Living within their means - spending no more than a family has available from their income - can be a struggle for people. Understanding the difference between a want and a need and knowing where money is spent and how to budget so that expenses do not exceed income are all essential life skills. By identifying wants and needs and creating a budget to track income and expenses, you can see how to live your life on a balanced budget and avoid debt.

**Wants vs. Needs**

Everyone has certain **needs** that must be met in order to survive, including essentials such as food, water, and shelter. When looking at needs realistically, living in society necessitates other expenses that qualify as needs even though they are not truly essential to existence. Some could include clothing, access to health care and hygiene products, transportation, and basic household utilities such as electricity. Needs also include obligations, such as paying off a loan. While you will still survive if you don’t pay off your debts, the consequences would be very serious to your financial well being, so it’s best to consider these types of obligations as essential as well.

In addition to our needs, we all have things we **want** - things it would be nice to have but that we could live without. For example, while we need clothing, expensive designer clothing is not essential. Similarly, transportation can take many forms. We might be able to get by with a bicycle or used car rather than a brand new luxury car. We need food, but we want candy bars. Next time you are tempted to make a purchase, ask yourself: Do I need this to live, or is this purchase just something that would be nice to have? Many times, you will find that you purchase something because you want it, not because you need it.

Does this mean that we should never purchase wants? Absolutely not! What it means is that we should develop a plan for using our money wisely so we live within our means and have the ability to purchase wants without acquiring debt. How can I do this, you ask? It’s simple. Create a **budget**.

**Budget Basics**

A budget is an itemized list of income and expenses over a given period of time; it allows you to plan how you will spend your money and see how what you actually spent compares to your plan. When you are developing a plan for how you will earn, save and spend your money, it is important to keep in mind that you have a finite amount of cash to work with. Using a budget to carefully track income and expenses can help ensure that you live within your means, meaning you do not spend more money than you make. Most people create monthly budgets since many major expenses such as housing, transportation costs, and utilities are paid on a monthly basis.

As you establish your monthly budget, you must think about meeting your needs first. After all of the needs have been listed, then you can begin adding wants to your budget. Before you allocate all your remaining funds to the things you want, you should set aside some money as savings or investments so you will have a “safety net” to prepare for retirement, or if something happens to your income unexpectedly.

The key to successful budgeting lies in making sure you do not spend more than you make. Sometimes unexpected expenses occur. Your car might break down or you might have an unexpected medical expense. If your budget is tight and you have not put money aside to cover these sorts of events, then it can be very easy to get o budget and incur unexpected and unwanted costs.

If you face unexpected costs, don’t have the savings to cover them, and cannot cut your budget enough to pay all of the unexpected costs, one of two things will likely happen. You will either have to make payments on some items past the established due dates, or you will have to borrow money to cover the costs. Both options create undesirable consequences.

Basically, there’s no such thing as “normal” when it comes to spending. Sure, there are norms, but even those are variable. And not only are norms variable, they’re defined by factors that are not within your control, such as your zip code, tax bracket – even the seasons! What you should be asking yourself is: What’s *your* normal?

To keep spending within *your* means, net income (after-tax dollars) should be budgeted according to…

* ***Your* needs**, which should be limited to just **50 percent** of your net income.
* ***Your* savings**, which should equal **at least 20 percent** of your net income.
* ***Your* wants**, which should only take up **30 percent** of your net income.

Establishing your 50/20/30 will require some money tracking, cost evaluating, and emotional digging on your part. Evaluating your baseline 50/20/30 will make financial decisions that much easier – just crunch the numbers to see if adding a new bill will fit your ratio.

Work through this scenario as an example: Thomas just graduated from his post-secondary educational institution with certification as a dental hygienist. He is living in Brunswick earning $50,000/year.

*[\*The career website Sokanu reports that “Dental Hygienists in Maine earn a median salary of****$62,190****per year.”]*

|  |
| --- |
| What is Thomas’s monthly net income? |

|  |
| --- |
| According to the 50/20/30 rule, how much should Thomas be allocating to:  needs [50]:  savings [20]:  wants [30]: |