How The Rich Get Richer and The Broke Stay Broke

[0:00:12.0] ST: Welcome Nation to the Financial Rock Star Show. I'm your host, Scott Alan Turner ready to help you get out of debt, save more money and retire early. In the studio with me is producer Katie who can dunk a basketball. No, that's not true. We're hoping the kids will pickup my athletic skills and her big brains.

On the show today we'll be answering your questions about money, business and life, if you have a question you'd like answered on the show visit Goaskscott.com. 40 shows in and I have yet to mention that until the Foo Fighters or Linkin Park agree to supply some intro music, we're stuck with that tune. Maden, Metallica, Ozzy, they're on the short list too. My apologies.

When I graduated college, I moved to Atlanta, I got an apartment with one of my fraternity brothers but not just any apartment. A luxury apartment in one of the nicest apartment properties around. A place called Post Properties, they're located all throughout the United States. By luxury I don't mean downtown Manhattan style but properties that are around the higher end of the rent scale for the average middle income person.

Perfect for a college graduate with no job, right? I lived in the high rent apartment complex until I bought my first high mortgage house. I did try to downscale one time to a one bedroom place that was not a Post Property but it had cockroaches in it and I hate bugs, I hate bugs. Especially the ones that crawl over you in the middle of the night while you're sleeping and give you a heart attack, that's a true story.

You got the willies going on right now right? I moved out of that place after two months, paid the penalty to break my lease and moved back to Post Properties. I spent a lot of money on rent when I was younger. Have you ever asked yourself why the rich continue to get richer and the broke continue to get broker? According to a new recent survey, the middle class, they're shrinking.

Middle class now accounts for less than 50% of the population for the first time ever but the answer becomes pretty clear when you look at how people spend their money. Now, we need to cover a few definitions first that we're going to be talking about. We got cash flow, that's your income, that's the money that you bring in, it might be rental income, interest from the bank, pension if you have it, your investment income, your paycheck. We've got expenses, that's money you spend.

Assets, you may have heard of before, you own or have equity in. Your house, your car, boat, furniture, your assets. Then you got your liabilities, that's what you owe money on, your house, your car, your boat, your furniture, student loans, credit cards, medical debt et cetera. When we talk about broke people, I'm talking about where most of us start out, where I started out after college where you may have started out, where you are right now maybe, living paycheck to paycheck.

We're not talking about people that are in the low income housing, they're unemployed, they're on welfare, the people who are just in really dire straits, it's really a small percentage of the classes but we're talking about the huge middle class which make up about 50% of us. Most of us in that group living paycheck to paycheck. That's how I used to live anyway.

You may be there in that situation right now so maybe you can relate. You end the month with no money or not enough money to finish out the expenses that you have for that month. Now what happens with people that are broke is typically don't have a spending plan in place. When the paycheck comes in, they go out and spend it all or often, more times than it all. I've done this as well.

When you spend more than it all, that's when you fall in to debt and they spend it on the stuff that they want, they don't need it, they want it. They're just unplanned purchases, you go to Walmart without a grocery list, you buy whatever. You buy some food, some stuff for the house, "Oh we need a new vacuum, maybe I want some hunting gear, some toys for the kids," there's just no plan, you show up and buy and you buy whatever, you get the idea. Just fill the shopping cart.

If you don't shop Walmart, you do the same thing at Target, you don't shop at Target you do the same at the Costco. Wherever it is that you shop. Costco is the worst because the bulk sizes, they cost twice as much than every other thing else.

You don’t need to buy five gallons of ketchup, it’s shopping at stores, shopping online, anywhere where there’s something to buy, they buy something.

How do you know if you have too much stuff? Well, there’s an easy test. You can ask yourself, “Do you rent a self-storage space?” Have a lot of stuff in there. “Is your garage or attic or spare bedroom full of stuff? Does it take you 10 or more minutes to find the cat in your house? Because it’s hiding in stuff. Can you see your countertops?” Easy test. If a thousand dollar comes in from a paycheck, a thousand dollar goes into someone else’s pocket for the purchase of stuff.

