3 STEPS TO
FINANCIAL RESILIENCE
ENDING THE PAYCHECK-TO-PAYCHECK CYCLE
MANISHA THAKOR MBA, CFA, CFP

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ABOUT

A nationally renowned financial literacy advocate, Manisha Thakor is Vice President of Financial Education at the Seattle-based wealth management firm, Brighton Jones. Her mission is to help clients “Live A Richer Life” – literally and figuratively.

MANISHA THAKOR, MBA, CFA, CFP

Manisha is the co-author of two critically acclaimed personal finance books: ON MY OWN TWO FEET: a modern girl’s guide to personal finance and GET FINANCIALLY NAKED: how to talk money with your honey. Manisha is a member of The Wall Street Journal’s Wealth Experts Panel, sits on Faculty at The Omega Institute, and serves on the board of The National Endowment for Financial Education.

Manisha’s financial advice has been featured in a wide range of national media outlets including CNN, PBS, NPR, The Today Show, Rachel Ray, The New York Times, The Boston Globe, The Los Angeles Times, Real Simple, Women’s Day, Glamour, Marie Claire, Cosmopolitan and Women’s Health.

Manisha earned her MBA from Harvard Business School in 1997 and her BA from Wellesley College in 1992. She is also a CFA charterholder and CFP® practitioner. Manisha lives in Portland, OR where she revels in the Third Wave Coffee scene and the stunning beauty of the Pacific Northwest. Her website is MoneyZen.com.

WELCOME TO 3 STEPS TO FINANCIAL RESILIENCE

If you're here, you're probably feeling a bit in over your head financially. Whether you're struggling with debt, frustrated with balancing your budget, or reeling from an unexpected expense, know that you are not alone.

The good news is that there's a path you can follow to lead you back to a healthy financial place, and this 3-step program will be your GPS on your journey back to stable ground.

Take your time on each step. This program is designed to meet you wherever you are in your financial journey.

This program will help you start:

Reducing your debt

Balancing your budget

Saving for the future

AND create a brighter financial future for you and your family through Financial Resilience!

WHAT IS FINANCIAL RESILIENCE?

Before we get started, let's better understand what being Financially Resilient means so you can start envisioning your goals.

Most of us are not taught personal finance in school. When we enter the workplace, earn money, and manage our own finances, we do the best we can by looking around and seeing what other people are doing with their money. Or maybe we just trust that the financial institutions that provide us loans, mortgages, and credit cards have safeguards to keep us from getting in over our heads.

Unfortunately not know how to properly manage your money can land you in a financially fragile spot. Being financially fragile is the inability to come up with $400 immediately in an emergency, or $2000 within 30 days for an unexpected cost. If you're currently in this position, know that you are not alone and this guide will help you start the journey.

Our goal for this program is to help you create financial resilience in order to remove a big stressor from everyday life!

When you're financially resilient, you have the peace of mind to enjoy life with an informed sense of what you can and can't afford, and the mental relief of knowing that you'll be able to handle many of life's unexpected curveballs.

HOW DID I GET HERE?

Whether it's credit card balances that feel out of control or a large debt like a mortgage or student loans, having too much debt can be incredibly stressful.

Society is changing rapidly, and you're not alone in your financial fragility. Many people are finding themselves struggling to the tone of almost 1 trillion dollars in debt in the US alone.

The most typical causes of debt are credit cards, housing and transportation, and medical bills. If you're in over your head in one or more of these categories, don't give up hope. The first step towards reducing your debt, is understanding how much you have.

Use this space to list all of your debt balances, along with their interest rates. This simple exercise can make it feel more manageable than seeing it across a dozen websites and spreadsheets.

Source	Dollar Amount Owed	Min. Monthly Payment	Interest Rate

TO CONSOLIDATE OR NOT

There are several different ways to consolidate (reduce your monthly payment) with some riskier than others. Let's take a look at each along with the associated risks so you can make an informed decision.

