THREE SIMPLE STEPS TO FINANCIAL INDEPENDENCE

ESI MONEY
THREE SIMPLE STEPS TO WEALTH
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The Road to Financial Freedom

Do you want to become financially independent?

Do you want complete freedom to choose what to do and not do?

Do you want to be the master of your own destiny versus have someone else in control?

If you answered yes to any of these questions, you’ve come to the right place.

This book details the few, essential steps anyone needs to take to become financially independent.

When I say “anyone”, I mean anyone. Any person who applies these principles consistently over time will become wealthier. He will also achieve financial independence well before most others.

And when I say “few”, that’s what I mean. There are only three simple steps that are vital to your success. I leave out all the stuff that doesn’t work or isn’t important.
Learning from Success

What’s detailed on these pages is the summary of 25 years of experience.

I am not a financial adviser or money professional of any kind. I’m just a normal person who learned how to manage money by trial and error as well as study and focus.

But the results speak for themselves. In those 25 years I have been able to accumulate a large net worth that has left me financially independent.

Why does that matter to you? According to The Miracle Morning, a key path to success is “to learn from the experts — those who have already done what you want to do.”

Now I would certainly not call myself an expert! Banish the thought! In fact ESI Money has an entire category dedicated to “experts” who are not really experts (they just pretend to be because it’s to their advantage.)

But if you’re wanting to be financially independent, then I’m your guy. I’ve done what you want to do. I personally prefer learning from someone who has “been there and done that” versus someone who has plenty of theories but no real accomplishments to back them up. I trust you feel the same.

Before we get to the details, let me share a bit about my background.

Who Am I?

I’m a 50-something guy who’s been married 25 years and has two kids (son, 20; daughter 18). We live in Colorado (and LOVE it!).

My interest in personal finance was a gradual process which built upon itself through a series of events. Some of the highlights include:

• I grew up rather poor in a small Midwestern town and knew I didn’t want to live that way as an adult. From a young age, I knew I wanted to be wealthy and I geared all my career choices towards high-paying professions.

• I worked my way through college and grad school. I spent the next 28 years working in marketing for large and small companies.
• My wife and I started helping others at our church with their finances. The training we took prior to assisting them not only equipped us to help others but also taught us a ton about managing our own money.

• Counseling others taught us a great deal about real-world money issues. We could see first-hand what was working and what wasn’t. Much of our learning was from seeing others’ mistakes.

• About this time I read The Millionaire Next Door and started applying the concepts I learned. It is, to date, the most influential money book of my life.

• We paid off all our debts early in our marriage, including our mortgage, and saved 36% of my income for over 20 years. We invested this money initially for growth and later for income.

• Along the way, we donated approximately 20% of our income. Helping those who are less fortunate is a key part of our family’s values.

• In 2005, I started a personal finance blog. As I wrote, I learned more about what it really took to become wealthy. It helped crystalize my thoughts and forced me to take action.

• I determined an arbitrary amount in both assets and income for what I thought it would take to retire early. Then, through a series of events, I became very tired of work. I wanted to leave for good. I wanted my freedom. I began to rethink my retirement plans. I calculated a very specific retirement budget and found that I had enough to retire at any time.

• In the fall of 2016 I retired with a nest egg whose income is large enough to provide for my family’s needs.

• I started my latest blog, ESI Money, shortly before I retired.

For more specifics on my financial life simply visit my “about” category.
From personal experience, and the experience and testimonials of my readers, I know these principles work. I hope you will take them to heart, implement them, and achieve your financial goals.

**What is Financial Independence?**

Depending on where you read, there are many definitions of financial independence (FI). For the purpose of this book we’ll use the following definition:

*Having wealth to cover expenses indefinitely.*

The keys to this definition are:

- **Your expenses are covered by your assets.** The income generated by them, drawing down (spending) your assets, or a combination of both.
- **You have enough to keep up this situation indefinitely.** If your assets cover your expenses for only three years, you are not FI.
- **You do not have to work.** You can choose to if you like, but it’s not required. This is the “freedom” part of FI. You have the freedom to decide what you want to do with your time.

The rest of this book is about getting you to FI – helping you accumulate the wealth to cover your expenses indefinitely.

**Three Simple Steps to Financial Independence**

As you can probably tell, I’ve spent a lot of time thinking about money management, writing about it, and living it out in my personal life.

And so, based on my experience, I’ve narrowed the path to FI down to these three steps:
Step 1: Earning.

You need income. The higher, the better but any income can work if you’re diligent. For most people, the key to driving income growth will be to develop their careers but others may pick a business or side business to grow their earnings.
Step 2: Saving.