Anyhow, a lot of times it’s for groceries, it’s for eating out, they make up a huge portion of most broke people’s spending’s. Hear me on this, I’m not picking on anybody. Buying stuff is fine , eating out, fine. It’s the lack of attention to the buying that causes people to not have any type of abundance though. It’s the, “Where did all my money go or why can I never seem to get ahead?” It’s what I would call unconscious spending.

It’s dangerous because it leaves people broke and when your expenses cancel out your income, you don’t have any money that can help you build wealth. Now, when we look at the middle class, we think, “These people, they’ve got it together, they’ve got nice cars, they’ve got nice clothes, nice homes, two and a half kids and half a dog.” Well, to me, the definition of middle class, that depends on what area you live in.

The high end of the middle class is usually round a six figure income, about $100,000 a year. The low end ranges from about $31,000 to $61,000 a year. The problem with the middle class is something we touched on in show number 23, the seven deadly sins of the financial freedom series. We talked about keeping up with the Jones.

In the middle class, the nice cars, the nice clothes, the nice homes, the bank owns them all. The middle class puts all their paycheck towards paying down their liabilities and because the bank owns everything the middle class has, the middle class doesn’t have any extra money to use towards getting rich either because they have to pay the banks off every month.

The bank used to own most of the stuff I had before I figured this out. They owned my car, they own my house, they own my furniture. So while the middle class might make $100,000 a year, it all get spent on things that can’t generate income. They have to make a big house payment instead of putting money into the stock market or putting money into a business or putting money into rental homes. The middle class, they buy stuff too but then they buy things that require big, monthly payments.

Cars, a home, vacations on the credit card, a boat, they are broke too, they spend more than they make. I’m quite familiar with the middle class, I spent a lot of time there myself. Now, what about the rich? The millionaire next door? What do they do differently? First, they spend less than they earn, they buy less stuff than broke people, they buy less things that require monthly payments that depreciate in value over time, like cars.

They don’t take on credit card debt, they take the extra money they have saved for making those decisions and put it to work for them so that it makes more money. Investing in stocks, growing a business, investing in a business, buying rental properties. That extra money is working 24/7 without any effort on their behalf to make them more money and then that new money is used to invest in more stocks and in more businesses and in more rental homes.

It takes more money and that money makes more money and that money makes more money or in other words, the rich get richer, it’s a formula and it’s a simple formula to follow. I just explained it a few minutes. If you want to be rich, do what rich people do, it starts with spending less than you earn and you go up from there. Now, onto your questions.

Amber wants to know if her score will go down if she goes to credit counselling? Your FICO score, that’s what the lenders look at when they make any determination if you’re a good risk to loan money to. Your credit score is based on the information that is in your credit reports. If you seek out a credit counselling service or go to credit counselling, one of the creditors might mention to the credit bureau that you’re seeking credit counselling but this has no effect in your credit score at all.

If you do something with a credit counselling agency, they're consolidating your payments, they're making payments on your behalf, which I do not recommend you do, then there's an indirect impact on your score because those payments have to be made on time by the agency. If that payment is late, yes, then in that case it's going to ding your credit score. The late payment will be reported to the credit bureaus and that will lower your score.

Now, shouldn't these organizations be making payments on time? That's why you hired them in the first place right? Your reputable companies will make the payments on time, the unreputable ones, who knows what those guys are doing? That's why it's in your best interest to avoid any type of consolidation. Consolidation also doesn't get at the root problem anyway, which is poor spending habits. You can get out of debt without consolidating your credit card bills, you just have to want it bad enough and your written plan to do it.

Consolidation companies usually want upfront fees and you may not get your problem solved. If you want credit counselling, visit the national foundation for credit counselling, they are a legit, nonprofit organization, you can get hooked up with a counsellor to help you out. You can visit my fico.com, they are the maintainers of FICO scores and we'll tell you everything you ever wanted to know about your credit score and more. Thanks for the question Amber.

If you have a money related question you like answered, please visit Goaskscott.com to get in touch with me, that website has my email address, Twitter you can also leave me a voice mail. Pleas contact me, I am here to help you. Shout out to Will R. and Jimmy H. Thank you guys for subscribing, I appreciate you listening. Do you want your name called out on the show, email me a screenshot showing you subscribed to the podcast and get your name heard around the world by five, sometimes six people and my two cats, it's that easy.

