Financial Literacy with Mr. 401(k)
['FinLit with Mr. 401(k)']
Winter Term 2023-2024
December 11, 2023

Making and Spending Money

Class 7: Budgets

Monday Money Matter$

Nonfarm payrolls rose by 199,000 in November, slightly better than the 190,000 Dow Jones estimate and ahead of the October gain of 150,000. The unemployment rate declined to 3.7%, compared with the forecast for 3.9%. Average hourly earnings, a key inflation indicator, increased by 0.4% for the month and 4% from a year ago, close to expectations. Health care was the biggest growth industry, adding 77,000 jobs.

Reference Date: December 8, 2023

Source: https://www.cnbc.com/2023/12/08/jobs-report-november-2023-us-payrolls-rose-199000-in-november-unemployment-rate-falls-to-3point7percent.html

Class Discussion

What do you think is a budget?

Budgets are Forecasts:

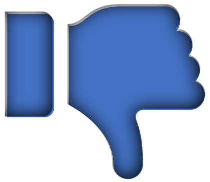
Forecasts of Income and Forecasts of Expenses

Budget Surplus

= forecasted income > forecasted expenses

Balanced Budget

= forecasted income = forecasted expenses

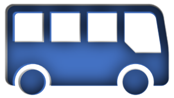


Budget Shortfall

= forecasted income < forecasted expenses

‘Needs’ vs ‘Wants’

Important: Personal Circumstances Matter



Must Haves

Necessary to satisfy day-to-day needs

(ex. Transportation to/from activities, school, work, etc.)

Should Haves

Important, but generally not necessary to satisfy day-to-day needs

(ex. Personal Vehicle)

Could Haves

Nice to have, but not necessary to satisfy day-to-day needs

(ex. Premium Electric Personal Vehicle)

