

Emergency Funds: Why You Need One & How to Build It

It falls in the category of “things you know you should do but seem like they can wait.”

If 2020 taught us anything, it's that being prepared for the unexpected needs to be a priority for everyone, regardless of life stage or career. Even high income earning households with comfortable cash flow need to anticipate life's curve balls.

It may seem like a daunting prospect, but breaking it down into small steps can make building an emergency fund much less overwhelming.

First, let's get clear on what an emergency fund is...and what it isn't. An emergency fund is money you set aside for those unexpected surprises life will inevitably throw your way. Think of it as a safety net for when things such as any of the following occur: job loss or furlough, an injury or illness that prevents you from working, natural disaster, major car or house repairs – the list goes on and on.

An emergency fund is not to be dipped into to cover last month's expenses when you overextended yourself, nor should it pay for the renovation you've been dreaming about for months. Instead, let your emergency fund be there like a long-time, trusted friend who provides safety and security when you need it most.

Here's how to build an emergency fund that will be there for you when you fall on hard times.

Enter how much you spend per month for each line item below.

Rent/Mortgage:	
Utilities (gas, electric, water, etc.):	
Phone, Cable and Internet:	
Car Insurance:	
Home/Rental Insurance:	
Life Insurance:	
Health Insurance (Including Vision, Dental):	
Transportation Costs:	
Debt Payments (credit card and all loans except mortgage):	
Personal Living Expenses (grocery, personal items, prescriptions):	
Daycare/Tuition/Childcare:	
Taxes:	
Add up all of the items above and then multiply the sum by six:	

Step One:

Calculate How Much You Need

This is the amount you need in your emergency savings fund. ▲

Answer the following questions and you're one step closer to having the emergency savings fund you need.

How much do you currently have saved for a rainy day?	
Now, subtract what you have saved currently from what you calculated in Step 1 that you'd need for your emergency savings fund. How much do you still need?	
After deducting your costs of living from your monthly income, how much can you TRULY afford to set aside each month to build up your emergency fund? Do not include discretionary spending such as dining out, entertainment, etc. in your costs of living.	
Finally, determine how many months it will take to achieve your emergency savings goal. Divide how much you can afford to save each month by the amount of money you still need to save:	

Step Two:

Determine the Path Forward

This last step is arguably the easiest to complete and will help you realize your emergency savings goals with significantly less effort. It also, however, is the step that's largely skipped or ignored and why many Americans still don't have the emergency savings they need today.

Step Three:

Make it Happen

Do yourself a favor and pay yourself first each month. Start today by opening a savings account that is not connected to your checking account. Then, create an automatic monthly transfer scheduled for a day or two after payday for the amount you determined you truly could afford to save each month.

Once that's done, sit back and watch your savings grow.