[BREAK]

[0:11:29.5] ST: This is a red alert warning. In my business mailbox the other day, I received an official looking letter. It had a credit card in it. At least it looked like a credit card. Everything about it looks like a credit card, it's got my name, it's got a 16 digit number a valid through date, it's got a magnetic stripe on the back but you know what? It is worthless. The paper it was attached to looks exactly like the paper issued when you get a new credit or debit card in the mail, it has your account number and the type of card.

Mine says in big, bold letters, "Here is your new," — I can't say the company name on the show for legal purposes because I would only get sued. "Here is your new premium platinum card, it's got an activation code too." If you get a debit or credit card in the mail, you know you have to call the phone number to get it activated, right? Now I've got a security freeze on my account so nobody can take out credit in my name. I figure, what the heck, I'm going to try this activation code and see what happens.

They can't prove it was me who entered the code anyway so I'm covered. I get to the website, I enter my code, that's okay, I get on to step two, enter in my contact information, I enter in bogus information so I don't want them to bother me and then I get a message saying someone is going to contact me. Suckers. Nobody's going to contact me because the information I entered was fake. This is a total scam, it's not a real card, you're not pre-approved for anything.

It's just a cleverly disguised marketing ploy to get you to sign up for this company's card. If you get a credit card offer in the mail, chuck it in the shredder. The best credit cards are not the solicitations you find in your pile of mail. I forgot to mention, the card said my available credit was get this, a $150,000. I don't even think the Amex Black Card has a limit that high, maybe it does outside my realm. Amex Black cards if you've never heard of them, they are by invite only. I've never gotten an invitation and I doubt I ever will.

Super Star Katie has the info for me, forwarding it on, it's now the Amex Centurion card formerly known as the black card. Here is the info on it, card holders are required an annual fee and in some countries also an initiation fee. In the United States the initiation fee is $7,500 in addition to the $2,500 annual fee from each card holder. All right, in addition to a variety of exclusive benefits, the card itself is made of anodized titanium with the information and numbers laser etched into the middle. That makes it worthwhile.

Anodized titanium and laser etching, of course it's $7,500. There you go, for the price of a slightly used Honda Fit, you can get a credit card to buy stuff with, that makes sense to me. The card has no spending limits, perfect. Here's another little tidbit. The largest purchase ever made on the Amex Black card, Centurion card was 36 million dollar, a rare porcelain chicken cup. All right, maybe someday I'll win the lottery so I can too buy a chicken cup.

Where do we go from here? A chicken cup for $36 million dollars. Now back to your questions. Meredith asks.

[0:15:12.8] M: "How you should store your seats in your business? Chicken cups to business of seats."

[0:15.23] F: For my business, our invoices have been digital when payments come in, they get noted in the software and the checker invoice gets filed away, easy.

[0:15:27.6] ST: Meredith who is in the sign business, I didn't share that is probably going to a lot of trade shows, craft events, working directly with a customer so they might be giving you cash, checks, credit cards. With that you can upload pdf receipts to the cloud based on services like FreshBooks or Quickbooks online. Let's say hey, Meredith and I are going out to lunch, Meredith is trying to win my business so she takes me out to five guys, burgers and fries, we have a nice meal, Meredith is buying, with this mobile apps, you can take a picture on the spot of the receipt when you log the expenses, you have the option of using a photo already stored in your iPhone as well.

Then at that time if you want it, you can throw out the receipt, you get the digital copy. Neat receipts, they can be found at neat.com as the name implies, it's a neat system. Neat in neatness and neat in the idea too. You have a lot of receipts and paperwork, it should save you some time but it may be unnecessary if you're scanning, using those features of FreshBooks or Quickbooks.

Both those services they've got trials so check them out, see which one you like better and see if they have the features you need before you go out and buying an expensive scanner and a service from a company like neat.

[0:16:51.6] ST: Okay, quick break, back in 30 seconds, I'll be answering more of your questions, you're listening to Scott Alan Turner.

[BREAK]

Hey nation, Scott Alan Turner here. Now, for those of you that are my long time listeners, you know I'm not one of those guys in the radio who promotes every product that shows up on their desk, you're never going to hear me try and get you to buy corn syrup, or recommending you to buy the DVD collection for Star Trek Deep Space nine, deep space night, No.

