The Millionaire Next Door

Author: Thomas Stanley and William Danko

There must be hardly any person who is not interested in getting rich. We all want to know that one secret which all the rich, seem to share. In "The Millionaire Next Door" authors Thomas Stanley & William D. Danko examine the common characteristics of millionaires, debunk the myths associated with millionaires and provide a detailed perspective of what a real millionaire looks like. Using real-life data and examples, the book analyses the habits of the wealthy and wheedles out their common attributes, practices and ways of life. The book makes for an interesting read and sheds perspective on the lives of millionaires.

Key Takeaways

- To be considered a millionaire, as per Stanley and Danko's definition, you must be worth US$1million or more.
- Being a millionaire goes beyond "appearance". Millionaires may not seem 'wealthy' from the outside.
- Frugality is a common trait of millionaires.
- Millionaires learn how to be efficient and responsible with money.
- The first step towards accumulating true wealth is planning how to spend your money.
- As a wealthy parent, it is important that you take the time to consider how you raise your children. You want to encourage them to be responsible with money.
- Consider whether you are truly benefiting your children when you gift them money. And question if it is actually having a negative impact on their future capabilities.
- There is always going to be a difference between those who work hard for their wealth and those who are born with it.

What makes a Millionaire?

"These people cannot be millionaires! They don't look like millionaires, they don't dress like millionaires, they don't eat like millionaires, they don't act like millionaires—they don't even have millionaire names. Where are the millionaires who look like millionaires?"

Most people would consider, the number of material possessions that a person has, as a true measure of his or her wealth. Consequently, most people think that rich people have a lot of material possessions. However, to be a millionaire one does not need to have a plethora of material possessions. Wealthy people do not necessarily only place importance on the possessions that they own. They seldom make their wealth obvious. You may not be able to tell that they are wealthy by looking at the car that they drive, the clothes that they wear or the watch they have on their wrist.

"Those people whom we define as being wealthy get much more pleasure from owning substantial amounts of appreciable assets than from displaying a high-consumption lifestyle."

For the purpose of this book, Stanley and Danko consider the 'wealthy' to be anyone who has a net worth of one-million (US) dollars or more. A couple of facts to note when considering this figure is that only 3.5% of American households can be considered wealthy by these standards and of that 3.5%, 95% of them will have a net worth anywhere between one-million and ten-million.

These figures will probably make you wonder why the book is focusing on such a small segment of the population. The reason that this particular segment of wealth has been chosen, is because it's entirely attainable, its reachable by many Americans and can be done in only one generation. It's not going to take time to build up to this level of wealth. They are the millionaires who live among us.

Frugality and Budgeting

A question plaguing many minds is, "why is only such a small percentage of the population considered wealthy." There are many households that earn a six-figure salary but have still not been able to reach the threshold. This is primarily because an alarmingly large number of Americans live their life spending tomorrows money. Many households in America are entirely debt-dependant. Living pay-check to pay-check, digging into savings and over-drafts.

"They are debt-prone and are on an earn-and-consume treadmills."

These are the people that spend their money on possessions that they believe will give them the wealthy image, possessions to essentially lift their 'success.' When in fact, the reality is that it's purchasing these very possessions, which is detrimental to their wealth. Millionaires, those who can be considered wealthy, always budget. The average lifestyle of the American millionaire is not what the public perceives it to be. The average millionaire is well into his fifties, has been married to the same woman, and lives in a middle-class neighbourhood. The average millionaire is more likely to buy a $40 pair of shoes than a $500 pair of shoes although he has the money. Another aspect of the millionaires in this country is their spouses. More often than not, the spouses of millionaires are more frugal than their counterparts. Most people will never become wealthy in one generation if they are married to people who are wasteful.

"They became millionaires by budgeting and controlling expenses, and they maintain their affluent status the same way."

When surveying the wealthy, it was discovered that most 'millionaires' had less than 7% of their total wealth as total annual realised income. The incredible result of this is that whatever the figure is under 7%, that's all that they have subject to income tax. To build wealth, minimize your realized (taxable) income and maximize your unrealized income (wealth/capital appreciation without a cash flow). Often, a household may be considered asset-poor, regardless of it's high income. The key reason that this happens is that they lead a high-consumption life, and in order to do this, they are required to maximise their realised income.

"Such people might wish to ask themselves a simple question: Could I live on the equivalent of 6.7 percent of my wealth? It takes much discipline to become affluent."

Planning & Frugality is the cornerstone to building wealth

The most common traits among the wealthy are efficiency and the ability to plan well. In order to become wealthy, people had to learn how to use their time, energy and money in the most efficient manner. Without efficiency, it would be a lot harder to accumulate any wealth. People who understand how to plan their wealth have the ability to set aside money for investments etc. A great goal to have is to have a minimum of 15% of your income available for investments. This is going to help set you up for more wealth.

Ask yourself how much your household spends in a year, and whether you know what portion of that spending comes out of different categories such as groceries, petrol, bills, mortgage etc. Unless you understand exactly how and where you are spending, it is almost impossible to truly control your money. If you can't control your money, it is not likely that you will ever accumulate a lot of wealth. The first step toward planning is to maintain a record of your expenditures and gains, to get a better understanding of where your money is coming from and where it is going. You can consider working with an accountant and come up with an achievable budget. Remember that knowledge is power.