You must spend less than you earn. It’s vital. Even if you make $1 million a year, if you spend it all you won’t get to FI. So you need to control expenses to maximize the difference between income and spending (within reason, of course. You don’t have to be frugal to the point of hating life). This difference is your savings or what I call your gap (more on that in a minute).
Step 3: Investing.

You take your savings and invest to grow it. While I opt for index funds, real estate, and P2P lending, there are many other ways to invest for success.
These three steps, combined with time and effort, equal a recipe for FI. Remember, though, that your mindfulness and conscientiousness towards the three steps will determine how long it takes you to achieve FI.

Now that we’ve outlined the three steps, let’s explore each of them in detail and address some practical tips for making the most of each.

**Earning**

You need earnings (income) of some sort to survive. And the higher they are, the more you can thrive.

Of course everyone would like to earn more money. But what are the best ways to do so?

There are many options but by far the single-best way most people can earn more is to grow their careers. That may not sound exciting, but it’s true.

There are two gigantic reasons why growing your career should be priority number one for anyone looking to earn more:

- **Your career is a multi-million dollar asset.** This fact alone should be enough for you to want to nurture and grow it. After all, if someone gave you a million dollars, you’d take some steps to make the most of it, right? Well, your career is more valuable than that and if you tend to it, you will reap substantial rewards.
• **Your career can be worth millions more if you treat it right.** Yes, literally MILLIONS more! What other idea, effort, activity, etc. do you have that provides a chance of earning you an extra million or two? Exactly. That’s why paying attention to your career is so important.

These are only the monetary reasons. It’s also likely that as you grow your career you’ll receive more responsibility, gain more in control of your work life, and have more interesting and challenging tasks to work on – all things that most people find attractive in a job.

Many will argue that there’s no way to get ahead in their current job or profession or company. There are always ways to do so. In every profession there are people who advance. They climb higher and get paid more. It can be done if you want it. However, if your job is so terrible that you don’t want to or can’t bear the thought of working on your career, you may want to consider a change.

**How to Grow Your Career**

Now that we’ve established that it’s important to grow your career, you might find yourself wondering how. I can help you there, too! I’ve identified seven tried and true steps to growing your career:

• **Over-perform.** There’s a specific way to do this to get the most results

• **Be likable.** Treat people how you’d like to be treated.

• **Network.** Easier than ever with LinkedIn.

• **Be attractive.** It’s not just about your physical qualities.

• **Continuing learning and developing skills.** Keep growing and keep earning.

• **Know how to manage yourself.** It’s not just about the work.

• **Know how to market yourself.** Resume writing, interviewing, and the like.

These steps require very little effort compared to the rewards they can generate. They also do not require a great deal of time. Small, daily efforts will add up over time to deliver big results.
I detailed these in *How to Manage Your Career to Make Millions More*. You can read the specifics there. I recommend you read the details and then develop a plan to grow your career.

You can also keep an eye out for my [career posts](#) as they will continue to provide suggestions for making the most of this valuable asset.

**Other Ways to Earn More**

Once you have your career humming, there are other ways you can add to your earnings. A few ideas:

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**Develop a side business/income.**

I’ve had a couple side businesses in my lifetime and they can be nice income supplements. Consider what skills you may have that others would be willing to pay for. You could do some consulting using your career skills (make sure you check for conflicts of interest before doing this) or develop your own small business from a hobby (ex., bike repair) or interest (ex., pet sitting).

**Get a second job.**

Probably not a great long-term solution, but having a second job for a period of time can help in one particular area (ex., getting out of debt). I spent several years as a soccer referee which allowed me not only to get a great workout but to earn some extra cash.

**Use cash back credit cards.**

Why not get paid for something you’re already going to do? I have [earned $12k in the last decade using credit cards](#) with the [most recent year yielding over $1,500](#). Of course it’s essential to avoid all fees and refrain from extra purchases to make this strategy worthwhile.
Admittedly, it’s more difficult to grow your income than it is to cut spending. This is because earning more requires time and extended effort with sometimes no guaranteed payoff. That’s why I focus on growing your career, as that’s where the biggest opportunity lies for most people.

You can keep up-to-date on earning ideas by subscribing (for free) to my weekly posts.

**Saving**

The most essential part to FI is savings. It’s this money you’ll use to create your investments and nest egg that will sustain you long after you’ve stopped working. And the good news is that saving money is easier than earning since you have more control. However, in order to create savings, you’ll have to control your spending carefully and mindfully.

That doesn’t mean re-using toilet paper and making your own toothpaste to save money. Rather, I suggest being moderately and selectively frugal. In other words, spend on what you like to spend on, but do it in moderation. And simply cut out all the other stuff you don’t like as much. This is where you can really save some big bucks.