I have a name to uphold to you, the Rock Star Nation. But if I were to recommend something to you, I would tell you about Spoon City. Many of you are sitting there right now listening to this mindless dribble at home eating a bowl of cereal for breakfast. Unless you're like my two year olds using their hands, you're using a spoon to shovel in those chocolate marshmallows sugar rose. Spoon design has remained unchanged for hundreds of years until now.

The fine folks at Spoon City have come up with the first ergonomic spoon to take your eating experience and health to a whole new level. Eating with a non-ergonomic spoon can cause side effects such as headaches, nausea, cramping, bloating, lightheadedness, stuffy or runny noses, chest pain, in some rare cases, spontaneous combustion. Head down to your local spoon city today, your mouth deserves the best.

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[0:18:11.0] ST: Welcome back Nation, that is a heavy tune, that tune is from my friend John's band, the Liberty Underground, let's get that right. Hey, if you know someone who has an original tune, they're in a band, they want their music heard by five, seven, sometimes eight listeners, drop me an email. If I think the music is a good fit for the show, it might end up in here. Ravine Wit writes.

[0:18:35.0] R: "I have a question which I'm still looking for the answer and I was thinking that many people have the same problem like me. I have an idea to buy a niche product."

[0:18:42] ST: Or niche depending on how you pronounce that word. I say niche. You say tomato, I say tomato, you say potato, I say potato or as I always get on my wife's pecan, like a pecan pie. Or anyway.

[0:19:00] R: "I have an idea to buy a niche product from USA to sell in Thailand," where he lives. Thailand, another pin in the map. "This business is just buy and sell. Anyone can do it if they wanted. I need some techniques to make the difference, in my mind, I have only two solutions being the only dealer in Thailand and changing the logo and packaging. Do you have any suggestions to the problem?"

[0:19:21.6] ST: I love the entrepreneurial spirit here all the way from Thailand for an equal opportunity question to answer on the show. This is an issue ever small business owner faces at one time or another. Competition. If I run a lawn mowing service, how do I compete with the other lawn mowing services? If I sell a product online, how do I compete with all the other online products.

If I sell used books, how do I compete with the other used book sellers? If I want to sell pizza, how can I compete with the other pizza place? That was only slightly different, I just sell better tasting pizza. But if all pizzas tasted the same, what would you do? Ravin was thinking of becoming a monopoly which is a fantastic solution if you can pull it off and changing the packaging of the product.

When I started green building education services, we were pretty much a monopoly because we were the only company offering an online product in our space but then the competitors started showing up. If you want to distinguish your product from competitors, offering the exact same thing, here is what worked for me, answering the question, "How do you get ahead of everyone if the products are equal?"

Number one, you provide superior customer service, faster response time, more interaction, always answer the phone, reply to email, reply on the weekends, evenings, holidays. Might sound crazy but I'm telling you it works. For some of you small business owners, you just need to provide okay customer service to get ahead. I mean, when someone sends you an email or a voice mail, call back and you'll make more money than you are now. I can't tell you how many service companies I've called and never heard back from.

I could enter any service industry, there is that exist out there and dominated just by providing great service. Really, I could do that and you could do that too. Another tip is offer better return policy. People are so concerned about losing a few bucks for the one person who tries to return a product on day 31 of 30 in their return policy that they don't offer these good return policies. The positive word of mouth is going to do more for your bottom line than being Scrooge McDuck in a stickler for the rules on these policies like Target.

Next offer a product or service at a lower price to keep out competition. This allows you to have a bigger market share. If you're first in market, you can keep others out of the market by having a stellar product at a price nobody would dare compete with you at. Next is you can be a better marketer. Superior marketing of a good product can be better than good marketing of a superior product.

Think, Microsoft Windows or Microsoft Word or Microsoft anything. Terrible, terrible products that aren't user friendly. That used to be the case, I don't use Microsoft product anymore, I can't speak for them nowadays. And it is a billion dollar company. So they've obviously done marketing right. Next is you can offer something as a bonus with your product, video tutorials, guides, free add on, free consulting, free service checkups, something a little extra that separates you from the other person over there doing this.

