Budgeting 101:
How to reduce stress, get out of debt and take control of your finances

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University of Arizona, Take Charge America Institute
What is a Spending Plan?

An income and expense statement sometimes referred to as a budget which records both planned and actual income and expenses over a period of time.

### My Spending Plan

<table>
<thead>
<tr>
<th>November</th>
<th>Planned ($)</th>
<th>Actual ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income (wages)</td>
<td>$2,100</td>
<td>$2,000</td>
</tr>
<tr>
<td>Unearned income (savings)</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td>Savings</td>
<td>-$200</td>
<td>-$155</td>
</tr>
<tr>
<td>Rent</td>
<td>-$1,000</td>
<td>-$1,000</td>
</tr>
<tr>
<td>Student loan payment</td>
<td>-$280</td>
<td>-$280</td>
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<tr>
<td>Food/Supplies</td>
<td>-$300</td>
<td>-$250</td>
</tr>
<tr>
<td>Utilities/Phone</td>
<td>-$150</td>
<td>-$150</td>
</tr>
<tr>
<td>Health Insurance</td>
<td>-$60</td>
<td>-$60</td>
</tr>
<tr>
<td>Transportation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Gas</td>
<td>-$60</td>
<td>-$55</td>
</tr>
<tr>
<td>• Car Insurance</td>
<td>-$50</td>
<td>-$50</td>
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<tr>
<td>Total</td>
<td>$0</td>
<td>$0</td>
</tr>
</tbody>
</table>
Each individual has a unique spending plan

- Based upon the following elements:
  - Values
  - Needs
  - Wants

Need
An essential item required for life

Want
Something unnecessary, but desired

Value
A fundamental belief about what is desirable, worthwhile, and important to an individual
Why create a spending plan?

Reduce Stress

Ensure income can cover expenses  Avoid new debt

Plan for the future

Get out of debt  Achieve financial goals

Pursue your dreams

Let money create opportunities, rather than constraints
People who budget have:

- Reduced financial stress
- Confidence
- Increased Financial Security

Because of reduced spending & higher rates of saving
Why Save?

*Your present self impacts your future self*

By saving money today you will have financial security in the future

**Emergency Savings**
- Cash set aside to cover the cost of unexpected events

**Short-Term Goals & Expenses**
- Pay for items that aren’t part of a typical spending plan

**Financial Security**
- Less stress
- More positive emotions
- Confidence
How Much Money Should Be Saved?

Three - six months worth of expenses in emergency savings

$2,000 monthly expenses $6,000

3 months

Depends on...

Income
Dependents
Job security
Insurance coverage
Pay off debts

- Highest interest rate first OR smallest balance first
Remember: your present self impacts your future self!

Saving money for the future

Giving up the purchase of something in the present
Saved Money Provides For Your Future Self....

... and can increase in value!

Time Value of Money - money available at the present time (today) is worth more than the same amount if received in the future.
What is Interest?

**Interest** – the price of money

When you don’t withdraw interest earned from an account the interest earns additional interest

Compound interest – earning interest on interest
How Does Money Affect the Time Value of Money?

Money = More Money Earned

Principal - original amount of money saved or invested

<table>
<thead>
<tr>
<th>Principal</th>
<th>Future Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100</td>
<td>$115.93</td>
</tr>
<tr>
<td>$1,000</td>
<td>$1,159.27</td>
</tr>
<tr>
<td>$10,000</td>
<td>$11,592.74</td>
</tr>
</tbody>
</table>

3% interest for 5 years
How Do Interest Rates Affect The Time Value of Money?

$1,000 Saved for 5 Years with Compounding Interest

<table>
<thead>
<tr>
<th>Interest Rate</th>
<th>More Money Earned</th>
</tr>
</thead>
<tbody>
<tr>
<td>1%</td>
<td>$1,051.01</td>
</tr>
<tr>
<td>3%</td>
<td>$1,159.27</td>
</tr>
<tr>
<td>5%</td>
<td>$1,276.28</td>
</tr>
</tbody>
</table>

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How Does Time Affect the Time Value of Money?

Time = More Money Earned

College Savings Fund

Felix and his parents
Saved for: 18 years
• Started when he was born
Contributed: $50/month
Total Contribution: $10,800

Savannah and her parents
Saved for: 4 years
• Started when she was a freshman
Contributed: $350/month
Total Contribution: $16,800

Both earned the same interest rate
Both currently have the same balance (about $19,500)
Savannah’s parents contributed significantly more
Time Value of Money Magic!

