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Introduction to Debt

Virtually every college student these days carries some debt, from student loans to student credit cards to library fines and more. Recent studies quote some outlandish numbers - the average graduating college student carries \$4,138 in credit card debt and \$22,500 in student loans. Managing that much debt successfully right out of college can be incredibly difficult and stressful.

This short guide isn't going to be the comprehensive guide to personal finance - there are already plenty of books, videos, self-help courses and more to do that. Instead, this guide is designed to help you mitigate the impact of debt you've already incurred, and help you start on a path towards digging out.

Let's start out with a few concepts that are really important, concepts that will help you make the most sense of the guide and get the most out of your money.

The Time Value of Money

The cliché that time is money is sort of true. More accurately, money is time - time you've spent working in the past and present to earn it, or time you've borrowed from your future work to use now in the form of money.

Money that you've earned for use now through a job is cash.

Money that you've borrowed from yourself in the future for use now is debt.

Given that we can't ever predict the future with any amount of certainty, it is always, always, always better to spend what you have than borrow what you don't have. Cash is king, as the financial experts like to say, and it's the absolute truth.

Students Speak: How did you earn money during college?

“ A part time admin/office job. Got a sense of how business works, managing styles and a taste of office politics. ”

- Violet Mae, Los Angeles, CA

For every dollar you spend on food, that's a dollar you can't spend on music. Every minute you spend at a job is a minute you can't spend doing something else. Every night you go out to a club is a night you can't spend preparing for exams.

Opportunity cost is important for debt reduction because **every dollar you spend paying on debt is a dollar that can't be used for anything else**. Once you've allocated that dollar to debt, it's gone. That's one of the principle reasons you should pay cash if you can, especially on small stuff like food. More on that later.

Opportunity Cost

There's a principle from economics called opportunity cost. Rather than spout economics jargon, here's the bottom line: *Money that you spend on something can't be spent on something else.*

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Interest is Rent

If you rent an apartment from a landlord, you are renting the use of four walls, a floor, and a ceiling. Renting that space, renting that place, means that you're making use of someone else's home for your stuff. The opportunity cost for the landlord is that while you're living in his or her place, they can't be living there either. In exchange for you living there, you effectively have to pay him or her to live somewhere else. When you're done living in an apartment, the landlord gets it back and you stop paying.

Debt of any kind - student loans, student credit cards, mortgages, auto loans - are effectively rentals of someone else's money. While you're using their money, they can't do anything else with that money because you've got it. When you borrow someone else's money, you have to pay them rent on it, the same way you pay rent to someone to borrow their apartment.

Tying the Concepts Together

These three concepts put together help you to understand why you're in so much debt and can give you clues for working your way out of debt.

Avoid borrowing if you can. Remember, at the end of it all, you're borrowing from yourself. You're fundamentally taking away money from your future self that your future self could use for other things like having fun or living well.

If you have to borrow, borrow at the lowest "rent" you can get. Unlike apartments which vary in quality and location, a dollar's a dollar, and renting one bank's dollar is no different than another bank's dollar in terms of quality. What does change from bank to bank is the rent (interest).

When it comes to repaying debt, your goal is to pay debts back as fast as possible, because the longer you are renting someone else's money, even at low rents, the more you spend on that rent, and the less money you have for other things.

Now that we understand these basic concepts, let's get to the business of reducing your debts.

Students Speak: How did you earn money during college?

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I was a server in a restaurant. Hours are flexible, money is decent. If your willing to learn, there's a lot that job can teach you.

- Brian Harrison, Boise, ID

Babysitting was my job of choice in High School and College. I had very flexible hours, and it's more fun than retail.”

- Susanna King, SC

How To Manage Your Debts

1 Before you go anywhere, figure out where you are

If you've ever gotten lost while driving around, you know that just driving randomly usually leads to getting even more lost. Rarely does random driving help you get un-lost. The same is true of your personal finances. Doing stuff randomly, on the spur of the moment, typically just makes things worst.

Take a cue from driving. The first thing to do when you realize you're lost in your own debts is to stop the car and figure out where you are. We do this with a budget.

We're not going to be doing the massive, multi-page mammoth budget that you've seen and been asked to do in classes or in that fancy personal finance software that someone gave you. No, in order to make sense of your debts, we need to avoid all the complicated stuff that got you into debt in the first place, and that includes all the failed budget schemes of the past. Here's a simple, key concept for your budget: cash flow.

Cash flow budgeting is a concept taken from the corporate world. For many people, especially most students, 80% of the fancy budget terms and ideas simply don't apply to you, like asset management, depreciation, and other concepts that make your eyes cross. The only two key financial indicators that truly matter to someone in debt are:

*The amount of cash is coming in the door = **income**.*

*The amount of cash is going out the door = **expense**.*

In any given time period, you want to have more cash coming in the door than going out the door. You are guaranteed to never be poor if you always have more cash coming in the door than going out the door. You are always guaranteed to be in financial trouble if you're always spending more than you're earning.

How do you figure this out? Simple. Take a blank sheet of paper and draw a line down the middle. In the left column put CASH IN at the top. In the right column put CASH OUT at the top. Tape this sheet of paper somewhere that you'll see it every day, ideally often throughout the day. Then throughout the week, every time you earn money with a paycheck, money from your parents, any kind of money earned, write it in the CASH IN column.