If I'm running a pizza place, I'm giving every customer a free chocolate chip cookie at the end of their meal, they're going to remember that, nobody does that. If I'm mowing lawns, I'm giving every customer a free perennial — that's a flower — each spring or a potted rosemary bushes in the fall. These little things, they make all the difference in the world and they cost next to nothing. Pennies, dollars, but people don't do it.

They'll pay $2,500 for an advertisement to be sent in the mail but they won't spend $500 bucks to get every current customer a little gift. All those customers are going to tell their friends about that gift, you're going to get back from the pizza, "How's the pizza? Pizza's okay but we got this great chocolate cookies at the end. You should go check it out." You get more customers because of great word of mouth. Thanks for the question Ravin Whitt, sorry for butchering your name, I apologize for when I have to do that.

Next question comes on my voice mail, let's have a listen.

[0:23:43.0] R: "Yes, Scott, I want to get out of debt real fast."

[0:23:46.9] ST: Ronald wants to know, not just how to get out of debt but how to get out of debt fast? First you got to check out my article "How to get out of debt quickly in four simple steps", link in the show notes. It shows the path to getting out of debt quickly. Then you have to pick how you're going to pay down your debts and you have two choices, you have the debt snowball method and you have the debt avalanche method.

Now, when you compare the debt snowball to the debt avalanche, there's some things you have to consider. First, from a mathematical perspective, only paying down the high interest debts first will always get you out of debt the fastest. If you had two credit cards, say we've got a car loan, $2,500 balance is 6% interest, and a MasterCard, $10,000 balance at 18% interest, paying the MasterCard down with its 18% interest will get you out of debt faster. Simple math. You pay more in interest at 18% versus 6%.

When you pay debts down on their interest rates from highest to lowest, that is called the debt avalanche method. The other form of debt payoff is called the debt snowball. Also simple to follow, you pay off your debts in the smallest balance to the biggest balance. When one debt is paid off, you take that money you're paying on that and you put it towards the next biggest debt.

So in that previous example, you pay off the $2,500 car loan first even though it had a lower interest rate. When that is paid off, take that money you're putting towards that, put it towards the MasterCard. Now the first thing people say is, "It doesn't make sense to pay off a debt with 6% interest for the one that has an 18% interest. You're paying more in interest and you're losing money. It's going to take you longer."

It's kind of like weight loss. If I tell you, "Go out and lose 50 pounds," while you know you could do it, let's say you're 50 pounds overweight, you're more likely to try it for a while, lose little weight and then put the weight back right back on. That's what frequently happens when people try to pay out a $20,000 debt before they're paying off a , $500 medical bill with a lower interest rate.

$20,000 balance, that starts to come down but you know, it's so overwhelming, it's taking so long. Let's just forget it and they quit, they can't see the light at the end of the tunnel. If I tell you, hey, go out and lose two pounds over the next 30 days on your way to losing 50 over the next couple of years, that's doable. You can get that.

You lose two pounds quick and you see the results in the scale, and say, "Oh, I see myself in the mirror, I can tell, I look a little bit different, this is cool, I'm going to keep going with it." You're building momentum, study after study proves the debt snowball is the quickest way to get out of debt because by working from the smallest debt to the first, no matter what the interest rates are, you build momentum and you see little successes and little wins, mathematically, it doesn't make sense.

Mr. Spock said, "No. This is illogical." But most people figure out the other way doesn't work because they try it and fail. If you fail to follow the debt avalanche method because you see no progress, you're going to end up paying more in the long run. On paper you can get out of debt faster by following the debt avalanche, in reality, most people don't stick to that plan just like most people don't stick to a diet.

They get frustrated, they don't see progress and they quit and they give up, put the weight back on, put the debt back on. If you're a nerd, you like numbers, if you're disciplined, the debt avalanche can work for you. I'm not telling you that it can't. Based on studies, the success rate of using the debt snowball is significantly higher, thanks for the question Ronald.

[0:27:32.6] ST: Caleb wants a new car. He says:

[0:27:34.8] C: "I just got an $18,000 bonus at work."

[0:27:37.6] ST: Nice work dude.

