FINANCIAL UNDERSTANDING

I. Introduction to the Series

A. Purpose

• Primary: To give you the knowledge you need to be good stewards of your financial resources.
• Secondary: If you learn to save more money and make more money, perhaps you'll share some of those savings and earnings with our parish.

B. Objectives

• Put money and property in perspective and understand how they relate to your spiritual life.
• Identify and prioritize needs and wants.
• Understand how to meet current financial needs through work, business, investments, and government benefits.
• Discover how to manage debt effectively.
• Learn how to manage a budget and spend wisely.
• Find out how to plan for adversity as well as anticipated events.
• Determine how to invest your savings.

II. Spiritual Dimensions of Financial Management

A. Scripture and Church teaching

• Mt. 6:19-21, 24. (Where your treasure is, there will your heart be also. . . . No one can serve two masters.)
• Mk. 12:41-44. (poor widow contributed all she had)
• 1 Tim. 6:10. (love of money is the root of all evils)
• 1 Tim. 6:17. (rich are to be generous)
• 1 Pt. 4:10. (use God's gifts to serve one another as good stewards)
• Sacrifice is important to spiritual development.
• We have a duty to provide for our material needs, those of our family, and those of others (*See* CCC ¶¶ 2252, 2404).
• The sacred bond of marriage is threatened by financial discord.
• It's hard to focus on spirituality and prayer when you're consumed by concerns about money.

B. Simplicity

1. Needs versus wants

• What do you really need to survive; what do you want to add value to your life?

2. Living simply

    • By evaluating your schedule of physical, emotional, and spiritual desires, achieve simplicity.

3. Slowing down

    • Find time to spend with family, friends, and interests through prioritizing.

C. Identifying and categorizing specific needs

1. Establishing priorities

    • Food, clothing, shelter (including utilities), health care, transportation, communication, education, child care, taxes, maintenance of home and personal property, support for church and charities, recreation, vacation, entertainment, toys, personal grooming, laundry and dry cleaning, pets, gifts.

2. Planning for future needs

    • Planning for adversity and future needs must be part of current priorities.
    • Pay insurance premiums, set aside some money for emergencies, and contribute toward a fund for the years when you are no longer able to work.

• Additional resource: Phil Lenahan, *7 Steps to Becoming Financially Free: A Catholic Guide to Managing Your Money* (2006) (published by *Our Sunday Visitor*, http://catalog.osv.com).

III. Meeting Current Financial Needs

A. Sources of income

1. Work

    • Stay current with job requirements and conditions of employment, be an effective team member, have a positive attitude, perform at peak levels, act with integrity, and prepare for advancement.
    • Balance faith, family and work. (Ex. 18:13-27; 20:9-11; *Catechism* ¶¶ 2184-2187).
    • Become more effective employees or employers by applying Catholic teaching in your working life. (*Christifideles Laici* ¶ 59; *Catechism* ¶ 2427; Ps. 127:1-2; Phil. 2:3-8; 2 Thes. 3:6-16).
    • Working is essential to obtaining the essentials of life. (Prv. 12:11; 16:26; 28:19).
    • Our work can serve as a reflection of who we are as children of God. It can be a constant witness to faith by the way we pursue the "daily work of our hands," the way we "spend" time. Our work can be a prayerful expression of faithfulness to God.

• Take continuing education courses, seminars and webinars. Stay current with technology. Be aware of opportunities in your industry and avenues for networking. Determine your marketability, and update your resume.

2. Business

• Don’t be afraid to take some risks.
• Be willing to think about possibilities.
• You may be able to do better by venturing out on your own.
• You know what your talents and interests are—can you apply them to meet people’s needs more effectively than others are meeting them?

3. Investments

• After retirement, income from investments, including retirement plans, is likely to be the most important factor in your financial security.
• While you are working, using income from investments to meet current financial needs jeopardizes long-term financial security. All income, including interest, dividends, and capital gains, must be reinvested to compensate as much as possible for the effect of inflation and taxes.

4. Government-administered benefits

• After retirement, Social Security should provide a significant contribution to your financial security and that of your spouse.
• Before retirement, Social Security disability or death benefits may provide a significant contribution to your family’s financial security if you die or become totally disabled.
• If you are injured on the job, workers’ compensation may provide a source of income, but it won’t be enough by itself.
• If you are laid off, unemployment compensation may provide a small amount of income on a temporary basis.
• Government-administered benefits by themselves will not provide financial security for you or your family.

5. Loans

• “Never go into debt for anything that you don’t expect to appreciate in value.” Phil Lenahan, *7 Steps to Becoming Financially Free: A Catholic Guide to Managing Your Money*, Chapter 8 (2006).
• Paying interest on credit cards and other consumer debt is the biggest reason most people fail to achieve financial security for themselves and their families.

