

# Unit 3:

## Budgeting, Savings, Reducing Expenses

Read Chapter 3 in the text.

Read Chapters 5 and 10 of The Financial Checkup.

### **Budgeting**

Most people think of negative things when they hear the word "budget". Words like "depressing", "impossible", and "no fun" come to mind. You can still have fun while you are on a budget; you just need to plan for it. Some people think it is like a diet, just telling you what you can't have. I prefer to think of it as a menu. You choose where you want to spend your money. Some people call it a spending plan instead of a budget. If you like that better, feel free to call it that. Budgeting is simply telling your money where you want it to go instead of wondering where it went.

A budget can be as simple as taking your paycheck, paying your bills, and spending what is left. It doesn't need to be hard and confusing; you just need to do it.

Read the information at the following website: [Budgeting: The Basics and Beyond](http://www.ianr.unl.edu/pubs/HomeMgt/g1166.htm) (<http://www.ianr.unl.edu/pubs/HomeMgt/g1166.htm>)

This website, the text, and The Financial Checkup all have steps for budgeting, and they are all a little different. Read all of them and decide the steps you want to take when budgeting.

# Unit 3:

## Why Budgets Fail

I have been a financial educator and counselor for several years. I hear people all the time say that budgets don't work. I have collected a list of reasons why budgets don't work. If you can eliminate those reasons - budgets will work!

### Why Budgets Fail:

1. No personal allowance - everyone in a household needs a personal allowance. I like what Robert Frost said, "No one was ever meant to remember or invent what he did with every cent." I agree! Everyone needs a little money they can use to buy a soda or go to lunch with a friend. The key is to budget for it and then spend only what you budgeted. Even if you can only budget a couple of dollars a week, that is your two dollars and you can do whatever you want with it! Couples get along a lot better if they each have their own spending money. We will talk about children later.
2. No revolving savings - you may do a wonderful job of budgeting . . . until. The "until" can be until the car registration comes, until Christmas, or until tuition is due. Those types of irregular expenses can cause havoc on any budget. You just need to plan for those irregular expenses. Read chapter 5 of The Financial Checkup.
3. No emergency fund - if you have an emergency that costs money and you have nothing to fall back on, you have to take money away from your regular expenses to pay for it. It is very difficult to stick to a budget when this happens. Having an emergency fund is one of the most important things you can learn from this class.
4. No miscellaneous category - unexpected things seem to pop up every month. It helps to have a miscellaneous category in your budget. If you haven't used this money by the end of the month, you could roll it over to the next month in case something bigger happens next month, or you could spend it on something you have wanted to buy.
5. No evaluation - lives change and so should budgets. If you try to use the same budget for many years, you will not be able to stick with it. Inflation increases the cost of living; children grow and require different expenses, incomes change, and goals change. There are many reasons to evaluate your budget almost on a monthly basis and make necessary changes.
6. Negative attitude - this one can ruin a budget before it gets started. If you asked a contractor to build you a home and he/she said, "OK, but it won't stand when I am done," would you have them build you your home? Of course not. Many people say, "Alright, I'll try a budget but I know it won't

work." Well, they are right. Your attitude can play a big part in the success of your budgeting experience.

# Unit 3:

## Types of Budgets

There are several different ways to budget. Some people may tell you that their way is the best and only way to budget. After working with many people, I can tell you that the best way is the way that works for you. Some people do well with a strict, more in-depth budget. For others, that is budget suicide. They need a way that is simple and easy. Try some different budgeting systems and find one that works for you.

Read the information on the following websites:

- [Money Management Recordkeeping](http://www.ianr.unl.edu/pubs/HomeMgt/nf5.htm)  
(<http://www.ianr.unl.edu/pubs/HomeMgt/nf5.htm>)
- [Using a Check Register to Track Your Expenses](http://montana.edu/wwwpb/pubs/mt8703.pdf)  
(<http://montana.edu/wwwpb/pubs/mt8703.pdf>) --To view this file you must have Adobe Acrobat Reader installed on your computer (opens a new browser window). If you already have acrobat installed and it comes up with a blank screen try opening acrobat first, and then click the file link on this page.