1 A.) **Using a traditional for-profit debt consolidation company** to roll your existing loans into one new loan is the most common, but the riskiest. You then pay off the new loan over a longer period of time or with a lower interest rate, reducing your monthly payments.
Risk: By paying back your loan over a longer period of time, even with a lower interest rate, you will likely pay more interest because of the longer loan term.

1 B.) **Using a "Fintech" consolidation company** to lower your interest rate and consolidate multiple loans into one.
Risk: You still have to pay off your primary balance in the same amount of time. That said, if your interest rate drops, the total amount of interest paid over the term of that loan will be substantially lower.

2.) **Working with nonprofit credit *counseling* firm** is another option, which negotiates with your debt holders on your behalf, to lower your rates or extend your payoff time.
Risk: You can lower your monthly payments for short term relief, but you can end up paying more in interest over a longer repayment time.

3.) **Transferring your debt to a zero-interest credit card** with the hope of paying the debt off before the promotional period is up and you start being charged interest again.
Risk: Watch out for the fine print. For example, any new purchases made on the card beyond the initial transfer amount may be subject to a high interest rate. Also, when you make payments to the card, the fine print may say that your payments are first applied to the 0% interest debt first, NOT the higher interest debt you've added on - thus restarting the debt spiral.

TO CONSOLIDATE OR NOT

So, should you consolidate?

If reducing your monthly payment from $360 to $240 is a lifesaver, maybe consolidation is still looking pretty good, and that's okay. If you can put that extra $120 a month to good use then paying an extra $1500 over 5 years can be a worthwhile cost.

The takeaway here is that it's important to fully understand the costs of consolidation. The offers marketed are not as easy and simple as they're made out to be, and they don't address the underlying problem of an imbalance between your assets and debts.

CREDIT CARDS

For many people this first step of reducing your debt is the most powerful of the three steps in this course. We'll take them one at a time starting with credit cards.

Time to put your earlier work into action. Take your credit card balances and interest rates from the exercise on page 6 and let's figure out an amount that you can afford to pay towards down your credit over time.

Add up all of the minimum payments of your cards and start applying one of these strategies:

1) Pay whatever you can above the minimum payments, towards your highest interest card. If you have some that are 8% and some that are 18%, pay extra towards the higher interest cards first! You'll pay down your debt even faster and be charged less interest this way.

2) Pay off your lowest balance card first, then try to put that card away and stop using it. The benefit here is more psychological. If you have multiple cards all with revolving balances, managing all those payments can create extra stress. By focusing on paying off the lower balance cards first, you give yourself a quicker sense of having made progress, and a less cards to worry about paying.

If you're not sure how much you can afford to pay monthly towards your credit cards, we'll take our deep dive into budgeting during Step 2 of this program.

Be sure to call your credit card company to make 100% sure that your extra payment is being used to reduce your outstanding remaining balance.

HOUSING & TRANSPORTATION

Housing and cars can be expensive!

Housing debt is almost $10 trillion or 70% of all outstanding consumer debt in the U.S. Auto loans make up another 9% of U.S. consumer debt, with their sum falling right between the outstanding aggregate amount of all credit card debt and all student loans.

Debt Reduction Strategies

Lenders often present the maximum amount that they will lend you as the amount that you can afford to borrow. But they are actually telling you that this is what they will lend you, not that that the figure represents the maximum you should be borrowing to keep your budget in balance.

If you have a mortgage or car payment that you're struggling to meet, that's a pretty clear sign that you may want to give serious thought to downsizing.

This can be a difficult and painful decision. But the benefit is that you can downsize your monthly payment without paying more interest or falling victim to other refinancing or consolidation traps. Whether you buy a cheaper house, decide to rent instead of buy, or sell your car to buy a used model, having a lower monthly payment for housing and transportation will be a huge weight lifted off your shoulders. It will make you less stressed about missing payments, and leave more room in your budget for paying down other debt, or even putting away some savings!

We'll cover how to identify whether your current payments are sustainable or not in Step 2.