B. Reducing debt

1. Consumer debt is probably the most important reason people fail to achieve financial security.

• Buying anything on credit is expensive; to see how much more it will cost, visit: http://mortgage-x.com/calculators/amortization.htm.

• The above assumes that you make monthly payments on the loan that are designed to pay it in full within a set period of time.
• Credit cards don't work that way—the companies subtly encourage you to make only the minimum payment; as a practical matter, assuming you continue to charge purchases to the card, you won't live long enough to pay off the balance. (*see* http://www.cardratings.com/calculatorframe.html)

2. Eliminate future consumer debt by:

   • not buying what you don't really need (*see* ¶ II.B. above)
   • using credit cards only for routine, recurring expenses and paying the balance in full each month by the payment due date
   • keeping track of credit card purchases just as you do purchases by check
   • planning for future expenses and maintaining a fund to cover them

3. Eliminate existing consumer debt by:
   • paying off credit card balances as quickly as possible, starting with the account with the highest interest rate if you have more than one
   • reducing other expenses and applying the savings to paying off balances
   • finding additional sources of income to help pay off balances

4. Be very wary of commercial debt consolidation and credit counseling services. If you really think you need that kind of help, be sure the firm you use is affiliated with the National Foundation for Credit Counseling. You can find affiliates at http://www.nfcc.org.

5. Avoid bankruptcy proceedings if possible.

   • If you are overwhelmed with debt and cannot manage it on your own or with help from others, seek a lawyer with experience in this area of practice.
   • If you do seek bankruptcy protection, remember your moral obligation should you someday be in a position to repay your debts (*Catechism* ¶¶ 2409 - 2411).

C. Budgeting

1. An inadequate personal budget is likely to result in failure to achieve financial security.

2. Use a budget worksheet like the one in the attached Excel file.

3. Ordinarily the only income you should include in your budget is your "take-home" after-tax pay for your work; **do not** include income from savings and investments in your budget unless you are already retired and have a plan to draw on that income for your monthly expenses.

4. If monthly expenses exceed monthly income, you must make some changes.

   • Find ways to reduce expenses.
   • Consider how you might be able to increase income.

5. Fully integrate the accounting of your purchases made by check, debit card, and credit card.

6. Use cash for very small purchases only and keep track of the budget categories for which you do use it.

7. Ensure that the "financial security" aspects of your budget are adequately funded.

8. Consider your obligation to support your church and those less fortunate, and don't shortchange that part of your budget.

9. Create your budget carefully and follow it (exercise budget discipline).

10. Remember to include expenses that occur less frequently than monthly in your monthly budget—you must create a "reserve" for those expenses.

    • Divide the amount of the payment by the frequency of the payment, and include that amount in the appropriate category in your monthly budget.
    • For example, if your personal property taxes are $120 every 6 months, the formula is $120 ÷ 6 = $20.
    • That $20 and all other expenses that occur less frequently than monthly should be transferred to a separate bank account (perhaps a bank money market account with limited check-writing privileges), which is used to pay those expenses when they become due.

D. Intelligent spending

1. Spend only within your budget and buy only what you need.

2. Use credit cards to your advantage—pay the balance in full each month and receive cash-back rewards. (*see* http://www.cardratings.com/cashbackcreditcards.html)

3. Use the library and the Internet to do research on major purchases—get evaluations, price comparisons, and check for the availability of used items, e.g., Craig's List, eBay; check autos through NMVTIS, CARFAX.

4. Use cash sparingly, and get what little you need from your bank account (assuming your bank does not charge an ATM fee for this service).

5. Consider the life cycle cost of what you are buying—something may be somewhat more expensive at the time of purchase but last longer and require less maintenance than an alternative item.

6. Buy things you know you are going to need when they are out of season or otherwise reduced in price.

7. Compare generic items and store brands with brand names you know.

8. When possible, negotiate the price of the item you're buying.

9. *See* Phil Lenahan, *7 Steps to Becoming Financially Free: A Catholic Guide to Managing Your Money*, Chapter 10).

IV. Planning for Future Financial Needs

A. Planning for adversity; insurance

1. Legal instruments pertaining to death and incapacity

   • A will is important not only to direct the distribution of your property but also to state who will be responsible for doing so and to appoint guardians for minor children.
   • A trust is useful for managing property when you can't or don't want to do so yourself, for managing property for children who are under age or not ready to manage it, and in some cases to provide tax planning for married couples.
   • An advance medical directive states your wishes about medical treatment (such as "do not resuscitate"), appoints an agent to make decisions for you if you are unable to so, and can provide for organ donation if you wish.
   • The purpose of a power of attorney is to name someone to make decisions about your property when you are absent or unable to do so; it is important to take certain precautions and to name someone in whom you have complete trust.
   • You should obtain the services of a lawyer who is knowledgeable about these kinds of legal documents to prepare them for you.