The envelope system works well for some categories but not all. You won't want to put your rent or mortgage payment in an envelope. It works well for smaller amounts that you can control. We use it for clothing. Before we started using it, my husband and I would need clothes but we didn't really budget for them. When we needed them it always hurt the budget. Now we each get a set amount each month. We can spend it each month or save up for bigger items.

# Unit 3:

## Budgeting Assignment

Read chapter 10 of The Financial Checkup. After tracking your expenses for one month, examine your spending. If you liked how much you spent in each category you can use that same amount for budgeting. If you didn't like it, you can adjust the amount to be what you would like to spend. Copy the budget worksheet and fill out the column "budgeted". This is what you want to spend for the next month. Put zeros for the categories you won't need. Make sure you don't plan to spend more than you plan to bring in.

For the rest of the month keep track of what you spend even if you already tracked the month before. This is a little different than tracking. You don't need to write down every single expense, you just need to know how much you spent. For example, if you have \$10 for personal allowance, you don't need to write down where that goes, just write down if you spent it all or have some left. If you use the envelope system, you will know how much you spent by looking at how much is left at the end of the month. You can also keep track in your checkbook. If you liked tracking everything, go ahead and continue that method.

Write down what you actually spent in the "actual" column. Then you can figure the difference between what you budgeted and what you actually spent in the last column. If you have any questions, please contact me.

# Unit 3: Savings

How are you doing with savings? The nation as a whole is not doing very well right now. In about 1992, as a nation we started a decline in our savings. In 1992 savings was 5.7% of our disposable personal income. This is what it has done since then:

1993 4.4%

1994 3.5%

1995 3.4%

1996 2.9%

1997 2.1%

Go to the following website and click on "highlights" of the Personal Income Section. Look at the personal savings rate below the graph to see how we are doing now.

[Bureau of Economic Analysis](http://www.bea.doc.gov/bea/glance.htm) (<http://www.bea.doc.gov/bea/glance.htm>)

A negative number means that we are spending more than we are making. The last time our nation had a negative savings rate was during the Great Depression. Why aren't Americans saving more? There are many theories. Credit is easy to get. The economy has been good for many years and we think we will always be able to have a job, pay our bills, and spend all of our income. That type of thinking may get us all in trouble.

When we get to the unit on credit, you will see that we pay much more for an item if we buy it on credit and pay interest on it. If we would all save for purchases we would have more to spend (or save). I hope you are all starting to read *The Wealthy Barber*. What does the barber say about savings? How much does he recommend you should always save?

Chapter 5 of [The Financial Checkup](#) talks about savings. Make sure you read it.

Read the information on the following website: [Thrift Living: News you can use - Don't Borrow, Save Your Money for Future Goals or Emergencies](http://www.urbanext.uiuc.edu/thriftyliving/tl-borrow.html) (<http://www.urbanext.uiuc.edu/thriftyliving/tl-borrow.html>)

Some people ask me if it would be better to put extra money toward paying off debt or in savings. There is not a clear cut answer for that. First of all, do you have any savings? If you don't, I would definitely put it in savings first. If you do have some savings, how much interest are you paying on your debt? If it is a credit card at 18% interest or higher, it would most likely be good to pay off that debt. If it is a lower rate on something like a house or car, you may want to split

the money. Put some toward debt and some in savings. When we get to mortgages, we will talk more about paying a mortgage off faster.

### **Revolving Savings Worksheet**

You can work on the revolving savings worksheet at any time. As I mentioned in the budgeting section, a revolving savings account can help you maintain a budget. Read chapter 5 of The Financial Checkup. Copy and fill out the revolving savings worksheet with your own information. If you have any questions about it, please contact me.