Throughout the week, every time you spend money on anything, anything at all, write it down in the CASH OUT column.

Do a sheet each week. At the end of 4 weeks, staple the sheets together and add up the month's totals. If your CASH OUT column total is bigger than your CASH IN column total, you've got some work to do.

Logically, there are two ways to get things fixed. You can increase the amount of money in the CASH IN column with a job (or a second job if you have one already) or other source of income. You can decrease the amount of money in the CASH OUT column by reducing spending in as many areas as you can while still meeting your obligations (bills).

Since it's usually easier to cut spending than to add income (because money is time spent working and there's only 24 hours in the day), focus first on reducing spending. There are two fundamental types of expenses:

Things you MUST spend money on. These are your debts, the money you owe that you are legally bound to repay. This also includes basic quality of life stuff like a place to live, food of some kind to eat, etc. In personal finance jargon, these are mandatory expenses.

Things you CAN spend money on, but don't have to in order to survive. These are things like cable, mobile phone service, eating out, beer, etc. In personal finance jargon, these are discretionary expenses.

Everything, and I mean everything, in category #2 is up for grabs when it comes to making your finances work. Your goal in managing your budget is to achieve a point where the money coming in the door equals or exceeds the money going out the door. Do whatever you need to do - that's why it's important to do that simple one-page sheet every week, so that you can leaf through the sheets at the end of the month and check off the things that you spent money on that you probably shouldn't have, and not spend on those again.

Students Speak: How did you earn money during college?

“ **I worked at a golf course all through high school and college part time, I loved it.** ”

- Miguel Llano, Rochester, NY

2 Stop getting into more debt

The first rule of not digging a deeper hole for yourself? Stop digging. This means that you need to absolutely, positively stop incurring more debt. Whether that means eliminating discretionary expenses in your budget that you're charging or not applying for any more credit cards or not taking out another student loan, stop getting into more debt is the first and most important thing you can do.

In order to stop getting more into debt, you need more money, right? So let's tackle some specific ways to fix that part of the equation.

3 Trim back spending to free up cash

Let's tackle your discretionary expenses next. These are, as discussed earlier, the expenses that you can live without, be they luxury foods or goods (beer), services (mobile, cable TV, etc.), dining out, entertainment, etc.

A lot of people make a critical mistake when it comes to trimming discretionary expenses - they prioritize the expenses they'll drop by dollar amount saved. Why is this a critical mistake? Because they'll trim out a few big ticket items and their quality of life immediately declines, at which point they usually go out and binge spend because they feel terrible.

Take a lesson from folks who are successful at dieting and weight loss - prioritize in order of things you care about most to least. You may love chocolate but can easily do without a side of chips with your sandwich at lunch, so rather than attempt to cut out what's the single biggest calorie item, trim out a big pile of small stuff that you can easily and happily miss.

Students Speak: How did you earn money during college?

“**As a second job, I waitressed and bartended. Hours fit around school and work schedule, I made good cash and I also had a social life at work.**

- Diane Vautier, New Hampshire”

The same is true for your discretionary expenses. Getting rid of your mobile phone may look like a big savings, and it may be necessary at a certain point, but if there are other discretionary expenses you can cut and easily do without, kill those off immediately, without a second thought. That will get you on the money saving track right away.

Reducing how much you spend on discretionary expenses is hard because we live in a capitalist, market-based society in which you're being asked, pleased, begged, and seduced into spending all the time. That said, a number of folks have done some great research into how corporations trick you into spending as much as possible. There's a guide, located at: <http://bit.ly/14bXXG> that's a terrific, must-read for anyone to learn the tricks and how to keep more of your money in your wallet or purse.

Finally, while some expenses are mandatory, **their exact dollar amounts aren't necessarily mandatory**. For example, having a place to live is more or less mandatory. What kind of place that is or whether you live alone isn't mandatory. Moving back to your family's home after graduation may be an option to consider, especially if your family lives in a place which has access to jobs and public transportation.

Food, as another example, is mandatory for survival, but some folks manage to make a second job in food service work double duty for them as they can get discounted meals or some free stuff as part of the job. Other people do things like join a CSA (community supported agriculture) which gets them tons of fresh food (mainly fruits and vegetables) at prices well below the supermarket. Still others join store membership programs and clip coupons religiously to stretch their dollar as far as possible.

Take a look at your discretionary expenses, perhaps with a close, trusted friend or family member, and determine together what creative ways you can make even the mandatory portions of your budget flex a little.

4 Start earning more money

If you do not already have a part-time job, get one. There are no excuses not to have a source of income during college. If you do have a job, pick up a few extra shifts instead of going out on Saturday night. There are solutions. The hardest part to fixing your finances is being self-disciplined enough to seek them out and act on them.

Conclusion

Thank you for reading this free ebook from StudentPlatinum.com, your resource for student credit cards, debt services, and credit education. We hope that you can put some of these tips to use. Remember, there are solutions to your debt problems.

To work on improving and building your credit visit:
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Credits and Colophon

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