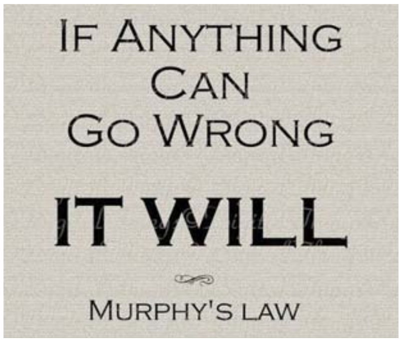
Lesson 13

But What About Murphy?



My best research tells me that Murphy's Law morphed out of a statement made by Captain Edward Murphy at Edwards Air Force Base, CA in 1949. Today's version is usually quoted as "If anything can go wrong, it will." Does that hold true with your personal monthly budget? Let me answer the question this way: I will be shocked if Murphy's Law takes a pass on your budget. There are just too many moving parts, and as we all know, life happens. Having said that, let's not forget the truth we learned earlier from **Proverbs 16:3, "Commit your works unto the Lord, and your plans will be established."** The Lord is now the One we depend on to help us implement our plan and to help us with the inevitable problems. At the same time, we know the enemy will try hard to steal our peace and joy.

Should we become discouraged and throw in the towel knowing that our best planning will more than likely experience a few wrecks along the way? Absolutely not, **because having the plan in place gives us a far greater chance of overcoming the setbacks than having no plan at all.**

Let's look at a couple of examples: First, you're cruising along; you've been working the budget for a few months and you're making progress. You're working toward Milestone 6 (paying off a car loan), when your spouse is unexpectedly laid off, reducing your Usable Income (UI) by 40%. What do you do? Answer: Immediately have a family meeting and explain the situation. Implement the GTW process and continue the GTW until the income is restored. I don't mean to oversimplify the situation, but you have a plan in place and tools to use at your immediate disposal. This fact is far superior to winging it and panicking when things go wrong?

Or let's say you're working toward Milestone 3 and have $800 in savings. The refrigerator that has been temperamental for months decides to quit, and the frozen food is rapidly thawing. Now what? Answer: Maybe a few options – a trip to a discount furniture or appliance store to find a refrigerator for $800 or less that will give you a few years service, or a quick search on the Web for someone trying to sell one in the process of a move. You then reengage the GTW process, if necessary, to quickly replenish your savings account. **What you don't do is grab the credit card** and buy a $2,000 refrigerator, because as you will see later, it will cost you far in excess of the purchase price.

Once again, you have a plan. You take the necessary steps to address the short term problem and you stay on track to meet your future Milestones. Is it discouraging to take a step backwards? Probably, but you know that **if you stay the course the long term benefits far outweigh the temporary setbacks.**

I hope you noticed that the two previous examples would have been minor bumps in the road if adequate savings had been available to meet the emergency. That's why in the Bible the Lord provides us the savings guidance that He does.

He knows that if we will follow His plan, the big crises become minor crises and the Holy Spirit is then free to flood us with His peace.

So, how can we accelerate the Milestone process and **get to the point where Murphy's Law is a moot point?** For most people, the answer lies in eliminating the nagging debt. When debt is no longer an issue, all of the dollars that were diverted to servicing debt can be diverted to servicing our savings or investing accounts.

In the next lesson, we will develop the process of accelerating debt reduction. But first, let's look at why consumer debt is a problem in the first place. I used the term "consumer debt" in the previous sentence because you may hear some people propose that some debt is "good debt"; that it can be used to leverage your position in investing and other business ventures and actually help you build wealth faster. Let's leave that discussion for another day, but for the purposes of this study **consumer debt is always bad debt**, for a few reasons.

First of all, interest on consumer debt (credit cards, department store accounts, furniture/appliance loans, car loans and any other loan on a depreciating asset) only benefits the creditor. There is zero benefit for the consumer. Most consumer debt carries with it high interest rates (10% or more and, often, much more). In addition, consumer debt can be insidious. The marketplace is very skilled at diverting the consumer's attention from the long term effect of consumer debt and persuading the purchaser that the monthly payment will be very low and manageable.

It is very important that you are aware of two of the most deceiving aspects of debt. I call the first one, the **Monthly Payment Illusion**; the second is the amount of interest you are paying the creditor each month just to service the debt.

Remember the $2,000 refrigerator used in the example a few paragraphs earlier?

The chart in **Figure 1** illustrates why you don't fall for the salesperson's pitch about the low monthly payments and buy it when you don't have the full purchase price. In Figure 1, I'm using the current interest rate of several popular department stores that sell appliances (25%+/-). If you use the credit card offered by the store and buy the refrigerator, you will have two primary choices when you receive the bill the following month – either pay the bill in full or send in a minimum monthly payment. Credit card companies are now required to include the total cost of the monthly payments, but most people don't pay attention to the information. The chart shows you the difference between what you would actually pay for the refrigerator if you paid for it when the bill was due ($2,000 plus tax) vs. the total cost ($5,680) and the time to payoff (10.5 years) if you chose the minimum payment option.

