

How Much Credit Can You Afford?

How much is your monthly take-home pay?

$$\begin{array}{rcl}
 \$ \underline{\hspace{2cm}} & \times .20 \text{ (20\%)} = & \$ \underline{\hspace{2cm}} \\
 \text{monthly take-home pay} & & \text{Affordable credit amount}
 \end{array}$$

A general rule of thumb is that your monthly installment debt payments should not exceed 20% of your monthly take-home pay. Installment debt payments would include auto loans, credit cards, student loans, personal loans, and loans for vacations, home improvements, or emergencies. For example, if your monthly take-home pay is \$1,000 you can afford no more than \$200 per month in credit payments.

How much is left over for credit payments after you have met your monthly expenses?

$$\begin{array}{rcl}
 \$ \underline{\hspace{2cm}} & - & \$ \underline{\hspace{2cm}} & - & \$ \underline{\hspace{2cm}} \\
 \text{(Monthly take-home pay)} & & \text{(fixed monthly expenses)} & & \text{(flexible monthly expenses)} \\
 \\
 - \$ \underline{\hspace{2cm}} & = & \$ \underline{\hspace{2cm}} \\
 \text{(Periodic monthly expenses)} & & \text{(Remaining Balance)}
 \end{array}$$

- a. If a balance is left each month, then you may be able to handle a credit payment.
- b. If income meets expenses but there is no balance left, then you should postpone taking on a monthly credit payment until there is more money available.
- c. If your expenses are greater than your monthly income, then you cannot afford a monthly credit payment. You will need to adjust your spending habits to meet your income.

How much money do you have available to meet emergencies?

$$\begin{array}{l}
 \$ \underline{\hspace{2cm}} \text{ monthly living expenses} \times 1 = \\
 \$ \underline{\hspace{2cm}}.
 \end{array}$$

$$\begin{array}{l}
 \$ \underline{\hspace{2cm}} \text{ monthly living expenses} \times 2 = \\
 \$ \underline{\hspace{2cm}}.
 \end{array}$$

$$\begin{array}{l}
 \$ \underline{\hspace{2cm}} \text{ monthly living expenses} \times 3 = \\
 \$ \underline{\hspace{2cm}}.
 \end{array}$$

Emergencies happen to all of us. If you do not have money put aside to cover emergency expenses when they happen, you will be unable to make your monthly credit payments as well as cover your living expenses. You should have enough money in a "liquid" form of savings to cover 1 to 3 months of living expenses.