MEDICAL BILLS

Medical bills are a double whammy. First you or a loved one had a health issue that was probably scary, and now you have a bill for it that you can't afford to pay?

Debt Reduction Strategies

Medical debts can be quite large and very stressful, but one upside is that most medical institutions are not predicated on a financial model that is intended to bankrupt you.

This means that our first step should be to contact the medical provider to see if they are willing to work with you to come up with a win-win payment plan.

For example, some medical payment plans allow you to pay a large bill in smaller monthly payments, rather than all at once within 30 days, and without accruing any interest. Many people are not aware of this option and do not exercise it, as it's not well advertised with a clear set of rules that all providers follow.

How to do this!

Call up the billing department and simply let them know that you can't afford to pay the whole thing at once and would like to know what your options are for paying over time. The important part is to start a payment plan before your bill becomes delinquent and is sent to a collection agency, and to continue making timely payments once you've started a payment plan.

STUDENT LOANS

If you've taken on student loans that aren't manageable, let's discuss how to focus your repayment efforts.

The main difference between deferment and forbearance is when some federal loans are deferred, interest also stops accumulating, which is a huge bonus! When you defer some other loans, interest continues to accrue while your payments are paused, so it's a good idea to continue making interest payments so your debt doesn't grow while its in forbearance. Deferment and forbearance are safer and smarter options than consolidation, but like consolidation, they are only a band-aid fix for extreme financial hardship.

Debt Reduction Strategies

If you have a mix of both federal and private loans, the most important thing is to never commingle them. The flexible payment options of federal loans are always a better option than consolidation.

In the long term, signing up and getting approved for "income-driven repayment" of federal loans may well be the best way for you to make sustainable monthly federal student loan payments. With income-driven repayment, the government calculates a monthly payment that is meant to be affordable for you based on your income.

For private student loans, some lenders now offer income-driven types of repayment, but many do not. Before considering consolidating your private loans, first look into income-driven options, as they may be smarter solutions if your lender offers them. Keep in mind that it's in your lender's interest to help you continue making consistent payments, and there is no penalty for calling them to inquire about more flexible repayment options.

If they don't offer any relief, consolidation may be your only option, as student loans can't be dissolved in bankruptcy. If you consolidate student loans, always remember to only consolidate your private loans, and to read the fine print and calculate the additional interest cost of your lower monthly payments before you sign on the dotted line.

HEALTHY SPENDING

Now that you've taken your first steps towards debt reduction, we'll turn to the other half of the financial puzzle – budgeting or Step 2 of the program.

Let's first identify what a well-balanced budget actually looks like. *The easiest way to do that is with the 50/30/20 rule where you aim to devote 50% of your after-tax income to NEEDS, 30% to WANTS, and 20% to SAVINGS.*

Needs:
Your spending essentials such asl housing, transportation, food, insurance, household items, and child care

Wants:
You put everything else in here – all the "fun stuff" like eating out, going to a movie, or new clothes

Savings:
In here you have your emergency fund savings for unforseen circumstances, near term savings for things like a car down payment or a wedding, and longer term retirement savings

Saving while living paycheck-to-paycheck? If you're rolling your eyes you're not alone. Traditional savings are often the first thing to go when money is tight. BUT, an important mindshift to make is that if you're financially fragile and in debt, paying down debt should be considered a contribution to your savings.

HOW MUCH CAN I AFFORD?

Determine Your Income

Let's start to applying the 50/30/20 rule to your own situation! This way, you'll have a much clearer sense of how much you can afford to spend in each area based on your own unique situation.

For this exercise, outline what an *ideal* budget on your income looks like below and we'll compare it to your current spending on the next page to address any imbalances.

List your income including deductions like 401k and insurance

DESCRIPTION	AMOUNT
Take-home pay	
Health insurance premiums deducted from your paycheck	
Retirement contributions deducted from your paycheck	
Additional income	
TOTAL INCOME:	

HOW MUCH CAN I AFFORD?