Figure 1

Monthly Payment Illusion					
Price	Minimum Payment	Interest Rate	Time to Payoff	Total Cost	Difference
$2,000	$45/mo	25%	10.5 yrs	$5,680	$3,680

My question to you is simply this: When you were shopping for the refrigerator and the $2,000 price tag had been replaced with a $5,680 price tag, would you have been motivated to buy it knowing that it would take you over 10 years to pay it off?

Unlikely, right? But we pay that kind of price for stuff when we are tricked by the illusion that a monthly payment is an acceptable method to pay. Obviously, the cheapest way to pay for the refrigerator is to pay the bill in full when it is due. Let's say you already find yourself in the above situation and don't have the money to pay the full amount. Watch what would happen if you doubled the monthly payment (paid $90 instead of $45 per month).

Notice in **Figure 2** that by paying $90 per month rather than $45, **the payoff time is reduced by 8 years!** And the refrigerator costs $714 more than if you had paid cash, rather than $3,680 more! **This is a perfect illustration of the time factor of money.** Remember this: when interest is compounding and working against you, you want to reduce the payoff time as much as possible (preferably to zero by paying in full); when interest is compounding and working for you (saving and investing), you want to extend time as much as possible. Compounding interest is a powerful tool as you will see in later lessons; **the key is that we want it to work for us rather than against us.**

Figure 2

Monthly Payment Illusion					
Price	Minimum Payment	Interest Rate	Time to Payoff	Total Cost	Difference
$2,000	$90/mo	25%	2.5 yrs	$2,714	$714

The second deceiving aspect of debt that is missed by most consumers is **just how much interest is being paid monthly** for credit cards and loan accounts. Another reason companies offer "low" monthly payments is that a huge amount of their profits comes from interest the consumer is paying.

In the previous $2,000 refrigerator example, initially only $3 of the $45 payment goes toward the price of the refrigerator. That means you are "donating" $42 in interest to the company for the privilege of receiving another statement the next month showing that you now owe $1,997! What if that scenario is multiplied a few times each month by other credit card bills, furniture loans, car loans, etc? The amount of interest many people are paying each month is staggering. Do you remember Melissa's situation from Lesson 9 of last week? Just the interest portion alone on her monthly credit card payments were more than $1000! You and I derive no benefit whatsoever by paying consumer debt interest – the only beneficiary is the creditor. This issue was the biggest motivator in my life to encourage me to get out of debt years ago. When I saw the amount of money I was paying each month in interest, it made me sick. I concluded that I had rather take that same amount of money and use it for more constructive purposes.

Maybe debt is not an issue for you, but if it is, I want you to determine how much total interest you are paying each month. Hopefully, it will be as much of a motivator for you as it was for me to get out of debt as quickly as possible. A **Monthly Interest Calculator** is available for you at the link provided on page A-6. The illustration below will explain the concept. You will need two pieces of information for each creditor: the current balance and the annual interest rate. This information is available on your monthly statement (either the printed statement or on-line).

The calculator allows you to enter the name of the creditor, the current balance and the annual interest rate. The amount of monthly interest in the far right column is computed for you. There is a Subtotal amount for all consumer debt (excluding mortgage(s)). In this illustration, the subtotal (almost $381 per month) is being paid in consumer debt interest. That amount doesn't include the mortgage and equity line interest because the mortgage generally represents an appreciating asset (obviously not guaranteed).

Monthly Interest Calculator			
Creditor (non-housing)	Balance	Annual Interest Rate	Monthly Interest
Credit Card 1	$ 6,000	18%	$ 90
Credit Card 2	$ 4,000	21%	$ 70
Department Store	$ 2,500	12%	$ 25
Auto	$ 8,000	8%	$ 53
Auto	$ 16,000	6%	$ 80
Student Loan	$ 15,000	5%	$ 63
Subtotal non-housing	$ 51,500		$ 381
Creditor (housing)	Balance	Annual Interest Rate	Monthly Interest
Mortgage	$ 175,000	4%	$ 583
Equity Line	$ 10,000	5%	$ 42
Subtotal housing	$ 185,000		$ 625
Total	$ 236,500		$ 1,006

If a concentrated effort was made to aggressively eliminate the consumer debt, you would essentially receive a $381 per month after tax pay raise! That money would then be available to help fund other areas of the budget or, preferably, be directed to savings to reach Milestone 6.

REFLECTION: Spend some time in prayer asking the Lord to sustain you through any Murphy Law interruptions. Think about the advantage you will have once sufficient savings are in place to reduce Murphy's impact. How will that encourage you to faithfully continue with your plan? How motivated are you to reduce debt and eliminate wasteful monthly interest payments? In what way does the paying of interest each month reflect on your stewardship of the Lord's resources? Identify and prepare to discuss with your group the statement or concept that was most meaningful to you in this lesson. **Record your thoughts:**

RUN WITH IT

ACTION STEP: Using the Monthly Interest Calculator (download from link on page A-6), compute your monthly interest cost. Determine how you will use the equivalent amount of money once the consumer debt is eliminated. Continue tracking your daily expenses using the spending areas listed on page A-4.

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