely.



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So how do you make sure you're doing what's best for your life stage -- and your risk tolerance? In my next few posts, we'll go through some tips for [investing](#) at each age, starting today, with your 20s.

Start with an emergency fund. No matter what your age, you need to have a cash cushion handy in case things take a turn for the worse. Younger workers, however, are less likely to have built up that savings, so investing takes the back burner until you do.

"You want to have that money set aside in some sort of savings or money-market account. As frustrating as it is to hear that you're going to earn close to zero percent on that money right now, it's still the best place for those funds," says Chad Norfolk, vice president and principal of [Financial Advantage](#) in Maryland. In reality, you may be able to get 0.2% or 0.3% at a local bank, and close to 1% at an online bank. If you go with online, make sure you can access your money easily if your tire blows or your dog gets sick, either with an ATM card or a bank-to-bank transfer. Aim to build that account up until you have six months of living expenses.

Pick a vehicle. If you have a 401(k) account at work, and your company offers matching dollars (or plans to later this year -- some companies eliminated their matching dollars during the recession, but many say they'll be reinstating the programs, at least partially, this year) you want to start there. It's a good place to get your feet wet -- you'll be able to contribute pre-tax dollars, and get an extra boost from your employer.

If you don't have access to a 401(k), or you max out your contributions -- the limit is \$16,500 in 2010 -- you should consider a Roth IRA. You can contribute up to \$5,000 in after-tax dollars and your money grows tax-free until you pull it out. Unfortunately, you can't contribute the full amount to a Roth if you earn more than \$105,000 a year as a single filer (\$167,000 for married filing jointly), so in that case, a traditional IRA is a great choice. And whatever vehicle you choose, make sure you set it up so you contribute automatically each and every month.

Look at your risk tolerance. When you're young -- whether you're a recent college graduate or climbing the corporate ladder -- you're investing for the long haul. This is money you won't need for 35, 40, even 45 years, so you have a lot of time to weather the ups and downs of the stock market. That means you can be a bit more aggressive than your parents or your older co-workers, but you still have to consider how you handle risk.

"Don't let parents, co-workers or other sources of advice paint you into the aggressive or growth camp just because you're young. It's very important to start an investment discipline and stick with it," says Norfolk. If you can handle a lot of risk and still sleep at night, that's great, but if huge swings cause you a lot of stress, it's okay to be a bit more moderate in your choices.

Simplify. You don't have to know the ins and outs of the market to be a good investor. In fact, it's often better to be hands-off. Put your money in a target date [retirement](#) fund, which will start out on the risky side and taper back to be more conservative as you get older. (If you want to take more risk, you can pick a fund with a target date that is later than you plan to retire; for less risk, pick one with a date that is earlier.)

You can also try mutual funds, says Norfolk. "Diversification is an investor's best friend, and funds can provide you with tremendous diversification and professional management." You can research mutual funds on morningstar.com ([MORN](#)).

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