Mastering Your Finances: Financial Freedom

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Achieving Financial Freedom is a big goal, but if you believe it, you can achieve it. If you decide Financial Freedom is what you want, there are a number of personal finance habits you can learn and practice to become wealthy.

What is Financial Freedom?

Financial Freedom means different things to different people, but it's basically the ability to do what you want with your time and energy without having to worry about money at all. Being financially free could mean having enough money saved up in bank accounts and investments where you don't need to work anymore. Financial Freedom could also mean owning a number of businesses which provide you with enough cash flow where you have your bills paid each month without having to work.

Becoming financially free is something everyone wants, but not everyone knows how to get there, or knows why it would be empowering. For me, Financial Freedom means being able to do what I want to do when I want to do it. No mind-numbing corporate meetings, no talking to pushy co-workers, no early morning commutes, only working on my hobbies and my passions.

There are many different versions of the Seven Steps to Financial Freedom. I've seen several but the one that I found to work best for me is the one by Dave Ramsey. Dave Ramsey calls his The 7 Baby Steps.

The 7 Baby Steps to Financial Freedom

For those of you who don't know, Dave Ramsey is a personal finance and money management expert with a radio show and many courses and workshops that help people get their finances in order.

- Step 1 – Save $1,000 for your starter emergency fund
- Step 2 – Pay off all debt (except the house) using the debt snowball
- Step 3 – Save 3 to 6 months of expenses in a fully funded emergency fund
- Step 4 – Invest 15% of household income for retirement
- Step 5 – Save for your children's college fund
- Step 6 – Pay off your home early
- Step 7 – Build wealth and give

Opinions vary, but I like these, and I believe that for most people, these steps are great for building wealth and reaching Financial Freedom.

They have worked for me, and I believe that they can work for you too. I believe that if you follow these steps, you will achieve Financial Freedom. While these steps need to be done in order to be fully successful, you can be working on several steps at once. Just bear in mind that each step must completed in order to achieve success with the next step.

Step 1: $1000 Starter Emergency Fund

An emergency fund is most important for your personal finance success. This first baby step is the STARTER emergency fund. It should be enough to get you through most simple financial emergencies. For example, what happens when the furnace or AC goes out in your house? What happens if your car breaks down, or you get sick? There's so many unplanned emergencies to account for. Having a basic safety net will be beneficial for your financial well-being, and will also be great for peace of mind. $1000 is just the beginning. Don't stop when you get to $1000. Keep going. The goal is to get thru step 3 where you have 3 – 6 months of savings in your emergency fund.

Step 2: Pay of all debt (except the house) using the Debt Snowball

Debt is dumb. You'll never get rich spending money. You get rich by saving money. You save money by spending less money than you earn. You have to decide for yourself about the tradeoff. What are you willing to NOT have in order to have the money to put into savings?

Debt is a hole you dig yourself. Interest is the silent thief who digs a bit deeper. The first step to getting out of debt is to STOP digging! Cut up all those credit cards and pay them all down to ZERO. Even if you stopped using credit cards, month by month the interest itself will continue to dig that hole deeper and deeper, so you want to get rid of this debt and this thief as soon as possible.

There are several debt reduction strategies, but the Debt Snowball is the one that worked best for me. I love the debt snowball. I don't know why I never thought of it myself. Previously I just paid a bit of money across all of my outstanding debts and it never seemed to help. The Debt Snowball is simple and it works. It's for credit cards, car loans, furniture loans, and all the rest of your 'signature' type loans.

Here is how it works in Dave's own words: *"The math seems to lean more toward paying the highest interest debts first, but what I have learned is that personal finance is 20% head knowledge and 80% behavior. The principle is to stop everything except minimum payments and focus on one thing at a time. Otherwise, nothing gets accomplished because all your effort is diluted. You need some quick wins in order to stay pumped enough to get out of debt completely. When you start knocking off the easier debts, you will start to see results and you will start to win in debt reduction. So list your debts in order with the smallest payoff or balance first (excluding the house). Do not be concerned with interest rates or terms unless two debts have similar payoffs, then list the higher interest rate debt first."*

I began by making a list of all of my outstanding signature debts, smallest to highest dollar amounts. Using my budget, I cut back on as much as I could so that I could put as much as possible into paying off the first debt (I still made the minimum payments to the other debts).

Once it was paid off, I took all the money I was paying towards this debt that no longer existed, and I applied it to the next debt. It took me about a year to get them all paid off. It could have taken less time if I had been able to work a part time job or find some other source of income, but I could not. If you have that option, then that will only increase the speed at which you get them paid off.

Step 3: Save 3 – 6 months of expenses in a fully funded emergency fund

Step 1 is to create a STARTER emergency fund. Step 3 is where you FULLY FUND it. Once you are debt free, you take all of that money that you were paying to reduce your debt, and now you start putting it into savings. This should be in ADDITION to the money that you were already putting into savings. Your goal is to have AT LEAST 3 months of expenses in the savings account. 6 months is better.