The purpose of controlling your spending is to create an ever-growing gap, the difference between what you earn and what you spend.
To help you get there, here are some of the best ways I’ve found to save money:

- **Have a cash flow plan.** Some people call this a budget but regardless of name, the concept is the same. You must know and track your spending to make any substantial progress in saving money. Doing so will help you identify where your money is going and help you direct and control it.

- **Buy a house you can afford.** Buying a house you can afford will save you thousands in interest payments. Reaching too high and buying the most house you can not only costs you for the house itself, but also locks you into a whole host of other costs which drag down your net worth.

- **Save when buying cars.** Either buy used cars or use a bidding process when you buy new. Do not finance a car purchase. Save in advance and pay cash.

- **Control small spending.** You don’t have to micromanage every nickel but if you’re not careful, small expenses will add up to a large drain.

- **Live in a low-cost city.** There’s no denying that some areas of the country are more desirable but they come with a hefty price tag. But there are also wonderful places that are very affordable.

- **Stay in shape.** Doing so will not only save you money in a ton of ways) but also help you earn more.

- **Stack discounts.** Why settle for 10% off when 50% off is much better?

- **Get rid of your stuff.** You’ll declutter your life, earn some money, and save a bundle, especially if you currently rent a storage unit.

- **Ask for discounts.** It doesn’t hurt to ask, does it?

These are just some of the ways to control your spending. I add new tips regularly so watch my “save” category for more ideas.

The good news is that you don’t have to do all of these. Just pick the ones that work best for you to keep spending as low as possible and you’ll be able to save.

Obviously the higher your savings rate, the faster you’ll be able to reach FI. If you maximize income and control expenses, FI will almost take care of itself. But you can do better than that as you work on step 3...
**Investing**

Now that you’ve started working to grow your gap, it’s time to invest the money. As you do, here are some guidelines to follow:

The most powerful investing weapon is time. So you will want to invest early and often, giving compounding as much time to work as possible.

Early in your investing career, your primary objective is growth. This simply means that you want your investments to increase in value as much as possible year after year, rather than produce income. This is how your net worth begins to snowball into something significant.

To accomplish growth, I recommend low cost, stock index funds. I used a three-fund portfolio from Vanguard and recommend the same for others who are more than ten years away from retirement. For more details and specifics about investing, including why index funds are best, I suggest reading *The Bogleheads’ Guide to Investing* and *The Simple Path to Wealth*.

After several years, when your investments reach a large enough size, you can begin to transition to income-producing investments like real estate, dividend investing, and P2P investing.

Keep watch on my invest category for an ever-expanding list of investing ideas and thoughts.

**Considering the ESI Scale**

Now that we’ve got a handle on the three steps, let’s see how you rate on each and where you can improve to grow your wealth.

There are almost as many ways to hit FI as there are moves in a chess match! But let’s look at some common things you’ll need to keep in mind as you earn, save, and invest.

To determine how well you are doing on a particular step, and where you need to improve, let’s use the following rating scale. Think about what we’ve discussed in each step and grade yourself:

- Excellent
- Good
- Neutral
- Bad
- Disaster
How did you do? Did you figure out your strengths and weaknesses? Hopefully you did and can now develop a plan to improve!

**Working the ESI Scale to Financial Independence**

It’s essential that you take a critical look at your behaviors and progress if you want to achieve FI. While you’re assessing yourself, here’s some food for thought based on my experience:

> You can’t be a disaster in any of the steps if you want to reach FI at a reasonable age. Failure in one is enough to kill progress in the other two.

- You can’t be a disaster in any of the steps if you want to reach FI at a reasonable age. Failure in one is enough to kill progress in the other two. For instance, if you are great at earning and saving but you lose a ton or can’t propel your earnings through investing, you’re dead in the water. If you can’t earn more than minimum wage, it’s going to be hard to make much headway with the other steps. And of course we’re all familiar with disaster of lifestyle inflation!

- If you’re “bad” in one of the steps you’ll likely be hindered significantly. There’s a reason Warren Buffett says “never lose money.” And if you’re bad at any of the three steps, you’re going to lose money. Maybe you can overcome it with stellar results with the other two, but I doubt it.

- To reach FI at any reasonable age you need to rank at least neutral on all of them so you aren’t harming your finances. “Neutral” is the absolute minimum for all three steps for those looking for FI.

- On a positive note, the better you are at all of them, the faster you’ll get to FI.

- To reach FI a bit earlier than most, you’ll need to be good at two of the three.