Millionaires and their flashy cars – A myth

"If your goal is to become financially secure, you'll likely attain it. But if your motive is to make money to spend money on the good life, you're never going to make it."

Our research revealed some interesting facts about motor vehicle ownership among the wealthy.

1. Just over 1/4 of those surveyed had not purchased a car in over 4 years.

2. Just under 1/4 actually own brand new cars.

3. The remaining purchase second-hand or lease.

This debunks the myth of the wealthy only owning brand new, flashy, top of the range cars. You can be wealthy and still choose to own a standard second-hand car.

"Being frugal is a major reason why members of the used vehicle-prone group are wealthy. Being frugal provides them with a dollar base to invest."

Family forms an integral part of the millionaire's life. Children of the wealthy often become "high-volume consumers" but are seldom wealthy themselves. The children spend to increase their status, they purchase luxury cars, buy flashy homes in nice areas and send their children to expensive private schools. The term economic outpatient care (EOC) defines the economic presents that children receive from their wealthy parents (or even grandparents.)

"They are living example of one simple rule regarding EOC: It is much easier to spend other people's money than dollars that are self-generated."

It's common for those that receive EOC from their wealthy parents to become 'under-achievers.' They tend to earn less of their own money because they don't feel that they need to. It is also common for those who have received EOC to spend more than they earn. They find it harder to separate their earnings from the wealth of their parents, who perhaps gift them too much. They have a tendency to rely on credit and debt. And one of the most common traits amongst this group of people is that they always invest less than those who don't receive any Economic Outpatient Care.

Unfortunately, many wealthy parents see no harm in EOC. They believe that it can be beneficial. And in some circumstances, believe that it is correct. However, in order to be successful later in life, these children need to be disciplined. Parents need to instil in them the ability to earn a living and provide for themselves without relying on hand-outs. This becomes a problem when those receiving the EOC are indisciplined, irresponsible and have no means of earning their own money.

So, it's been made pretty clear that gifting your children money, which obviously feels like a nice and generous gesture, can often do them more harm than good. However, as a parent, you would like to provide them with something that will make them financially stable and responsible adults.

10 Rules for affluent parents raising productive children

- Don't let your children know how wealthy you are.
- Always focus on teaching discipline with money and the art of being frugal.
- Do your best to ensure that your children don't have a complete understanding of your wealth until they are mature, disciplined and in a working profession, providing for themselves.
- Don't discuss inheritance with your children.
- Don't use cash as part of a negotiation, especially with your adult children.
- Distance yourself from your child's family matters.
- Never see your children as competition.
- Remind yourself that each one of your children is their own individual, independent person.
- Always acknowledge your children's achievements, make them feel good about what they can achieve. Don't acknowledge or celebrate simple symbols of success.
- Ensure that your children understand that there is more to life than money. And show them that many things hold more value than money itself.

The Workforce

In the next ten years, there will be a growing amount of money in this country than ever before. Opportunities to serve the wealthy will be greater than ever before. Those who are specialists in meeting the demands and solving the problems of the wealthy will be in great demand. Specialists with the highest skills are more likely to benefit than those who don't have those skills. Specialists who will benefit include:

- Medical and dental care specialists
- Asset liquidators, facilitators and appraisers
- Educational institutions and professionals
- Professional services specialists
- Housing specialists/dwelling products/services
- Fund-raising counsellors
- Travel agents / consultants and bureaus

Get rid of the silver spoon and work hard instead

There really is no magic formula for accumulating wealth. While being self-employed can be a good first step, one must be cognisant of the fact that a majority of business owners actually never see their money accumulate into true wealth.

As a business owner, you will be aware of the success odds, you'll be aware of the competition, the vulnerability of trends and the unknown. And for this reason, less than one in five business owners, who can be considered wealthy, will leave their business to their children to run and own. In order to be a successful business owner, you have to have a real motivation to succeed. You need to want to be self-employed. Successful business owners need to love what they do and take pride in 'going at it alone.' If you're simply handed a business on a silver platter, you are unlikely to have the same drive and desire. It's likely the business will not continue to succeed in the same way.

Simply put, the majority of millionaires are actually modest, don't spend their money on things they don't need and adopt a common sense strategy to wealth building. That's how they became rich in the first place.

One of the biggest lessons from the book is that if you want to become a millionaire then you must learn to budget, save, and invest your money. This means that you need to make a financial plan, create a well-diversified investment portfolio as per your asset allocation strategy, and then stick to it. The good thing is that you don't need to be alone on this journey. You can seek the help of a financial planner who can assist you in determining your risk profile, clearly articulating your return requirements, and then creating a customised asset allocation strategy. Once this is done, you can seek to choose to invest in mutual funds. They can help you diversify your investment portfolio as per your asset allocation strategy by giving you an option to invest in multiple asset classes like equity, debt, gold, etc. They also give you the advantage of having your money managed by expert fund managers. Most importantly, when you invest in mutual funds, you can choose to automate your investments through the Systematic Investment Plan (SIP) route. When you invest in a mutual fund via the SIP route, you invest a fixed amount of money in a mutual fund scheme of your choice. Further, these investments are made as per your chosen time intervals which could be fortnightly, monthly, or even quarterly. The best thing is that you can start your SIP investment with as low as Rs. 500. This ensures that you can start your financial planning journey almost immediately and get on the path to becoming a millionaire.