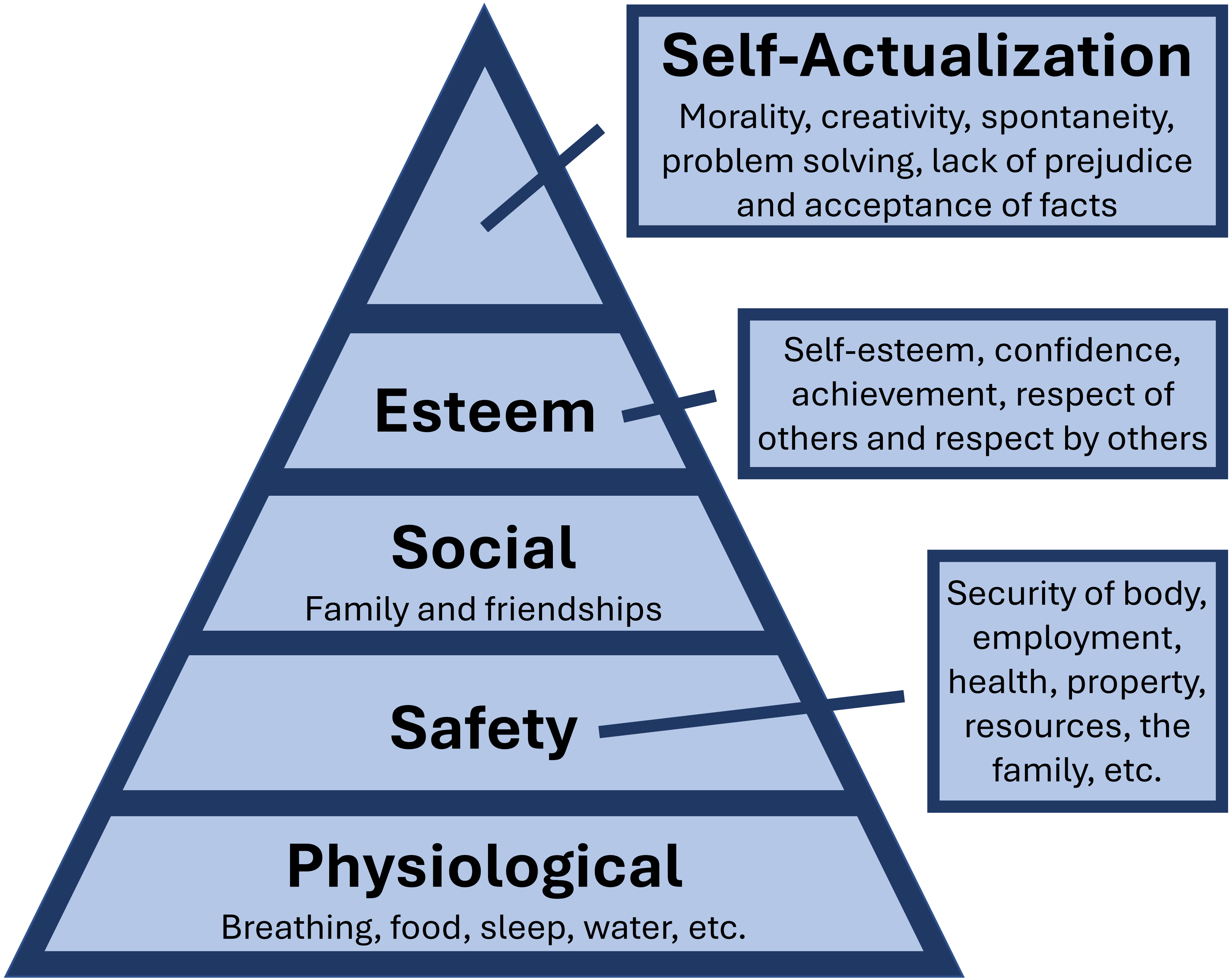
Wants

Entirely discretionary, but may enhance lifestyle

(ex. Sports Car)

Maslow’s Hierarchy of Needs

Maslow's Hierarchy of Needs, introduced by psychologist Abraham Maslow in 1943, is a theory comprising a five-tier model of human needs, often depicted as levels in a pyramid. Needs lower in the hierarchy must be satisfied before individuals can attend to higher needs. This theory is applicable in budgeting, where securing ‘needs’ takes precedence over ‘wants.’



Practical Application

Suppose you have $500 in total monthly income. Deduct essentials 1st and prioritize them below. 2nd, allocate some amounts for personal & growth. 3rd, Distribute any remaining money for your wants. Spending should not exceed income.

Essentials

- Lunch Money/Snacks: $________________________
- School Supplies: $________________________
- Transportation (ex. bus fare): $________________

Personal & Growth

- Cell Phone/Data Plan: $________________________
- Hobbies (ex. music, sports): $________________
- Savings for College/Big Purchase: $______________

Wants (Leftover $)

- Games and Apps: $________________________
- Movies or Event Tickets: $________________________
- Eating Out/Fun With Friends: $_______________

Goal-Oriented Budgeting System

Step 1
Identify our target savings goal (ex. a new bicycle)

Step 2
Determine how much we need and when we need it.

Step 3
Set aside a certain amount routinely (ex. weekly or monthly) to attain the savings goal.

Important
Tracking progress over time helps to stay motivated and adjust, if necessary.