Depending on your job, 3 to 6 months of expenses in savings may not be enough. If you are self-employed, you might want to consider having a full year of expenses saved in the bank. Also, bear in mind, that this is for the 'loss of job' emergency. You don't have to have half a year's salary in savings, but half a year's EXPENSES. And if you lose your job, I am pretty sure that a lot of those WANT expenses are going to get zeroed out until you are employed again. This emphasizes the importance of Step 2. If you have a lot of debt, then it is not so easy to remove them in an emergency. So, get that car and those credit cards paid off ASAP.

As was seen in 2000 with the 'Tech Wreck' followed by 9/11, and in 2008 with the 'Bank Crash', and most recently in 2020 with the Pandemic, you never know what can happen that is out of your control. Having 6 months (or more) worth of money in savings can ensure that you can survive such tragedies.

Step 4: Invest 15% of your household income in retirement

When it comes to long-term investing, time is your best friend. This makes sense because the longer you can put money into investments, the more you will have at the end. However, the one thing that people don't think about is interest. Just as interest is a thief when it comes to debt, interest is your other best friend when you are investing. Year over year that interest will compound. That is to say, you will be getting interest on your interest.

I was a fan of mutual funds years before I ever found Dave Ramsey, and I was pleased to hear that he agreed with me. Statistically very few investments out-perform the stock market (as a whole). Some of the safest mutual funds are those that are based on the market itself, such as S&P 500 Funds. This article is not the place to go into detail about what mutual funds are, what a market-based fund is, etc. There are many, many financial web sites that go into that detail. I will say that unlike savings accounts where you get a fixed interest rate of return with no risk of loss, the stock market goes up and goes down, so it is possible to lose money. I have included a couple of links above as starting points for you to educate yourself about investing. I strongly suggest that you educate yourself as much as possible regarding the various types of investments so that you thoroughly understand the pro's and con's of each investment type so that you can determine where and how much you want to risk your hard-earned money.

Whether you are self-employed or work for someone, you need to take advantage of every retirement investment opportunity available. This includes a SEPP/IRA for those who are self-employed, and a 401K for those who are not. If your employer provides fund matching for investing you should definitely take advantage of this 'free' money. These types of investments also provide tax benefits. By putting money into retirement accounts, you can possibly lower your income taxes. Again, you need to educate yourself.

Step 5: Save for your children's college fund

When we moved to Florida, I opened a Florida Prepaid College plan for each of my kids as soon as they qualified. Back then my cars were paid for and the total cost of the Prepaid College plan for all of my kids was about what I had been paying towards a single car payment. Dave Ramsey recommends against a Prepaid College Plan and recommends other types of investments for college. You will have to decide for yourself which plan is best for you.

Believe me when I say, there is nothing like the peace of mind knowing that your kids will have the money necessary for the opportunity to go to college, if that's right for them.

Step 6: Pay off your home early

I have a 30-year mortgage. Dave Ramsey recommends a 15-year mortgage. Using a mortgage calculator I learned that that by being 1 payment ahead and by paying a few hundred dollars or so on the principal each month I could significantly cut the duration of my mortgage.

For example. My current mortgage company has an auto-pay capability where they take payments every 2 weeks instead of 1 per month. Each 2-week payment is about (but not exactly) half the monthly payment. Instead of 12 large payments, I have 26 smaller payments which is about equal to 13 annual payments. The benefit of this method is that not only is each payment more manageable (and more easily fits into my semi-monthly paychecks), but 'hidden' in those smaller payments is that one extra monthly payment. It also means that I am paying down interest more frequently which reduces the overall cost of interest. For me, this simple payment plan will reduce my mortgage by about 5 years.

Also, according to the mortgage calculator, if I were to pay an additional 50% extra per month directly towards the principle, I could conceivably cut the length of my mortgage in half, and save literally tens of thousands of dollars over the life of the loan. (As the car people say: "Your mileage may vary").

I have heard of several other techniques that people have used to shorten the duration of their mortgage payments. This works for me. You will have to decide for yourself which technique is best for you.

Step 7: Build wealth and give

Each step moves you progressively to being totally debt free. By the time you reach this step you will be debt-free with money in the bank for emergencies, retirement, and best of all, having fun. It has been said that "No matter how wealthy you become, there's one thing you should always remember: It doesn't matter unless you share it with others".

With these 7 steps, you will be on your way to Financial Freedom.

However, if you are still struggling to get past step 1, a Budget is the single best tool for taking control of your finances.

Budgeting

If you're not in control of your money, your money is in control of you. The only way to get control of your money is to know where it comes from and where it goes. This is what a budget does. It is a TOOL for finding out what happens to your money. The EveryDollar Complete

Guide to Budgeting provides a step-by-step approach to creating a budget.

A Budget will make your money go further and do more. Budgeting is the process of identifying your income and expenses to be able to stay within your means—often with bigger financial goals in mind. For example, tracking this month's groceries might mean finding the money you need for an autumn trip to Mexico. Or it could mean being debt-free by the end of this year. On a practical level, a budget helps you track spending and avoid missed payments, plus it can also help you realize your real-world dreams. Keep your budget current by creating a new budget every month.

If you need assistance with the path to Financial Freedom, you may want to consider a Financial Coach to help you find and then travel that path.

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Be Debt Free - Financial Coaching

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