Pre-funding vs Post-funding: How simple math will save you tens of thousands of dollars in college costs

BY PETER DUNN

Interest - it will either cradle you lovingly in its arms, or it will bear hug you to death. You get to decide which path it will take. This terrifying realization is especially true when it comes to funding your child's education.

You've read the reports, you've seen the news stories and you've heard the radio ads: people with a college education will significantly out-earn those of us without one. While life obviously isn't about money, most folks would rather have a legitimate shot at increased earning potential. As an adult, you understand this, and that's likely part of the reason you want to send your child to college.

Not long after coming to this conclusion, people begin to think about how they are going to fund the higher learning that leads to increased earnings.

There are two primary funding mechanisms for most people, and they both involve interest. Some people choose to deposit money into college savings plans, which offer various opportunities for growth, thus decreasing the amount of deposits it takes to fund a child's education. Others choose to go the student loan route, which results in a college education being more expensive, due to interest. It's not any more complicated than that.

For example, let's say the total cost of a college education is $80,000. If you begin to set money aside for college, and it's fortunate enough to grow, you won't have to pay $80,000 for the college education. You will have paid a portion, but the growth will have paid the rest.

Now, what if you use student loans to fund an $80,000 education? The $80,000 education easily turns into a $90,000 education or more, due to student loan interest.

You will decrease the cost of a college education by contributing to a 529 college savings plan, because the growth within the account will do some of the work for you.

If you were to open a 529 college savings account with a $10 deposit when your child is born, and then deposit $200.00 every month until they turn 18 years old, you'd have $70,155 (based on a 5% rate of return). You will only have deposited $43,200 in the process. Yes, in order to pay for the $70,155 education, you would have only needed to save about $40,000. That's why you want interest working in your favor.

continued on following page

Here's what interest looks like when it's working against you.

At a current undergraduate student loan rate of 4.29%, an $70,000 education funded by student loans will cost the borrower just under $88,000.

Would you rather save $40,000 now for a $70,000 education or pay nearly $90,000 later?

As we strive to educate our children, it's important we begin by making a wise decision based on our old buddy math.

****The calculations used in this article are hypothetical. You may or may not earn a 5% rate of return on your investments. For that matter, you're likely to pay more than 4.29% interest on your student loans.

Peter Dunn a.k.a. Pete the Planner® is an award-winning comedian and an award-winning financial mind. He's a USA TODAY columnist and the author of ten books, six of which were featured in a nationwide launch at Barnes & Nobles stores in January of 2015. He is the host of the popular radio show The Pete the Planner Show on 93 WIBC FM and is a columnist for the Indy Star. Pete has appeared regularly on CNN Headline News, Fox News, Fox Business as well as numerous nationally syndicated radio programs. For more information visit petetheplanner.com. Connect with Pete on Twitter, Facebook, and LinkedIn.