# Unit 3:

## Reducing Expenses

You may find as we discuss things in this class that you just don't have enough income to reach all the goals you wish to reach or even just to pay all your expenses, especially while you are a student. When you find that your income is less than your expenses, you have three options:

1. Increase your income.
2. Reduce your expenses.
3. Do a combination of both.

Most of you are probably in school so that you can eventually increase your income. Some people find that they need to take on a part time job just for a few months to clear away some debt. Increasing your income can be a very good way to find the money to accomplish your goals. Sometimes you don't have the time or means to increase your income and then you need to look at reducing your expenses. Paying off debt is an excellent way to do that. You may want to reduce in other areas in order to find the money to pay the debt off quicker. Following are some ideas that students have suggested in my classes for reducing expenses:

- ✓ Limit impulse buying by not carrying cash or credit cards (whichever is the problem). Take 24 hours to think about larger purchases.
- ✓ Take a list to the grocery store and stick to it. Use coupons if you would really buy the product. Shop sales but don't run all over town chasing down sales while using a lot of gas.
- ✓ Understand marketing and advertising. They want you to think you NEED it.
- ✓ Ask a friend for help. Take them shopping with you so they can help you get ONLY what you need.
- ✓ Know how grocery stores are set up - the milk and bread are always at the very back so that you will walk past other items and buy them also.
- ✓ Spend more at the grocery store and less at fast food places. We often run to get fast food because there is nothing in the house to eat.
- ✓ Try shopping at outlet stores, discount stores, and thrift stores.
- ✓ Be careful with free products. Is there something attached that has a price tag?

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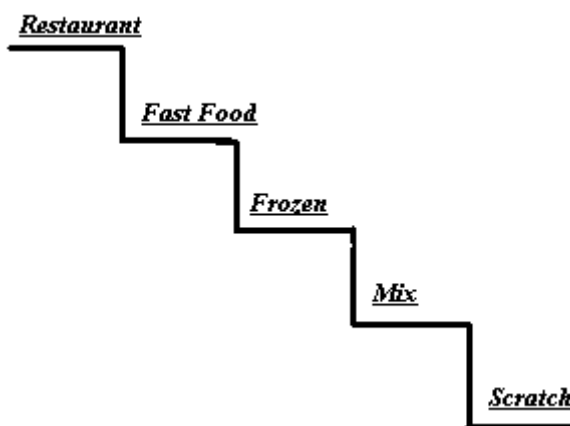
## Step-Down Principle

Another way to reduce expenses is the Step-Down Principle. You can use the Step-Down Principle for one month for the you-pick assignment. Read the syllabus for more information.

### The Step-Down Principle

Do you need to reduce your debt load or save more but can't seem to find the money to do it? The Step-Down Principle is a simple, easy way to reduce expenses. By reducing expenses you can find that needed money to reduce debt or save more.

To use the Step-Down Principle, imagine a staircase. Think of a purchase you will be making and list all the different ways to make that purchase. Put the most expensive way on the top step. Then list the next most expensive way to purchase on the next step and continue on down to the least expensive way on the bottom. For eating, the top step might be a restaurant. The next steps might include a fast food outlet, frozen or already prepared food from the grocery store, mixes from the grocery store, and finally cooking from scratch.



Decide which step you are most likely to use for that purchase. Then, see if you can step down one or more steps. The savings can be tremendous. For example, four pancakes might cost about \$3.49 at a restaurant, plus a tip! At a fast food restaurant they may cost about \$1.99. Frozen pancakes from the grocery store might cost about 78 cents, a mix 48 cents and cooking them from scratch might cost only about 16 cents. If you were planning on buying pancakes at a restaurant but stepped down to buying a mix and cooking them at home, you could save 78%! Even if you do not cook from scratch, you can still save a lot of money by stepping down one or two steps.

The Step-Down Principle works well with clothes. The top step might be purchasing at an expensive department store. The next few steps would include less expensive stores, sales, thrift stores and maybe even hand-me-downs.

