

Seven Steps To Credit Literacy



The **Seven Steps To Credit Literacy Approach** is designed to help clients achieve optimal credit health. Credit and debt education are important in today's world, as the impact different facets of your life. Credit and debt education not only help you obtain cars, homes, loans etc....; they also determine the amount of interest paid and gained. Seven Steps To Credit Literacy, outlined below, consist of:

Seven Steps to Managing Household Finances & Budgeting

Seven Steps to Managing Credit and Debt

Seven Steps to a Personal Savings Strategy



Managing Household Finances / Budgeting

Step 1: Set Realistic Goals

Step 2: Identify Income and Expenses

Step 3: Separate Needs and Wants

Step 4: Design Your Budget

Step 5: Make Your Plan Actionable

Step 6: Seasonal Expenses

Step 7: Look Ahead

Step 1: Set Realistic Goals

Goals for your money will help you make smart spending choices. Ask yourself: What do I want my finances to look like in one year? Decide what's important to you and start there. [More about this](#)

Step 2: Identify Income and Expenses

You probably know how much you earn each month – but do you also know where it all goes? Find out by tracking what you're spending. Spend as you normally would, but for a few weeks, jot down every cent you spend. It's easy and you might be amazed by what you find out. [More info on this](#)

Step 3: Separate Needs and Wants

Ask yourself: Do I want this, or do I need it? Will spending this money get me closer to my financial goals or further away? Can I live without it? Set clear priorities for yourself and the decisions become easier to make. [Learn more](#)

Step 4: Design Your Budget

Make sure that you are not spending more than you make. Balance your budget to accommodate everything you need to pay for. One easy way to do this is with our free, easy-to-use budget calculator spreadsheet and worksheet that's built for Canadians. [Learn more about crafting a budget](#)

Step 5: Make Your Plan Actionable

Match your spending to when you receive your income. Decide ahead of time what you'll use each pay cheque for. Ask yourself: Have I allocated money for my necessities (housing, food, utilities, transportation, etc.)? Have I put money aside for my debt payments, unexpected expenses, savings, and the fun stuff? This will protect you from going into debt further because you won't rely on credit to pay for your living expenses. [Learn more](#)

Step 6: Seasonal Expenses

You know that things will "just come up" – school expenses, new shoes, or an annual membership. Set money aside to pay for these expenses so you can afford them without going into debt. [More on this](#)

Step 7: Look Ahead

Getting on track with a budget can take a month or two. You've lived all this time without a spending plan, so give yourself time to adjust. Don't be afraid to ask for help if things aren't falling into place – help is just a phone call away.



Managing Credit and Debt

1. Take Account of Accounts

First things first: Make a list of all your outstanding debts. Include the interest rate on each so you'll be able to determine which ones are causing you the most financial pain.

2. Check Credit Report

This will help you make sure you haven't forgotten about an outstanding debt. Plus, it's always a good idea to make sure there aren't accounts on there you don't recognize. If you want to find out your credit score, check with your bank or credit card company to see if they can provide you with your score at no cost.

3. Look for Opportunities to Consolidate

If you have multiple high-interest loans, can you consolidate them into one loan with a lower interest rate? Do you have access to a low-interest personal loan that you could take out to pay off high-interest credit card balances? Before consolidating or refinancing any student loans, you should carefully review your eligibility for federal loan forgiveness programs which may be impacted by loan consolidation or refinancing.

4. Be Honest About Spending

If your debt feels overwhelming, it's worth taking an honest look at what you're spending each month. Are there expenses you can cut back on or eliminate? Part of reducing your debt is limiting the additional debt you take on.

5. Determine How Much You Must Pay

Once you've consolidated, determine how much you must pay each month by noting the minimum payments and put the total into your budget spreadsheet. If the amount is more than you can manage in your budget, you may need to contact lenders to see about arranging different terms.

6. Figure Out How Much Extra You Can Budget

Once you have the baseline of how much you must pay each month in your budget, determine how much extra from your budget you can devote to debt reduction. Hopefully, those expenses you reduced give you a little more discretionary money to put toward this goal.

7. Determine Debt-Reduction Strategy

How you attack your debt is up to you. The two most popular strategies are to pay off balances with the highest interest rates first or to pay off the lowest balances first. The former will save you more money over the long run, but the latter can help you keep momentum and see progress. Either way, you're taking steps in the right direction, so stick with your plan!

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Personal Savings Strategy

1. Automate Your Savings

2. Set Up an Emergency Fund

3. Tackle High-Interest Debt First

4. Save For Short-Term Goals

1. Automate Your Savings

To better organize your savings goals, start by getting a clear picture of your financial situation. Automating your savings is also a smart way to increase your savings. Putting your savings on autopilot is an easy way to separate savings from spending money. It's tempting to spend money after it hits your checking account. Automating your savings helps you avoid that temptation. Two ways to automate your savings are to split up your direct deposit and funnel part of it into a savings account and to set up a recurring transfer from your checking account into a savings account. Typically, you can take either a percentage of your paycheck or a fixed amount and use direct deposit into a savings account. You can also set an amount to be moved from your checking account into your savings account and then set the frequency of the transfer.

2. Set Up an Emergency Fund

Common advice for emergency funds is to save at least three to six months' worth of living expenses before you start saving for other goals. The emergency fund is separate from your other savings. It is a ready source of cash for unexpected expenses and a hedge against tapping a 401(k) or other long-term savings accounts. A sufficiently padded emergency fund also keeps you from having to use credit cards or borrow money to pay bills if you lose your job, need a costly car repair, or encounter some other major, unplanned expense. The amount to set aside "depends on how long you expect to be looking for work," says Judith Ward, vice president and senior financial planner with T. Rowe Price in Owings Mills, Maryland. "Households with just one worker or folks who earn commission may want a little more just because of that uncertainty."

