

BUDGET PROGRAM

Mission

- The mission of the budget program is to better educate clients of pitfalls, interest calculations, and proper budgeting.

“Watch the pennies closely and the dollars will take care of themselves.”

Pitfalls

- Credit cards
- Payday loans
- Living outside of your means
- Lack of personal savings
- The “monthly payment” trap
- Rent to own
- Gambling

Credit cards

- The average interest rate for credit cards in the United States is 18.9%.
- The average household in the United States has a balance of \$8,400.00 in credit card debt.
- The average household in the United States pays about \$1,200.00 per year in credit card INTEREST alone
- A \$1,000.00 credit card charge will take approximately 22 years to pay off and will cost a total of \$3,300.00 (Assuming minimum monthly payment at 18.9%.
- The typical credit card purchase will cost 112% more than if paid with cash.
- The typical consumer will actually spend 12 to 18% more if they pay with credit card than with cash.

Credit cards (continued)

- Credit card companies will often allow consumers to pay a minimum monthly payment, which is often around 1 or 2% of the balance. Why?
- This allows the credit card companies to extend the line of credit. For example, if a consumer can pay \$100.00 per month in credit card debt service, the credit card company can extend the line of credit to \$5,000.00 with a 2% payment. If they required a 5% payment, the line of credit could only be extended to \$2,000.00.

Credit cards (continued)

- If the average household has \$8,400.00 in credit card debt at 18.9% and pays the monthly minimum payment, it will take over 64 years to pay off and will ultimately cost \$30,515.00.

Payday loans

- A payday loan is a small, short-term loan that is intended to cover a borrower's expenses until the next payday. Typical payday loans range from \$100.00 to \$500.00 over two-week periods and interest rates can range up to 400%.
- Over two-week periods, the typical loan costs about \$15.00 for every \$100.00 lent. This comes to an annual percentage rate of 390%, but an effective annual rate (EAR) of 3,686%.

Living outside your means

- Most of us are living on a fixed income. Unfortunately, many of us are not living on fixed expenses. In fact, many of us are unsure where our money is actually spent.
- Some of our monthly needs expenses such as fuel, food, etc. fluctuate causing budget deficits. This often leads to other pitfalls such as credit card spending, payday loans, and lack of saving.

Lack of personal savings

- A common rule is to save 10% of your income for savings. This may need to be adjusted based on your personal financial situation.
- Savings should be established for numerous purposes:
 - Retirement
 - Emergency fund
 - Education

The “Monthly Payment” trap

- Have you ever wondered why television commercials often advertise what the monthly payment is, but show the terms and price in fine print?
- Lower payments can be offered, but often have higher loan rates and terms, which result in higher costs.
- For instance, a \$10,000.00 loan at 6.0% can be offered for 36 months at \$304.22, with a total cost of \$10,951.00. That same loan can be offered at 84 months at \$146.09 with a total cost of \$12,271.00, a total of \$1,320.00 more.

Rent To Own

- Rent to own businesses, often called rent-a-centers, offer products such as furniture, appliances, and electronics. They typically offer these products at a relatively low monthly payment over a period of time such as 18 months.
- For a television, you can pay 78 weekly payments of \$8.50 with a final payment of \$37. This equals a total cost of \$700 for a television that would cost approximately \$200. If the same person would save \$8.50 per week, they would have enough to purchase the television at 24 weeks, saving \$500.

Gambling

- The gambling industry has grown tenfold in the United States since 1975
- Over 15 million people display signs of gambling addiction
- Casinos profit over \$30 billion per year while lotteries profit \$17 billion
- The average debt incurred by a male pathological gambler is between \$55,000 and \$90,000.
- 65% of pathological gamblers commit crimes to support their habit
- After casinos opened in Atlantic City, the crime rate in the thirty-mile radius increased 100%

How interest works

- Simple interest can be calculated by multiplying the interest rate by the amount of the loan.
- Compound interest, such as most credit card debt, is similar to simple interest, with the exception that the balance of the loan is revolving and factors in unpaid interest.
- The Rule of 72- When an investment is made, you can determine how long it will take to double your money by dividing your interest rate into 72. For example, if you invest \$100.00 at 6%, you will have \$200.00 in 12 years.