Envelope Budgeting System

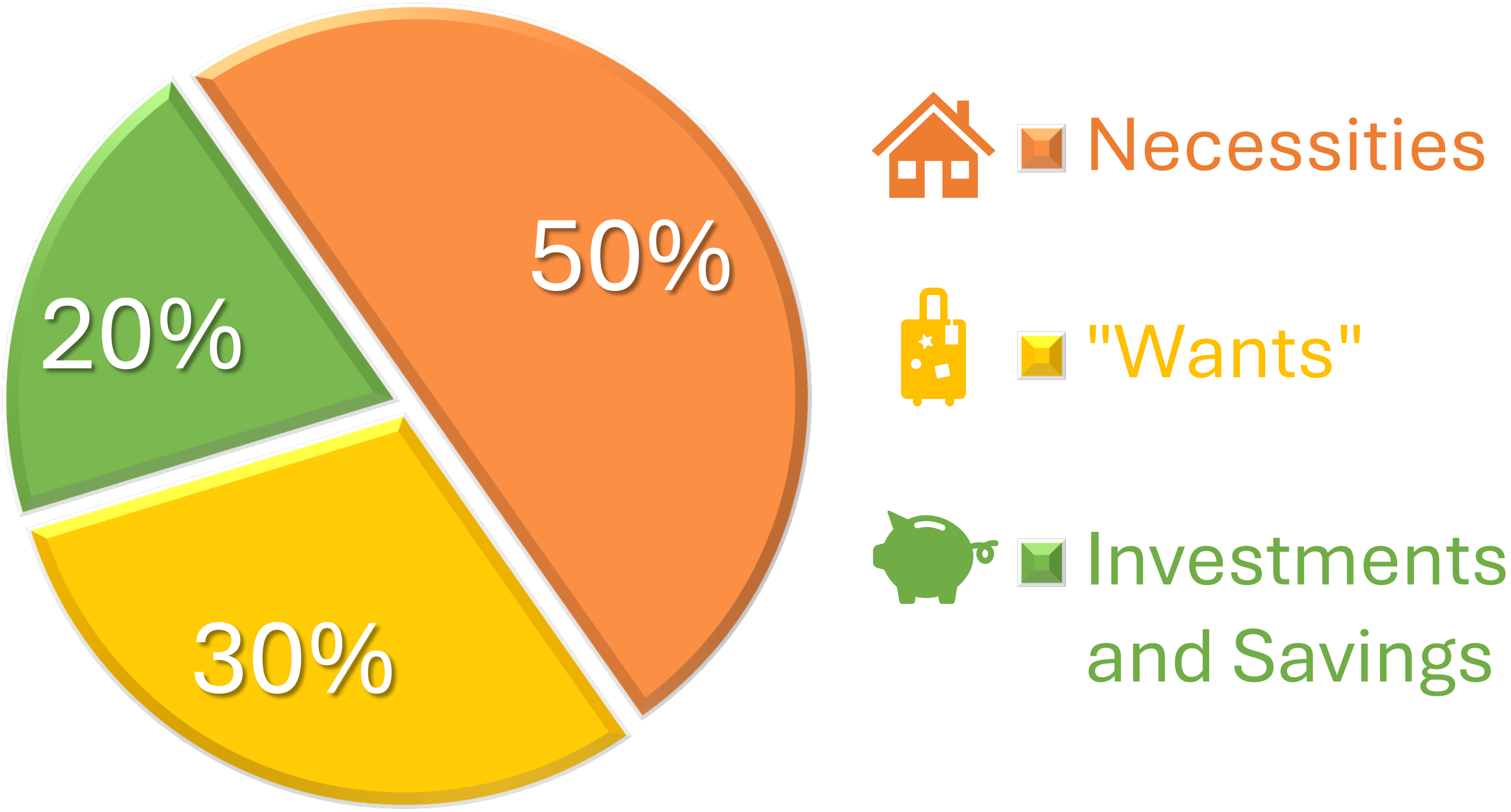
Step 1	Step 2	Step 3	Important
Label envelopes with budget categories.	When you receive money, divide it among the envelopes based on your budget plan.	Spend only what is in each envelope for that category.	When it's gone, it's gone – this helps prevent overspending and keeps you within budget.

Events	Games	Investing	Savings	Snacks	Sports
10%	20%	15%	15%	25%	15%

50/30/20 Budgeting System

Approach

Determine total monthly income. Then, allocate the income as follows: **50%** to necessities, **30%** to wants, and **20%** to investments and savings.



Sample Budget Guide Handout

Budget Item		Approach	Formula
A	= Income	Forecast all income sources. Include forecasted earned income, passive income, and portfolio income.	
B	= Long Term Financial Security	Invest 15% of forecasted income for long term financial security (ex. retirement).	= A x 15%
C	= Income Taxes	Estimate income taxes based on total forecasted income and applicable tax rates.	= A x [Tax Rates]
D	= Emergency Savings	Save 5% of after-tax forecasted income in an emergency savings account. Accumulate 3 to 6 months of expenses.	= (A – C) x 5%
E	= Essential Expenses	Spend no more than 50% of after-tax income on essential expenses, which should include all must haves, and some should haves.	= (A – C) x 50%
F	= Other Expenses, Savings, or Investments	The balance of income can be spent on discretionary expenses – any remaining should haves, could haves, and some wants. The balance could also be saved or invested.	= A – B – C – D – E

Money Mavericks

Objective: Help a student to develop a budget. The student provides part-time childcare services. The student forecasts total income for the year of $6,000 = A. The student anticipates a 10% income tax rate. Use the Sample Budget Guide to calculate Budget Item B, C, D, E, and F.

