Financial Math

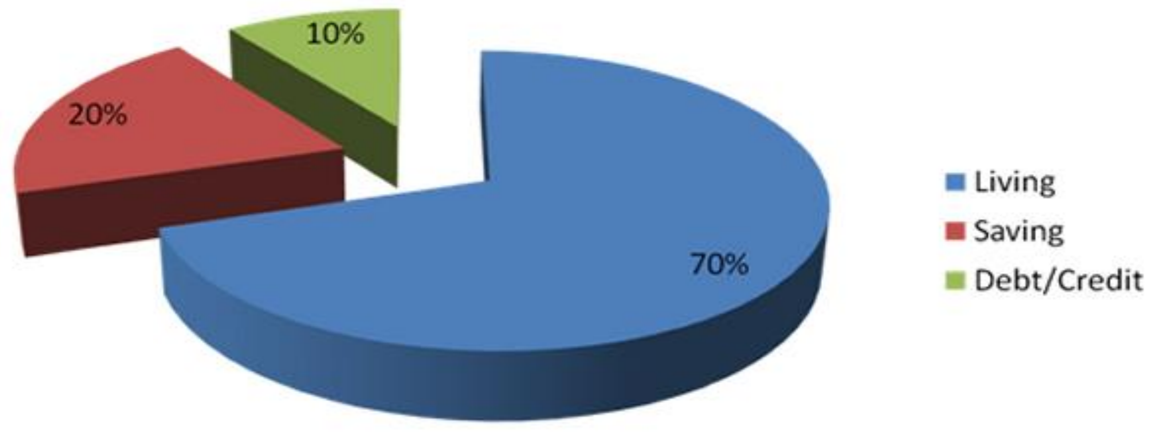
CREDIT UNIT: 20/10 RULE

TUESDAY, FEBRUARY 11TH, 2020

20/10 Rule – Safe Debt Loads

This general "rule of thumb" helps you understand how much credit you can afford.

Credit cards are loans, so avoid borrowing more than 20 percent of your monthly take home pay on all of your loans (not including a mortgage). And payments on those loans shouldn't exceed 10 percent of your monthly net income.



20/10 Rule – Safe Debt Loads

20: Never borrow more than 20% of yearly net income

10: Monthly payments should be less than 10% of monthly net income

** Mortgages don't count*

20% of Yearly Net Income

EXAMPLE: never borrow more than 20% of your yearly net income

If you earn $400 a month after taxes, then your net income in one year is:

12x $400 = $4,800

Calculate 20% of your annual net income to find your safe debt load.

$4,800 x 20% = $960

So, you should never have more than $960 of debt outstanding.

NOTE: *Housing debt (i.e., mortgage payments) should not be counted as part of the 20%.*

10% of Monthly Net Income

Monthly payments shouldn’t exceed 10% of your monthly net income

If your take-home pay is $400 a month:

$400x10% =$40

Your total monthly debt payments shouldn’t total more than $40 per month.