How interest works

- There are numerous avenues to reduce debt such as consolidation loans, consumer credit counseling, bi-weekly payments, and many others.
- One of the most effective practices can be debt stacking. Debt stacking is an approach to debt elimination that identifies a particular debt to eliminate, making minimum payments on the others and making increasing payments on your targeted debt. When that debt is satisfied, the monthly payment that was used for the satisfied debt will then be applied as an additional payment on a different debt. This practice requires discipline to not acquire new monthly debt or expenses.

Bi-Weekly Payments

- A bi-weekly payment is paying half of the monthly payment every two weeks. This essentially results in one extra payment per year. While it does not sound significant, it can greatly reduce your interest expense and term of the loan.
- For example, a \$100,000.00 mortgage for 30 years at 7.0% would result in a monthly payment of \$665.30. A typical mortgage plan would ultimately cost \$139,511.06 in interest alone and take 361 months to pay.
- A bi-weekly mortgage plan would pay \$332.65 every two weeks. This plan would cost \$105,047.45 in interest and be paid in 284 months.
- What could you do with \$34,463.61 and 77 months of debt-free living.

Budget Planning

- Determining your financial status and plan
- Determining your required monthly expenses
- Determining your discretionary monthly expenses
- Determining your debt service expenses
- Prioritizing needs vs. wants
- Developing a monthly budget that will suit your financial plan

Determining your financial status and plan

- Identify your currently assets and liabilities
- Determine the variables of your liabilities
- Prioritize your liabilities and establish a debt elimination plan
- Identify your savings needs
- Establish a savings and investment plan

Determining your required monthly expenses

- Housing
- Food
- Transportation
- Care
- Debt service

Determining your discretionary monthly expenses

- Entertainment
- Cable
- Upgrades (Nicer home, nicer vehicle, etc.)

Example

- John and Bob both earn \$2,400.00 per month.
- They both have \$5,000.00 in credit card debt at 18%.
- They both have \$6,000.00 in restitution at 3%.
- John has committed to getting out of debt. He has elected to purchase at \$5,000.00 vehicle at 10%. He has purchased basic cable. He has also committed to not eating out. His financial plan is to first pay off his credit card debt, then apply debt stacking to then pay off his vehicle and restitution.
- Bob has purchased a \$10,000.00 vehicle at 10%. He is making a \$100.00 per month payment on his credit card. He has expanded cable. He also eats out everyday. Bob has not elected to practice debt stacking.

Example

Expense	John	Bob
Rent	400	400
Utilities	200	200
Phone	60	60
Insurance	100	100
Gas	200	200
Automobile	160	320
Auto insurance	80	130
Cable	35	65
Grocery bill	300	540
Restitution	200	200
Credit card debt	580	100
Entertainment	85	85

Example

- John has committed to paying \$940.00 per month in debt service.
- According to these assumptions, John will satisfy his credit card debt in 12 months, his auto loan in 17 months, and his restitution in 21 months.
- Upon his satisfaction of his restitution debt, he will have \$940.00 per month to use how he chooses for the rest of his life.

Example

- Bob has elected to make the minimum payments on each of his three debts, and has elected not to apply debt stacking.
- Bob will satisfy his restitution debt in 34 months, his auto loan in 38 months, and his credit card debt in 94 months.

Example

- John satisfied his debt in 21 months and paid a total of \$17,036.10, with only \$1,036.77 of that in interest.
- Bob satisfied his debt in 94 months and paid a total of \$27,172.15, with \$6,172.18 in interest.

Closing thoughts

- It is YOUR money. You work for it. Let it work for you.
- Questions?????