Money Mavericks Exercise Answers

Given: Income is $6,000 and Tax Rates are 10%

Budget Item		Formula	Show Your Work	Answer
A	= Income		$6,000	**$6,000**
B	= Long Term Financial Security	= A x 15%	$6,000 x 15%	**$900**
C	= Income Taxes	= A x [Tax Rates]	$6,000 x 10%	**$600**
D	= Emergency Savings	= (A – C) x 5%	($6,000 - $600) x 5%	**$270**
E	= Essential Expenses	= (A – C) x 50%	($6,000 - $600) x 50%	**$2,700**
F	= Other Expenses, Savings, or Investments	= A – B – C – D – E	$6,000 - $900 - $600 - $270 - $2700	**$1,530**

Class Discussion

How much do the latest video game consoles cost?

Beware of ‘Sneaky’ Costs

Don’t forget about ancillary costs when budgeting. They add up quickly!

Game Console
$500 + Sales Tax

Controllers
$75 Each + Sales Tax

Video Games
$20 to $70 Each + Sales Tax

Monitor or TV
$200 to $2,000 + Sales Tax

Headphones
$50 Each + Sales Tax

Batteries
$10 / Pack + Sales Tax

Electricity
$3 / Month + Taxes

New Console
5-Year Obsolescence
$500 + Sales Tax

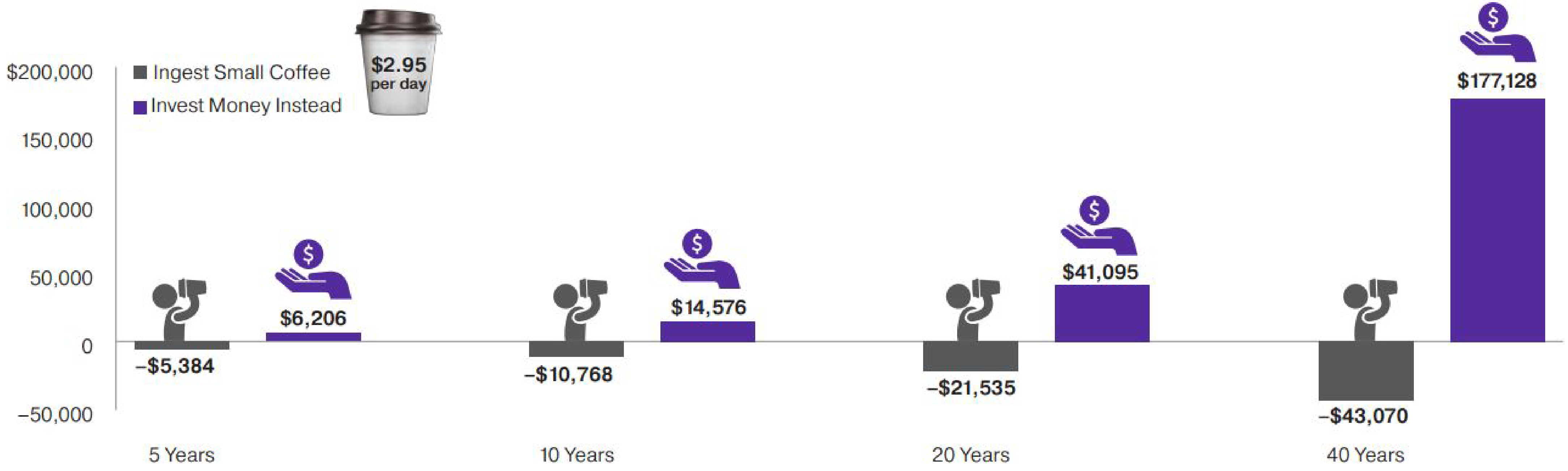
Once you have spent money on something, you cannot spend it again on something else.