Quality is of course an issue to be considered. However, sometimes high quality clothes may be purchased at thrift stores for a fraction of the department store cost.

Try stepping down for entertainment. Instead of having the whole family go to a first release movie, can you go to a second release movie, rent a video, or better yet, play sports or games together? Can you use it for transportation? Is there a bus system available? Do you have a bicycle that can be fixed up and used? With that comes the added benefit of exercise.

The Step-Down Principle helps reduce expenses without cutting out the purchase all together. If you really enjoy eating out but feel that it consumes a large portion of your budget, try stepping down the number of times you eat out. If you usually eat out 12 times a month, write 12 on the first step and lower numbers on the lower steps. Eating out once a week might be a good alternative. Or try reducing the amount of food you purchase at the restaurant. Take away the appetizer, the drink, or the dessert. Maybe you could enjoy the evening only ordering dessert.

Have fun trying the Step-Down Principle. Get others involved. Watch your expenses go down as you "step down" to better finances.

# Unit 3:

## Teaching Kids About Money

Since this is a "family" finance class we will spend a few minutes talking about teaching children good financial principles. Try to teach your children real life information. It is easy to want to make life easy for our children. But in doing this, sometimes we are actually hurting them. They will eventually go out into the real world and have to live by its rules. That can be pretty harsh for someone who has never learned how finances work.

### Allowances

Some experts differ on whether or not children should receive allowances, but most of the ones I have heard recommend giving allowance. This is a great way for children to learn to budget their money and make mistakes while the consequences are smaller. It is better to give children an allowance and then require that they pay for their own activities. Some parents give larger allowances and require that the children pay for clothes, school lunch, and other things besides activities. If you don't give allowances but pay for all of their expenses including activities, they will learn that money is always there when they want it. Is this something you want them to learn?

One of my sons always spent his allowance as soon as he got it. It was often on things I was not excited about either, like candy. Later in the month when his friends would call to see if he could go to a movie or some other activity, he would ask me if he could go. I would respond with, "Do you have the money?" He wouldn't be able to go because he didn't have the money. This was a good way to teach him about budgeting and not spending all your money at the beginning of the month. I am happy to say that he is much better about spreading out his spending and planning for things (although he still buys candy - sigh).

Should allowances be tied to chores? Again there is some controversy on this matter. If you tie the allowance to chores, how much is each job worth? And what if they don't care about the money, do they not have to do the chores? I prefer to not tie allowances to chores. The children get the allowance because they are part of the family. They do the chores because they are part of the family. Now those of you with children probably know that they usually need something to motivate them when they don't want to do their work. We tie the chores to privileges. They can't play, watch TV, play computer games, etc. until their work is done. You will have to see what works best for you.

One of the best ways I have seen to help them learn about simple budgeting is to get small jars, boxes, or some kind of container that are labeled for different places they want to put their money. One container needs to be for spending, the rest you can decide on as a family. Here are some suggestions: savings for a

goal, long-term savings, charity, or vacations. When you pay allowance, pay it in small bills and coins so they can easily divide it into each container. There are many other concepts you will want to discuss with your children such as compound interest and the time value of money. As they get older it will be very important that you teach them about some of the concepts we will discuss in this class. Many teenagers have negative marks on their credit histories before they even know what a credit history is or how important it is to keep it clean. Many schools do not offer financial education as a required class. If your children are going to learn these important concepts, it is probably up to you!

Read the information on the following websites:

- [Thrift Living: News you can use - Parents Help Children Learn about Money](http://www.urbanext.uiuc.edu/thriftyliving/tl-childmoney.html)  
([www.urbanext.uiuc.edu/thriftyliving/tl-childmoney.html](http://www.urbanext.uiuc.edu/thriftyliving/tl-childmoney.html))
- [About Money and Children](http://www.ianr.unl.edu/pubs/homemgt/g1164.htm)  
(<http://www.ianr.unl.edu/pubs/homemgt/g1164.htm>)