- If you want to reach FI when you are 50 or younger, you have rate “excellent” in at least one category and “good” in the other two.
• The most common paths for reaching FI in relation to E-S-I seem to be “excellent - good - good” and “good - excellent - good”. The ones who retire really young are “excellent - excellent - good.”

• I don’t think anyone is excellent at investing. I think “good” is the best most of us can strive for realistically. That leaves earning and saving as the focus areas for everyone.

You should continually work on growing in all of these areas so you can hit FI as soon as possible.

**When Can You Become Financially Independent?**

So, you begin working on earning, saving, and investing. You grow each of these over the years. And now you want to know when you’ll be financially independent.

The short answer is “it depends.” The long answer is that it’s not possible to determine without knowing your post-retirement expenses. This is the amount spent annually when a person reaches FI. I recommend developing an FI budget for a year or two from your expected retirement date so you know exactly if you can cover your costs. If you’ve been doing a budget up to this point, knowing your expenses and putting together an FI budget should be a breeze.

Then, once you have enough income and assets to cover these expenses indefinitely, you are FI. For instance, if Joe completes a rough budget and knows he needs $40k a year to live the lifestyle he wants, then that’s the number he needs to cover. Once the combination of his post-retirement income and the amount he can withdraw annually from his assets surpasses $40k and can be sustained indefinitely, he’s FI.
Examples of Reaching Financial Independence

I read many FIRE (Financial Independence Retire Early) sites and am amazed by the various ways people have achieved FI (especially those in their 30’s and 40’s).

The FI spectrum ranges from those who only need $30k a year to cover expenses while others need $100k (or more!). Here’s an example of one end of the spectrum compared to my situation.

The most common path, the lower end of the spectrum, is as follows:

• High income while working
• Low expenses
• Savings rate of 50% or more
• Invest in index funds, real estate, and/or dividend stocks
• Reach FI with an annual expense number of $30k or less at a relatively young age

My path was a bit different since I wanted a higher level of income in retirement. Here’s how things panned out for me:
• High income while working. I had a successful career during my working years.

• Moderate expenses. We were semi-frugal but not misers.

• Savings rate of 36%. Could have been better but could be worse.

• Invested in index funds initially and then real estate

• Reached FI with an annual expense number of $97k at an early retirement age (early 50s)

There are people above and below these numbers, but this range probably covers the majority of those who reach FI and gives you plenty of middle ground to shoot for.

And there are all sorts of combinations to reach FI that you may want to consider:

• Average income, very low expenses, very low FI income needed

• High income, very low expenses, very low FI income needed (these are the people retiring in their 30’s)

• Average income, moderate expenses, great investments, low to mid FI income needed

And on and on...

The possibilities are endless and as unique as the people striving for FI.

**Running Some FI Numbers**

For those of you who want more concrete examples, let’s look at some scenarios using [this calculator](#) and various assumptions.
We’ll use someone with an $80k annual income. Here are some scenarios (these assume the person has an existing portfolio with a value of $500k):

- Income: $80,000
- Savings rate: 10%
- Annual spending: $72,000
- Annual savings (the gap): $8,000
- Years to financial independence: 22.3

- Income: $80,000
- Savings rate: 25%
- Annual spending: $60,000
- Annual savings (the gap): $20,000
- Years to financial independence: 15.3

- Income: $80,000
- Savings rate: 50%
- Annual spending: $40,000
- Annual savings (the gap): $40,000
- Years to financial independence: 6.7

Even if you had zero in your portfolio, if your gap was $40k on an $80k income, you’d hit financial independence in 16.6 years.

See the power of the gap? This is why it is so important – growing it can shave YEARS off the road to financial independence.

If you want to answer the question a bit more in depth, I suggest the great book How Much Money Do I Need to Retire? It’s the best book on retirement I’ve ever read.
To help you get there, here are some of the best ways I’ve found to save money:

- **Have a cash flow plan.** Some people call this a budget but regardless of name, the concept is the same. You must know and track your spending to make any substantial progress in saving money. Doing so will help you identify where your money is going and help you direct and control it.

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Next Steps

So what do you need to do with all of this knowledge? Here are a few steps to get you well down the road to FI:

Set a retirement date. You may miss it, but with a date you’ll retire earlier than you would without one.

Develop a retirement budget. Include costs, income, and the assets you’ll need to make that budget work.

Create a strategy for managing and growing your earnings, savings, and investment to cover your retirement budget and reach FI.

Implement your plan and stick with it.
Yes, it seems simple, but it works. Becoming wealthy isn’t that complex, it just requires knowing the basics and having the discipline to work on them over time.

**Thank You**

Thank you for taking the time to read this book. I wish you the best of luck in your FI journey!

If you have any specific questions or comments, feel free to [contact me via email](mailto:contactme@esi.org).