



Extension News Column

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How do you know when you owe too much or are you spending too much? The financial industry has a few rules of thumb that all of us should measure our behavior against on a regular basis. Use these financial comparisons to see if you are financially healthy.

- The price of your home should be no more than 2.5 to three times your annual income. That means you must make between \$82,000 and \$100,000 a year to afford the median home price in the Fairbanks area at \$257,000. Some mortgage lenders have allowed a higher ratio due to the high cost of homes in many areas, but stick to the original and you'll find it easier to make your house payment.
- Your monthly debt payments including house, car, student loans, and credit card should be no more than 35 percent of your monthly gross income. Some mortgage brokers may stretch this ratio to 40%, but this leaves you very little room for error or unexpected expense.
- How much money should you save? Most experts say that you should save at least 10% of your income. The easiest way to do this is to pay yourself first. Your employer may be able to redirect 10% automatically, or if not, write a check to your savings account.
- Do you have an emergency fund? You should have 3 to 6 months of expenses in an account. Notice I said expenses, not income. This is one of the most difficult rules of thumb for most of us to follow. By following the 10% rule above, you may soon find this rule within your reach.
- Short-term debt should not be more than 20% of your income. Add up the minimum payments on your credit cards, your car and student loans, and other forms of debt. If this number is more than 20% of your income, you need to make efforts to reduce this debt. Many people just starting out on their careers with heavy student debt and low starting salaries may find themselves violating this rule. Don't despair, just work to pay off some of this short-term debt and don't add to your debt by shopping.
- How much insurance should you have? Most experts say 5 to 8 times your annual income. But the best idea is to take your cash flow statements and your net worth statements and consult an insurance agent.
- How much do you need for retirement? Figure on 20 times what you want to live on each year. If you want to have \$75,000 to live on annually, you'll have to save \$1.5 million. If your house is paid for, you may need less money, or if you intend to retire early, you'll need more.

Now, the purpose of this article is not to make you feel like a financial failure, because most of us have violated one or more of these rules of thumb. But the idea is to take a close look at your financial situation and make efforts to bring your finances back in line.