Visualizing an "Opportunity Cost"

Every Purchase Has an Opportunity Cost

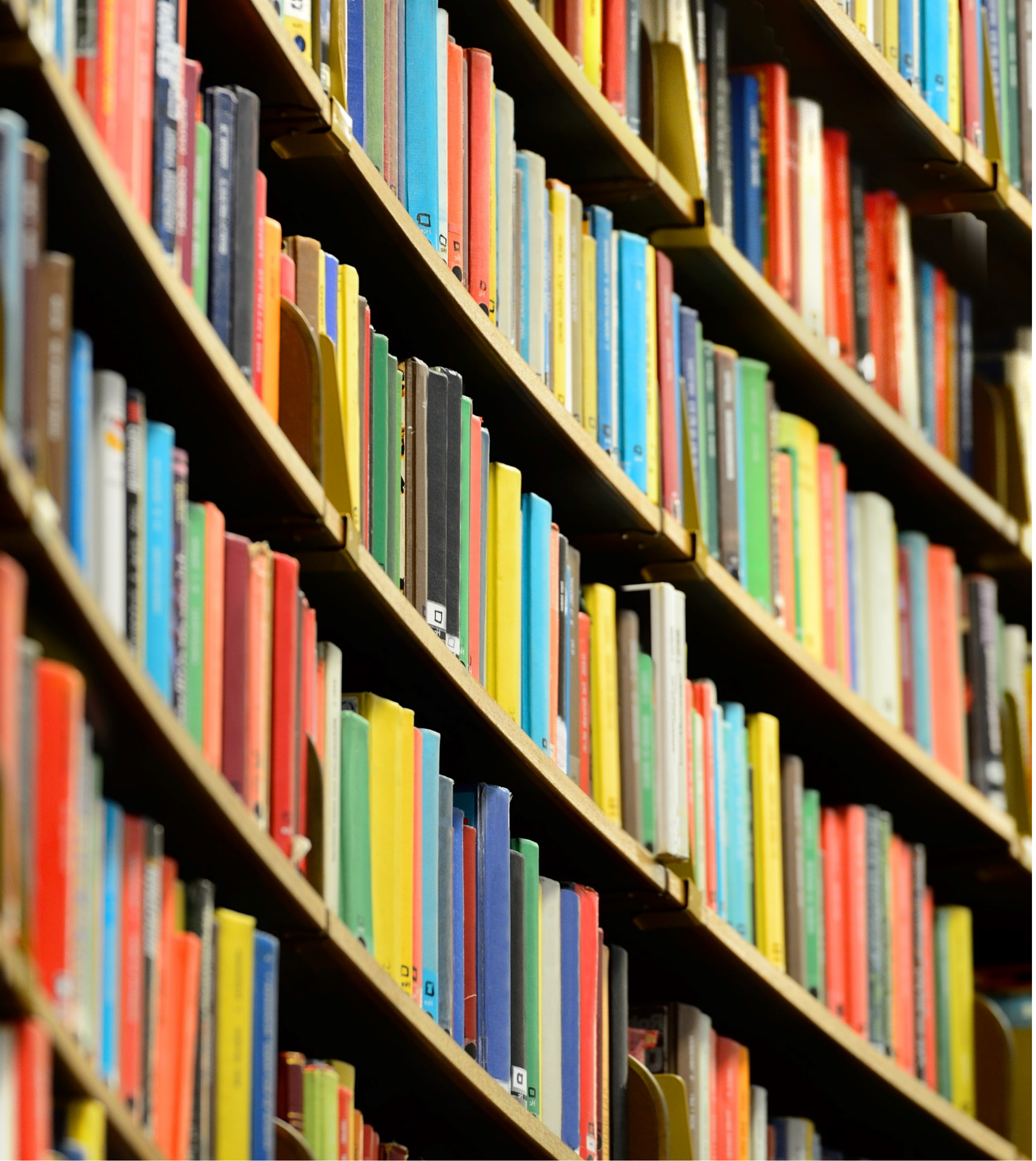
"In economics, one of the most important concepts is opportunity cost—the idea that once you spend your money on something, you can't spend it again on something else." —Malcolm Turnbull

The Opportunity Cost of Drinking a Small Coffee Every Day (Ingest) vs. Investing that Money*



Three Key Takeaways

1. Budgeting involves forecasting income and expenses, aiming to create a surplus.
2. Differentiating between 'needs' (essentials for day-to-day living) and 'wants' (discretionary spending) is crucial for effective budget management.
3. Utilizing budgeting systems can help allocate your resources wisely and saving for future financial goals.



Where to Learn More

- Budgeting for Teens: 14 Tips for Growing Your Money Young, by Mint
- Budgeting for Teens: What You Need to Know by Rebecca Lake
- The Budget Book for Young Adults: Guide on Budgeting Basics for Beginners, Including the 50/30/20 Budget Approach by Sasha Winters