Determine Your Income

Using the 50/30/20 rule, figure out how much you have for each category. *This is what your ideal budget should look like each month based on your after-tax income.*

50% 30% 20%

Needs: Wants: Savings:

Example: Take your monthly after-tax income and break it out into 3 buckets: 50%, 30%, and 20%. If you have $5,000 to spend, $2500 goes to needs, $1500 goes to wants, and $1000 should go towards savings or paying debt.

HOW MUCH CAN I AFFORD?

With your income apportioned to needs, wants, and savings, let's break them down to some slightly smaller items next.

WORK THIS WAY

Start from your income and work your way down without exceeding it

INCOME	DESCRIPTION	AMOUNT BUDGETED
50% NEEDS: $______	GROCERIES	
	CAR PAYMENT	
	CAR INSURANCE	
	GAS	
	CHILD CARE	
	UTILITIES	
	HOME/RENTER'S INSURANCE	
	HOME REPAIR	
	RENT/MORTGAGE	
30% WANTS: $______	EATING OUT	
	SUBSCRIPTIONS	
	MEMBERSHIPS	
	HOBBIES	
	NON-ESSENTIAL SHOPPING	
	ADDITIONAL "NEEDS"	
20% SAVINGS OR DEBT PAYMENT: $______	RETIREMENT CONTRIBUTIONS	
	EMERGENCY FUND SAVINGS	
	STUDENT LOAN PAYMENTS	
	CREDIT CARD PAYMENTS	

BALANCE YOUR BUDGET

Now that you know what your *ideal* budget looks like based on your income, time to look at how you're currently spending in order to identify any imbalances between your actual spending and what you can afford to spend. No need to stress, we'll then look at the best actions to get your budget back on track!

INCOME NEEDED	DESCRIPTION	AMOUNT SPENT
TOTAL NEEDS: $______	GROCERIES	
	CAR PAYMENT	
	CAR INSURANCE	
	GAS	
	CHILD CARE	
	UTILITIES	
	HOME/RENTER'S INSURANCE	
	HOME REPAIR	
	RENT/MORTGAGE	
TOTAL WANTS: $______	EATING OUT	
	SUBSCRIPTIONS	
	MEMBERSHIPS	
	HOBBIES	
	NON-ESSENTIAL SHOPPING	
	ADDITIONAL "NEEDS"	
TOTAL SAVINGS OR DEBT PAYMENT: $______	RETIREMENT CONTRIBUTIONS	
	EMERGENCY FUND SAVINGS	
	STUDENT LOAN PAYMENTS	
	CREDIT CARD PAYMENTS	

WORK THIS WAY

Start from your spending and work your way up to the total.

Don't worry if this exceeds your actual income

STRATEGIES FOR BALANCING

If you're one of the many hard-working folks finding yourself living paycheck-to-paycheck, it's a stressful situation you know. If you spend more than you can afford in either your Needs or Wants buckets, it can leave you without enough money to pay down debt and lead to that debt ballooning over time.

So, how can you make room in your budget to pay down debt and save a little for a cushion in case of emergency?

If you're close to in balance, you may be able to get there with a few of the smaller tweaks, like:

- Cancelling unused memberships like the gym
- Cutting back on eating out and instead cook at home
- Switching to a cheaper cable or streaming plan
- Calling your cell phone company to ask about promotions
- Taking a one week vacation from clothes shopping

If you're really unbalanced, it's a good idea to consider a larger rebalancing. This means thinking about the bigger, harder choice such as downsizing to a smaller house or apartment, or selling your car and buying a cheaper used one.

These big changes are not ones to immediately do after reading this, but it's something to seriously consider if you're spending a lot more than you make each month. Putting off hard choices can make a bad situation even worse.

AFFORDING TO SAVE

Welcome to the Step 3 of your Financial Resilience journey! We've already addressed how to sustainably pay down debt and learned how to analyze our budgets to address the imbalances. Hopefully you're starting to feel like you're both armed with more knowledge than when you started and that you have some specific, tactical actions you plan to take right now.

