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Pay Yourself First

I think it's fair to say Americans have been through and seen a lot over the last year and hopefully we have learned something from the experience. We've all heard every pundit's perspective of what's now being called the "Great Recession" but one outcome that I find interesting is an increase in the national savings rate to about 4% over the past year. This may not be what is needed for the quickest possible economic rebound, but hopefully this could be a sign that American's priorities are shifting away from the short-term gratification of spending toward long-term financial security.

To put into perspective how much we've become accustomed to spending, consider that, according to the St. Louis Federal Reserve, Americans were saving an average of 10.94% of their income 1982. So for every \$100 we earned, \$10.94 would be stashed away for a rainy day. Now in 2008, this rate had dropped to 2.63% or \$2.63 saved out of every \$100. While I am using some of the most extreme examples going back all the way to 1959, it is surprising to see how our spending habits and priorities have shifted over the years.

While there are several factors that are always beyond our control, there are also several simple things we can do to start paying ourselves first and put an extra dollar or two in our pocket:

1. Track spending and make a budget. Without a plan it can be too easy to find yourself wondering how you're down to your last dollar at the end of the month. Identifying even small daily expenses and eliminating or just reducing them will add up over a period of months or years. After spending categories have been identified, put pen to paper and write down where you want to be at the end of each month.
2. Follow the budget! It can take discipline but it can be done. The reward is worth your effort.
3. Save for something. Whether it's for a new car, home, a rainy day, or that one item you've always wanted, it's always gratifying to see your savings account grow each month. Once you've reached your goal, ask yourself if you really want to part with the money you've worked so hard to accumulate.
4. Pay off credit card debt. Since this is one area where many people get themselves into financial trouble, avoid it before it becomes a problem. Some advisors say you should pay off cards with the highest interest rate first, but it can also be helpful to start on those with the smallest balances. This approach can provide a sense of accomplishment and may provide the confidence needed to tackle the one with the high balance.
5. Get your credit in check. A credit report is one of the important factors lenders use to determine your rate and whether or not you are approved for the loan. Unfortunately, many people are unaware what kind of condition theirs is in. You can view your report once a year from each of the 3 main reporting bureaus at www.annualcreditreport.com at no cost. Once you've verified it's correct, get working to improve it. Late payments reflected on a report greatly reduce your score and any lender would want to see a pattern of timely payments. A good credit history will get you a lower rate on your loan and the savings can add up substantially over a lifetime. While paying just ¼% more on a home loan as a result of a below average credit history may not sound too bad, you'll be cheating yourself out of thousands of dollars over the typical 30 year period.

6. Look into refinancing your mortgage now while rates are low. If you currently rent, look into whether it makes sense to purchase a home. Rates are at historic lows and your mortgage banker can quickly run the numbers for you to see how much you could benefit (see Nathan Durst's article a few weeks ago about "net tangible benefit"). Even on a mortgage under \$100,000, reducing your rate and/or going to a shorter term can save you tens of thousands of dollars.

While there are many more ways to put a few dollars in your pocket, these steps can start you in the right direction. It doesn't happen overnight and it does take some work, but the benefits may mean you can rest easy in the future. If you are ever in doubt or need of assistance, come see your banker. We're always happy to assist and help if possible. Please contact me by email at mdaily@p-s-b.com or by phone at 309-385-4375.

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