[0:27:39.9] C: "I've been saving up in my car fund for the past year and I've got $25,000 cash, I live in an apartment, have no other debts, I have an emergency fund and I'm saving 20% for my retirement. Is it okay to buy a new $25,000 car if I'm paying cash?"

[0:27:56.0] ST: Wow, $18 grand as a bonus. That is nice work. Congrats. Must be a sales person or something like that. You have no debt, saving for retirement, emergency fund, you got all those checked off, you got your financial house in order, is it ever okay to buy a new car in cash? If you're not going to cry over losing the depreciation when you drive off the lot, day two, that car is going to be worth $21,000, how are you going to feel about burning four grand?

Here's an activity for you though. Go to the bank, withdraw $4,000 in cash now that you have it, bring it back to your apartment and set it on the kitchen table. Don't tell the neighbors or friends you're doing this because you don't want them robbing you. Then, eat dinner with that $4,000 in front of you. When you watch TV that night, put it on the couch next to you like a little pet. When you go to bed, you put it on your night stand. Then when you wake up in the morning, you have coffee with it.

Think about all the things you could do with that $4,000. Then when you go back to work next day, you put it in the bank. I bet, your perception is going to change. Maybe not, you might not care about spending the money and affording the loss, it is a loss no matter how you look at it. When you drive off the car lot with a new car, that money is gone, cars are depreciating assets.

I am not against people buying new cars if that's how you want to spend your money and if you can afford it but most of you can't and you shouldn't be buying new cars. Caleb can, he has to make his own decision. My mother in law just bought a brand new 2015 Toyota. Now, it was a better deal than the used 2014's in this case. It actually made sense for her to buy a new car because of the price.

But it's going to be the last car she probably ever owns. Two of my last three cars we bought new but we've been driving them six years and eight years respectively. If you buy new, buy with a mindset, you're going to drive this car until the wheels fall off. Then you get the most value out of it as you can. Don't buy a new car if you plan on trading it in every three or four years, that's just dumb, that is where money is wasted.

Even if you can afford it, it's just wasting money. I guess if you have that much money to work, it's okay but 99% of people don't. Since 99% of all cars are financed, most people are making the mistake of buying a new car. According to the book The Millionaire Next Door, the average millionaire buys two year old cars. Now why is that?

Because they know a new car takes a massive hit in depreciation in the first two years and you can get a really nice two year old car with low miles for a lot less money. Let somebody else take that hit in the depreciation, not you. Yeah, it's okay, buy a new car if you can afford it. Should you do it? Not unless you plan to drive that car for 10 to 12 years. Otherwise you're just wasting money. Thank you Caleb for the question.

[BREAK]

[0:31:03.3] ST: Many people struggle to save or stick to a budget or put down the chocolate cake, that's me. Or find ways to live a life of abundance and significance. Are you feeling lazy? Do something anyway. Did you fail yesterday? Do something anyway, are you ready for bed? Do something anyway. You can't get your partner onboard, well, do something anyway. You can't find the willpower, do it anyway.

I found in my own life, I'm sure you have two, starting is half the battle, just showing up gets you part way there. Sometimes it's just the matter of standing up to get going. Once you get going, it's not so hard anymore. Amazing results are the result of herculean consistency. Those are the words.

Can you do me a favor please? Take 30 seconds right now, text three of your friends the link Getfr.com and tell them to check out the show. I really appreciate you guys listening and would love it if you could help me spread the word. Super simple, just text getfr.com and tell them how awesome my cats are and the advice is okay too. Next time on the show, how to finally take control of your spending. What is the secret? It's no secret but I will tell you.

That's it for this episode, I'm your host Scott Alan Turner, Rock star Katie is my producer, special bumper music today provided by The Liberty Underground. Thanks guys for the audio tracks, find out more about them and all the links mentioned in the show on the show notes on Scottalanturner.com. Today's episode is powered by Ben and Jerry's ice cream. Thanks for listening, I appreciate you.

[0:32:47.2] ANNOUNCER: Okay nation, for your free copy of the guide, "How to save $1,000 in one week", simply subscribe to the podcast right now on iTunes and text the word "saving" to the number 33444 to prove that you did it. Subscribe now to get out of debt. Save more money and retire early. See you next time.

[END]