In this final step, we'll look at how to make progress towards *saving*. It may feel like a pipe dream right now, but it's important to have goals in mind and know what to shoot for after you pay down your debt and balance your budget.

Saving is the third key step to achieving sustainable financial resiliency – it's what actually gives you the resilience, or safety net, to withstand life's inevitable unexpected financial road bumps without getting back into debt.

Your first thought might be "How can I possibly afford to save anything while I'm still underwater?" Like we just discussed, you should be devoting most of your 20% "savings" to paying down debt at this stage, but with every dollar of debt you pay down you ARE saving yourself from having to pay interest on that debt going forward so you can and should feel great about that progress!

LEAKING MONEY

The first step towards being able to save anything significant down the road is to establish the habit now, by finding any "leaking money," you can divert into your savings.

"Leaking money" is all the money we spend on things that don't bring us joy. Some examples include martial arts or piano lessons that you think is building character and culture in your child, but they don't enjoy it and it stresses you out to nag them to practice all the time. Or maybe it's something tiny like an online subscription you totally forgot about until you checked out your bank statement again in the last section.

Continued on next page...

LEAKING MONEY CONTINUED

The most powerful way to identify your leaky money is to ask yourself the question "how much joy am I really getting out of this?" If the answer is not much, that's a quick win. You've got a leak that can be immediately plugged.

Another way is to think about how many hours you'd have to work to pay for that item. A quick way to do that is to take your after tax monthly pay, multiply by 12 and then divide by 2,000 Example: $5000 * 12 = $60,000. Divide $60,000 by 2,000 and you have $30/hour. Now if you see something that costs $300 you can ask yourself if it's worth spending 10 hours of your hard work on.

Give it a try! Challenge yourself to find at least 5 leaks in your budget right now that you can start your savings with:

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CREATE AN EMERGENCY FUND

Creating an emergency fund might feel like a far-off goal and that's okay at this stage. To keep yourself motivated, remember that once you've got your emergency fund in order, you will have officially achieved Financial Resilience! You'll have the funds saved to accommodate an unexpected financial shock without going into debt or upending your life.

3-6 Months of Essentials

The size of your emergency fund depends on your family size and income situation. If you have two stable incomes, aim for 3 months and if you have one income, aim for a 6 month emergency fund. Based on your budget from the previous section, what are your own monthly necessities, based on needs plus minimum debt payments? That's how you'll find your recommended emergency fund. It's okay if it's a number that feels like a long way off – you might not get there for a few years, but you will get there if you continue following the 50/30/20 rule and slowly saving towards it.

In the meantime, stake out some landmarks to shoot for on this long saving journey.

The first goalpost is $400. If you can only put in $25 or $50 a month for now, you'll be there in about a year. If you can really tighten your belt for a few months, you could be there much sooner. With this amount saved, you'll have conquered the first part of financial fragility – having $400 immediately in an emergency. Congratulations!

But we're not going to be satisfied there – the goalposts are going to keep moving. The next amount to shoot for is $2,000. This will allow you to cover a larger emergency, and if you save this much you'll have fully conquered financial fragility! If you can manage to increase your monthly contribution to $200, you can be there in a year, and even if you take longer, saving slowly to $2000 is a great accomplishment!

From there, you can set a goal of $4000 and then $6000. You can think of these either as 2 or 3 years of financial emergencies. After that, set yourself goals in months of necessities, so you'll have a 1-month emergency fund, a 2-month emergency fund, etc, until you reach that 3 or 6-month full emergency fund.

SAVE FOR THE FUTURE: COLLEGE

This last section could be its own program! To keep things simple, we'll take a straightforward look at some simple recommendations to start saving for retirement and higher education. There are some key big picture best practices when it comes to long-term saving that are good for everyone to be aware of so that's what we'll focus on.