2. Life insurance

   • How much you need depends on assumptions you make about how long your survivors will need financial help and how much they will need; consider an online calculator to get a ballpark figure: http://www.calcxml.com/calclist.html
   • Buy guaranteed renewable term life insurance only, and buy from a company that is ranked the 90th percentile or higher in the Comdex ratings.
   • Life insurance is no longer needed when retirement plan assets exceed the value of the policy.

3. Disability insurance

   • Review your workplace group disability policy to see what is covered, for how long, and what percentage of your salary will be replaced.
   • Consider purchasing supplemental disability coverage.

4. Medical insurance

   • If you are generally healthy and live a healthy lifestyle, consider a high-deductible policy.
   • Compare plans online; these are two potentially useful sites, but there are many others:
      • http://www.vimo.com/health-insurance-plan/ (click on VA)
      • http://www.ehealthinsurance.com/

5. Insurance to cover other risks to income and assets

    • Consider purchasing an umbrella policy to extend your liability limits.

6. Emergency fund for six months of living expenses

    • Establish a fund in an FDIC-insured institution; shop for the best interest rate on liquid funds. (*see* http://www.bankrate.com)

B. Planning for anticipated events

1. Preliminary points

    • Don't commingle funds for different goals; for example, keep retirement funds separate from college funds.
    • Adjust the mix of investments in each fund as the time horizon for that fund shortens. (*see* ¶ V.A. below)
    • Consider the effect of inflation and taxes on the future purchasing power of your savings, investments, and benefits.
    • Interest, dividends, capital gains and capital gain distributions, and any other earnings must be reinvested and not used for any other purpose.

2. Retirement

    • Determine what your monthly expenses will be during retirement; they will probably be about the same as they are now, except for your contribution to your future financial security and possibly your mortgage interest if your home is paid off.
    • Determine how much income you will have from Social Security and other government-administered benefits.
    • Determine how much additional income you will need to meet your expenses from the date you retire until your death (it's best to assume 30 years).
    • Invest enough money to create the fund necessary to produce that income beginning on the date you retire (it's best to assume that after you retire, the return on your investments will not exceed the decline in purchasing power caused by inflation and taxes).
    • If your employer has a matching contribution plan, contribute monthly to such a plan if you are allowed to select the investments; contribute to an IRA.
    • Consider using a Roth 401(k), Roth 403(b), or Roth IRA rather than a traditional retirement plan or IRA.

3. Higher education

    • Don't contribute to a college savings plan unless you are already contributing the amount you need for retirement to a retirement plan.
    • Consider using a 529 plan. (*see* http://www.savingforcollege.com)
    • Keep in mind the relatively short time horizons for the use of the funds and adjust investment options accordingly.

4. Replacement and repair of property

   • Establish a fund for replacement of vehicles, appliances, etc., and for maintenance and repairs of real estate and personal property.

5. Other needs

V. Investment Principles

A. Asset allocation

• Over long periods of time, the average return on investments in stocks and similar securities has more than offset the effect of inflation and taxes.
• As the time when funds will be needed draws nearer, the allocation must be changed to include investments that are less volatile than stocks and other equity-type investments; most Treasury securities are very stable when held to maturity.
• The allocation is a matter of judgment and risk tolerance—it is necessary to balance the risk of not keeping up with inflation against the risk of market decline.

B. Market timing

• It is very risky to try to buy stocks and other equity-type investments when prices are low and sell them when prices are high; very few market timers are successful over extended periods of time.
• Dollar cost averaging is effective—contribute the same dollar amount at the same time each month to improve the total return on volatile investments.
• Re-balance the allocation of your assets at least annually to make sure market forces have not adversely affected your formula.

C. Diversification

• Diversification of investments across asset classes, markets, market sectors, and individual securities is essential; don't invest much in your company's stock.

D. Investment products

• Index funds with low management fees and low turnover are generally the best option for the equities portion of most investors' portfolios.
• Consider your moral obligations when selecting investments. (*see* Phil Lenahan, *7 Steps to Becoming Financially Free: A Catholic Guide to Managing Your Money*, Chapter 12)

E. Recommended books

• Burton G. Malkiel, *A Random Walk Down Wall Street* (2007); David F. Swensen, *Unconventional Success* (2005).