3. Tackle High-Interest Debt First

It's crucial to tackle high-interest debt as quickly as possible because the interest added each month to the balance is money you instead could be saving. A popular savings strategy for paying off debt is to zero out the highest-interest debt first. Once you've cleared that balance, move on to the debt with the next highest APR. This strategy, called the avalanche method reduces how much interest you pay over the long run.

4. Save For Short-Term Goals

Once you have established an emergency fund, separate your next priorities into three savings buckets, which include short-, medium- and long-term goals.



5. Save For Medium-Range Goals

6. Save For Long-Term Goals

7. Use multiple savings accounts

Personal Savings Strategy cont...

5. Save For Medium-Range Goals

If your dream is to save for a down payment on a home, your child's college education or your child's wedding, you'll need to go beyond belt-tightening and set up midterm savings buckets.

6. Save For Long-Term Goals

Saving for the longer-term often requires looking beyond standard banking products, such as savings deposit accounts and CDs, to earn higher rates of return on your savings.

7. Use multiple savings accounts

Having more than one savings account is another way to earmark your money for different financial goals. Having multiple savings accounts can help ensure that money meant for one savings goal isn't being used for another.

If all your savings is in one account, for example, money meant for your emergency fund might accidentally be used for a vacation.

Having multiple savings accounts also gives you a clearer picture of how you're progressing toward your different savings goals. If you have \$20,000 saved and it's all in one account, it may be harder to keep track that you have \$5,000 saved for an emergency fund and \$15,000 for a home purchase.

And because many banks offer savings accounts that feature the same interest rate, no matter how low your balance, you don't need to put all your savings in the same account to get the highest yield.

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Example of short-term goals

- Car down payment

Let's say you want to buy a used car a year from now and you plan to spend \$12,000. You'll need to save \$1,000 a month, so you must figure out how you're going to fund this short-term savings bucket.

- Vacation

A vacation could easily cost a few thousand dollars, depending on where you are going and how many people are coming along. Adding short-term savings goals can help you afford the vacation you want by saving just a little bit at a time.

Best savings accounts for short-term goals

Both a high-yield savings account and money market account are smart choices for building your short-term savings.

- High-yield savings account

A high-yield savings account returns a better yield than many standard savings accounts and can help boost your savings. The interest earned could be put toward registration fees and taxes on your new car or you could reinvest it and start another short-term bucket.

- Money market account

A money market account is another useful tool for saving for short-term goals. Like savings accounts, money market accounts are liquid, which means you have ready access to your cash. Unlike savings accounts, many money-market accounts include checks and/or a debit card, making withdrawals easier.

Certificates of deposit aren't as liquid as savings and money market accounts. Money deposited into a CD is held by the bank or credit union for a specific period — typical terms are one month to 10 years — and taking the money out prematurely could result in an early withdrawal penalty.



Examples of medium-range savings goals

- Weddings

Weddings are another large medium-term savings goal. The average cost of a wedding is \$28,000, according to The Knot's 2021 Real Weddings Study. Of course, a more frugal wedding can be a joyful event, too, but it's still smart to plan for a big expense.

- Down payment on a house

A CD may be of great use here, but you could also tap your individual retirement account for up to \$10,000 for a home purchase without incurring a penalty.

- College

To save for your child's education, consider using a 529 savings plan. These tax-advantaged savings plans work much like a 401(k) or IRA. Your contributions are invested in mutual funds and other investments.

With midterm savings buckets, avoid exposure to too much risk. The goal is to preserve or increase capital.

Best savings accounts for medium-range goals

Good vehicles for saving cash for medium-range goals include:

- Money market account

Whether it is a brick-and-mortar or an online bank, a money market account is a suitable option for saving for the medium. Online banks tend to have a higher yield due to lower overhead but be sure to check which money market rates are best for your circumstances.

- Savings account

You can earn higher APY with a savings account than a traditional checking account, allowing you to squirrel away funds without the temptation to access them in the short-term. High-yield savings accounts typically pay higher rates than traditional savings accounts, which can help you save more.

- Certificate of deposit (CD)

Laddering CDs is a common option for savings strategies, helping you fund that down payment for your new home. If you choose a CD, additional deposits are usually not allowed during the CD term after the initial deposit. Your money will be tied up for a specified period, and if you withdraw the money early, you'll incur a penalty that will eat into your interest earnings. No-penalty CDs are an exception.

If you're going to fund this savings bucket with a CD, time the maturity date as close to the wedding date as possible to avoid an early withdrawal penalty.



Examples of long-term savings goals:

- Retirement

Retirement is perhaps the one savings goal where the time horizon is long enough that you can usually ride out market volatility that's common when investing in stocks and bonds.

Recommended account for long-term goals

- 401(k)

An easy way to fund a retirement account is to participate in your employer's retirement plan, which is typically a 401(k), 403(b) or 457 plan, depending on whether you work for a private employer, a nonprofit or the government, respectively.

Generally, your taxable income will be reduced by the amount you save.

- IRA

If your employer doesn't offer a plan, decide if opening a traditional or Roth IRA is obtainable. Most experts say the only way investors can achieve a comfortable retirement is to invest a percentage of their long-term savings in equities.

Given current low savings rates, the stock market remains for many households the only option to earn returns that can outpace inflation. And though stock prices may fall — and sometimes drastically — the average return of the S&P 500, a broad measure of stock performance, is more than 9 percent over the last 20 years.



Helpful websites

Thebalance.com

Investopedia.com

Citations

Mymoneycoach

Bankrate

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