Don't save for college

This little secret may sound harsh or controversial but is actually incredibly pragmatic. The secret is, don't save for your children's higher education until you're fully maximizing your own retirement savings. If you're living paycheck-to-paycheck, this may mean you only manage to save for your own retirement and not for your children's college. This may sound cold and unfeeling on the surface, so let's look at why it makes sense for both you and your loved ones.

Paying for college for your children and funding yourself through retirement are two giant expenses that compete directly with each other. Yes, the payout for college is earlier than retirement, but you're saving for both during your prime earning years. It's rare to be able to save the full amount needed for both a comfortable, independent retirement and to fully pay for your children's college. If you have to choose, the smartest long term saving you can do is for your own retirement.

Retirees who don't save adequately for themselves end up relying on their adult children for financial support. This means placing a massive burden on your children, often at the same time they are facing significant financial challenges of their own.

SAVE FOR THE FUTURE: RETIREMENT

Once you've got a balanced budget and an emergency fund built, you'll be in great shape to start contributing towards retirement.

Let's use "Joy" as example of what it looks like to invest 20% of your income. Joy makes $5000 a month, so the 20% or $1000 she is investing would grow over time if she contributes it to her 401k until she reaches retirement. Let's say she's starting a little late at age 40, with no money saved for retirement, and she plans to retire at 67. We'll assume her average annual return will be 7% after inflation.*

With those assumptions, Joy's savings at retirement will be $950,000, so just shy of $1 million! Even more incredible than this is that she will have only put in $324,000, and about $630,000 will be purely from the growth of investing her savings. If you can't contribute that much – say you can only contribute $500 a month over the same time – your savings at retirement will still be $316,000. To determine how much you might be able to save and decide on some retirement goals for yourself, check out Dave Ramsey's retirement calculator.

TYPES OF RETIREMENT ACCOUNTS

What about where to put the money? Let's look at different types of retirement accounts.

401k's are the most common type of retirement account, which are set up by companies for their employees. You can contribute to them from your paycheck before taxes.

IRA's are a good option for those without an employer-sponsored 401k. With both a Traditional 401k and a Traditional IRA, you can make untaxed contributions, but when you withdraw money during retirement, you'll pay income taxes on those withdrawals. The main difference of a Roth IRA is that the taxes are in reverse. You don't get a tax deduction for contributions that you put in, but then because you've already paid taxes on your contributions, you can withdraw them tax-free during retirement. This is a good strategy if you feel like you can afford to pay the taxes better now than in retirement, or if your taxes are already low because of other factors like income or dependents. Traditional IRAs make sense if you're struggling and could really use a bigger tax refund.

*(1) there is no guarantee past returns will repeat in the future, (2) that 12% figure is BEFORE inflation; depending upon inflation the "real" rate of return could be closer to 8-9%, and (3) in the following example we are assuming Joy is invested in 100% stocks during this whole time period.

SAVE FOR THE FUTURE: INVESTING

This could be its own program, so for now we'll cover the basics. Cash in retirement accounts can be invested in the stock and bond markets rather than just sitting in a savings account accruing a measly few tenths of a percent interest.

Investing in stocks and bonds always carry risks, that's why they come with the potential for earning a higher return than keeping your money in a low interest savings account. You have the potential for (but not the guarantee of) higher long run returns by investing in stocks and bonds for the long run because you are being compensated to take on extra risk.

Manisha's favorite way for people to benefit from retirement savings without having to become an investing expert is to invest the money in your 401k and/or IRA in what is called a "**target retirement date" investment**. Target date retirement funds are designed by financial institutions offering them to have a different mix of stocks and bonds depending on how close you are from retirement.

For example, when you're 30 years away from retirement, your savings will be invested in more stocks than bonds. By contrast, as you get closer to retirement your investment mix will shift more towards bonds, which historically have had lower risk - and thus lower return - than stocks over the long run. When you invest in a target date fund you end up owning pieces of literally thousands of different stocks and bonds so it's a great way to make sure all your eggs are not in one basket - a powerful and important concept that is called "diversification" in official financial speak.