Pomegranate Financial

Refresh & Simplify
Your Financial Life

Newsletter

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Emergency Funds & Banking

The Federal Reserve has increased interest rates by 2.25% this year. Certainly there are more increases to come in the last four months of 2022.

Inflation was 8.5% for the last 12 months that ended July 2022.

Interestingly enough my checking account at US Bank still pays 0%. My US Bank savings account still pays 0.01%.

So right now is the best time to review your emergency savings and bank accounts.

First, I'll start with how much you should have (as a minimum) in emergency reserves, and then provide some ideas on where to put those emergency funds, especially since big banks aren't nudging to help you out (even by the pennies).

The CFP Board* recommends keeping at least 3 to 6 months worth of your 'essential expenses' in an emergency fund. That's 6 months if you have one source of income, and 3 months if you have 2+ sources of income. For example, if two spouses work, then 3 months should be sufficient.

Hey! You are more than welcome to have a bigger savings! Covid-19 has certainly taught us that you can never have too much in savings!

***The CFP Board is the standards-setting organization for CERTIFIED FINANCIAL PLANNERS™. They administer and oversee CFP® certification.**

They are like the American Medical Association, but for financial planners.

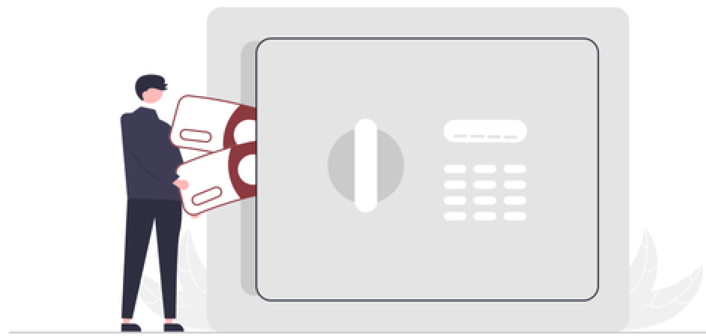
Essential Expenses are what I call 'necessary expenses' because you still pay them when you don't have a job.

Mortgage/rent, food, transportation, utilities, phone, etc. Imagine losing your job - what expenses do you have pay to get by?

Automate Your Emergency Fund - Create A Barrier To Access To It

If you don't have the 3-6 month emergency fund, then start now by automating. Create a transfer each week or month to a separate account to grow your savings. Then make it difficult to access that savings. Put the debit card in your safe or hide it under your mattress. Don't link the account in a way that allows you to transfer it at the grocery store.

Okay, now the more exciting topic - getting that money to do something for you, without taking on too much risk.



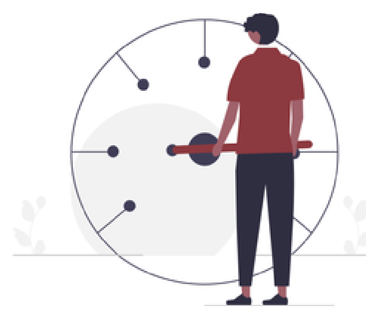
I typically recommend the following:

1 Month of Expenses:
<u>Main checking account</u> - so you avoid transferring funds from savings to checking unless it is an actual emergency. However, emergencies only happen 0-3 times per year. Examples: medical, family, travel, appliance breakdown, etc.

2 Months of Expenses:
High interest bearing savings account! Good news is that there are many options these days other than US Bank (most big banks). This account should be completely liquid so you can transfer funds without penalty.

Here are a few with their current Annual Percentage Yield:

- **Betterment: 1.60%; what I use :)**
- **SoFi: 2%**
- **UFB: 2.21%**
- **Citizens Online: 2.1%**
- **CitiBank: 2%**
- **Capital One: 1.75%**
- **Amex: 1.75%**



These are not CDs! They are savings/money market accounts that pay interest. Interest is not guaranteed and will likely change.

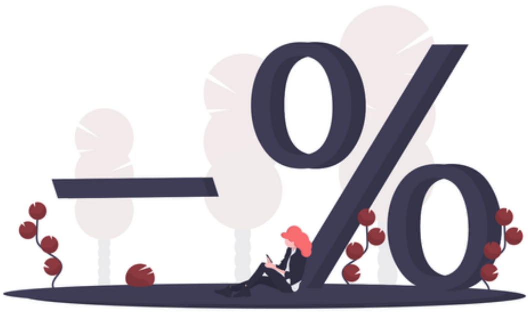
Hey, $10,000 at 2% = an extra $200 per year.

INFLATION:

If inflation has gone up by 9% this year, then your emergency savings has lost 9% of it's value. AND your monthly expenses have probably increased by about 9% or more.

<u>NOTE:</u>

It's probably time to reconsider how much your emergency fund should have - and make a plan to increase it.



Months 4-6 of Expenses:
This is where I am more flexible in my recommendations with clients and where I disagree to some extent with the CFP Board. The CFP Board recommends still maintaining these expenses in an account akin to the savings/money market account.

However, here's my flexible perspective and general recommendation. Specific situations often vary.

What Nobody Talks About = Actually Using Your Emergency Fund:

Ideally you never use your emergency, but life happens and you certainly will. It just happened for me and my credit limit came in clutch - ask me later about my own recent use of savings!

Where do you start? When an emergency happens - you typically start with your credit card! Yep, you heard that right. You probably start with the credit card because of points, limit, flexibility, and convenience. The credit card gives you an extra 30-60 days to see if you can pay it off with extra income, set up a payment plan, or if you in fact you need to dip into savings.

If a payment plan can be set up, then you consider the options. For example, medical debt payment plans can often be set up with 0% interest if paid off in less than 12 months.

Finally, if no other flexible options exist then you can pay off the credit card with your 1st month of savings in your checking account. The 2nd & 3rd months of savings in your money market account hopefully take care of the rest.

Let's Get To The Point:

Taking a small amount of risk with your 4, 5, and 6 month emergency savings is something that might actually be worth it. I'm talking CDs, Bonds, a 30% stocks/70% bonds portfolio, etc. The idea is to get some return over time for these savings to try to keep up with inflation.

In the event you lose your job - then ideally you have a severance package, unemployment compensation, or you find another job within 3 months.

But what do you think? Does this make sense for you? Do you think it's being too conservative or taking on too much risk? Email me your thoughts.

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Have you heard of I Savings Bonds?

These are US Treasury Bonds currently paying at approximately the rate of inflation. Check them out and let me know what you think!