

## **Why Personal Budgeting Is Important**

Tracking the money you spend and planning ahead for future expenses can prevent you from overspending or spending money that is needed for upcoming expenses. Having it written down helps you visualize how much money you have to work with and what you're spending that on.

Unless you're a wealthy heir with a magically endless source of funds, you only have a certain amount of money to work with each month; that's your income. And, on the other side of the equation, you have certain expenses that money goes toward each month.

A budget helps ensure that these two sides of the equation match up. Even if you're only thinking in the short term, planning out what things you need to spend your money on from week to week and month to month means you won't accidentally spend too much on food and end up short on rent.

That's assuming you don't have any plans to save for long-term goals, plan for retirement or achieve any of the life milestones that many people hope to reach, such as buying a house, earning an advanced degree or having a wedding. Assuming you're someone with hopes, dreams and plans that require some amount of funding and long-term saving, a budget is all the more vital, because it helps you map out how you're going to achieve those goals.

Even if you aren't trying to reach a goal, like saving a certain amount of money or paying down debt, having a personal budget is still key to better financial health.

## **How To Make A Monthly Budget**

To create a budget, you need to take a look at your whole financial picture. Look at how much you make, how much you have, and how much you spend.

### **Figure Out Your Income**

First, you need to know what you're working with. Figure out how much money you typically have coming in each month. If your income varies, figure out a monthly average. If it varies significantly, err on the side of pessimism when coming up with your average. For example, if some months you make \$2,000 and other months you make \$5,000, it may be helpful to budget based on the lower number.

### **Figure Out Your Expenditures**

The next step is to figure out how much you spend each month, and on what.

Some expenses will be pretty similar each month – rent, insurance, groceries, etc. – and thus easy to track. Other expenses, such as eating out or varying household incidentals, will probably be different from month to month, making them more difficult to plan for.

However, you can make budgeting a little easier by tracking your regular spending or having an app do it for you. Then, figure out an average for how much you spend on these types of expenses, and if you can, give yourself some wiggle room. That way, if you spend less than planned one month, you can save that extra money for a month where you end up spending more.

## Do The Math

Once you know the what-goes-in versus what-goes-out of your finances, you're ready to start planning.

Ideally, once you add up the costs of all your expenses, the total number will be less than your [net income](#). If your expenses are more than your income, you'll need to look for ways to cut back.

If the two numbers are about the same, think about what your goals are, and what you're currently spending your money on. If you want to make saving a priority and currently aren't putting any money away for that, you'll need to make some sacrifices.

If you're already spending less than you're earning, then you have some money to play around with that you can spend, save, invest or put towards paying down debt.

## Identify Areas You Could Cut Back

If you're spending more than your budget can handle, you'll have to do an audit of what you're spending your money on and find ways to spend less.

The most obvious place to start is with nonessentials that you wouldn't miss too much. Look at all the subscriptions and memberships you're paying for. Maybe you don't really need multiple video streaming services, or perhaps you haven't gone to the gym in months. Finding expenses like these to cut out will add up, especially over time, and can potentially save you a good chunk of cash.

Then, look at some of the fun stuff you spend your money on – things that you like and are nice to have, but that you don't necessarily need. While it's perfectly fine to spend your money on things that give you joy but aren't necessities, the key is to pick and choose the things that are most important to you, and cut back on stuff that's not as important.

A potentially more significant way you can cut back also tends to be more difficult – reducing how much you spend on necessities. For example, if you're currently spending a lot of your money on rent, it might be worth it to consider looking for a new place with lower costs, or bringing in a roommate. You won't always be able to make cuts in this area, but it can be worth it to take a look and make sure you aren't overspending on something unnecessarily.

## How Much Should I Be Spending?

One difficulty with creating a good personal budget is that people might not realize what areas they're overspending in, which can hinder them from having an effective, efficient budget. While you can look at averages for an idea of how much you should be spending on a certain area of your budget, they might not necessarily fit your situation, as everyone has their own individual needs.

One budgeting concept that can be helpful is the 50/20/30 rule. This is a formula that tells you how to allocate spending: 50% of your income goes towards needs (housing, transportation, groceries, etc.), 20% to savings (including things like a [401\(k\)](#) or an emergency fund) and 30% to everything else (like going out to eat, concert tickets and other discretionary spending).

Another potentially helpful rule of thumb states that you shouldn't spend more than 30% of your gross income on housing. However, this might not necessarily be helpful to those who live in areas where housing costs are high.

Ultimately, you're going to have to figure out what works for you. By tracking your spending and creating a budget, you can get a good idea of what your spending needs are.

### **Using Your Budget To Achieve Goals**

One of the best things a budget can do for you is help you achieve your financial goals. On its own, a budget is great for helping you avoid money issues – which isn't an insignificant thing – but using your budget to help you achieve goals really puts your money to good work.

The big three goals to think about are creating an emergency fund, putting money away for retirement and paying off debt.

How you prioritize these goals is up to you, though many experts strongly advise focusing first and foremost on an emergency fund. With a well-funded emergency savings account, you'll be able to pay for unexpected costs instead of taking on debt to cover them. And if you end up losing your source of income, you'll have some money to cushion you and cover your basic living expenses while you search for a new job.

Once you've got your emergency fund in place, you can start paying down debt, if you have any. Getting rid of your debt means you'll have room in your monthly budget for other expenses and goals. And starting early on saving for retirement is important as well because the longer you save and the more money you save, the more you'll have for retirement, making it less likely that you'll have to continue working past the typical retirement age.

After that, what goals you decide on are completely up to you. Do you want to buy a house in two years? Figure out how much you'd need to save each month for a down payment. Planning a big vacation next summer? Create a savings account and start tucking money away. A good budget, with space allocated for your savings goals, will help you get there.

### **Keeping Up With It**

When it comes to budgeting, you're never really finished.

It's important to stay on top of your finances. That means continuing to track your spending and sticking with the guidelines you've created for yourself. Additionally, if your circumstances change, you should revisit your budget plan and decide if there are any areas where changes need to be made.

One way you can stay on top of your finances is with [Rocket Homes<sup>SM</sup>](#). Create an account to get your free credit score and plan for what's next by using our Rocket Home's Score Simulator to see how different scenarios can affect your credit score.