Initial Investment (Principal): $100.00 at 7% compounding interest

Year 1
Interest Earned: $7.00
Amount Investment is Worth: 107.00

Year 5
Interest Earned: $33.26
Amount Investment is Worth: 140.26

Year 10
Interest Earned: $56.46
Amount Investment is Worth: 196.72

Year 15
Interest Earned: $79.19
Amount Investment is Worth: 275.90

Year 20
Interest Earned: $111.07
Amount Investment is Worth: 386.97

Year 50
Interest Earned: $845.46
Amount Investment is Worth: 2945.70
What would it take to have $1M when you retire?

• **Assume an 8% return and retirement at age 70.

• If you’re 25, you need to invest $200 a month.
• If you’re 45, you need to invest $1,100 a month

• Check out Dave Ramsey’s Investment Calculator to customize numbers for your situation:
  https://www.daveramsey.com/smartvestor/investment-calculator
Spending Plan Development Process

Step 1 - Track Current Income and Expense

Step 2 - Personalize Your Spending Plan

Step 3 - Allocate Money to Each Category

Step 4 - Implement and Control

Step 5 - Evaluate and Make Adjustments

Develop the spending plan

Maintain the spending plan
Personalize Your Spending Plan

How will you develop a spending plan?

What is the intended time period for your spending plan?

What categories will your spending plan include?

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Allocate Money to Each Category

Reference tracking from Step One

Determine what changes to make

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When allocating money consider:

- **Contractual (Fixed Expense)**
  - An amount due each month that is not easy to eliminate or reduce
  - Rent, Internet, Cell phone, **Savings**

- **Non-contractual (Flexible Expense)**
  - Easy to reduce or eliminate
  - Food, Entertainment

- **Trade-offs and opportunity costs**
- **Goals**
- **Contractual expenses**
Personalize Your Spending Plan

**What is your income?**

- Estimate your monthly income
- If in doubt, be conservative.

**What expense categories do you know?**

- Input your debt payments, rent, and contractual bills.
How Much Can You Save?
Identifying Money to Save

Examine current spending

What changes can you make to reduce current spending?

Ask yourself if items are a need or a want

Consider small, often daily, expenses

Consider large, often monthly, expenses

What are ways to reduce spending?
Pay Yourself First

Your present self impacts your future self!

- Save a predetermined amount of money
- Do so each time you are paid
- Do so before using money for spending
- Make it automatic!
Implement and Control

Make your planned spending decisions

Use a control system to stay on track

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Control Systems

- Money management computer software
- Internet-based spending plan program
- Depository institution programs
- Check register system
- Envelope system

Which control system would help you stick to your spending plan?
BUDGETS are flexible!

Net Gain?  |  Net Loss?
---|---
• Add more money to savings or another expense | • Increase income
• Decrease expenses | • Both

A spending plan should have income and expense matching one another (reach zero)

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<td>Income (wages)</td>
<td>$1,200</td>
<td>$1,160</td>
</tr>
<tr>
<td>Savings</td>
<td>-$120</td>
<td>-$120</td>
</tr>
<tr>
<td>Rent</td>
<td>-$450</td>
<td>-$450</td>
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<tr>
<td>Food</td>
<td>-$175</td>
<td>-$157</td>
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<tr>
<td>Utilities/Phone</td>
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<td>-$50</td>
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<tr>
<td>Insurance</td>
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<td>-$40</td>
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<tr>
<td>Entertainment</td>
<td>-$155</td>
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<tr>
<td>Transportation</td>
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<tr>
<td>Gas</td>
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<td>-$53</td>
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<tr>
<td>Car Payment</td>
<td>-$160</td>
<td>-$160</td>
</tr>
<tr>
<td>Total</td>
<td>$0</td>
<td>$0</td>
</tr>
</tbody>
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Evaluate and Make Adjustments

- How well did your spending plan work?
- Is your spending plan helping you reach goals?
- Do you need to make any adjustments?

Step 1 - Track Current Income and Expense
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Is your spending plan helping you reach goals? Do you need to make any adjustments?
Summary

• A spending plan is an important financial planning tool
  ▫ Helps you achieve goals
• Make your spending plan work for you
• Make sure to control, evaluate, and adjust your spending plan

When properly done an effective spending plan creates **wealth**

Wealth- is what is left over once assets are subtracted from your liabilities.
QUESTIONS?
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