Do You Have Enough in your Emergency Fund?

By Gleba & Associates

The biggest financial mistake most Americans are making is not maintaining an emergency fund.

The single worst money mistake you can make is to fail to maintain a cash cushion for emergencies.

Nearly half (49 percent) of Americans are still living paycheck-to-paycheck, even as the "Great Recession" ended in 2009, according to a GoBankingRates survey.

Nineteen percent of Americans have nothing set aside to cover an unexpected emergency, according to HomeServe USA data. Nearly 31 percent of Americans don't have at least an extra $500 set aside.

The lack of a financial safety net is an incredibly precarious and stressful situation to be in. Eventually, an event like a job layoff or a medical emergency will happen to most of us. Without an emergency fund, this can trigger debt that gradually spirals out of control.

So why do few Americans ignore an emergency fund? Many people do not treat emergencies with urgency and respect. The gambling mentality of "I'll take shot that it won't happen" is a bad attitude and poor planning for the uncertainties in life.

If income is lost, how do you pay the necessary bills to not get kicked out of your home, haveyour power turned off, or continue to put food on the table?What about unexpected health- or home-related expenses?"

Many people are forced to run up credit card debt which is an expensive way to handle emergencies.

Ask yourself these 2 questions:

1) How much cash in the bank would help you sleep okay at night?

2) Add all your monthly expenses and include an additional 20-50 % depending on your age and sources of income. We feel 4-6 months of income is appropriate, and if you are retiring 6-12 months of expenses is good.

Rainy Day Fund

The primary roadblock to building anemergency fund is your own disinterest. The problem is that you do not feel that having money aside is important until it is too late.

Financial planning doctrine tells us to have three-to-six months of expenses on hand in a readily accessible, ideally interest-bearing account. For wealthier clients, it's important to consider a number of factors when determining how much coverage they need, including a breakdown of expenditures, risk of an emergency occurring and duration of the emergency.

To identify whether the emergency fund is enough, we look at the percentage of expenditures that are discretionary, like dining out and entertainment versus fixed expenses like a mortgage and car payment.

Once we back out a large percentage of discretionary expenditures and savings, we have a good idea of what your monthly expenses you need to cover. We find some people surprised at what they really need when we look at a worst-case-scenario budget.

Identify the Risks

It's also important to identify the risks of an emergency occurring.

If the emergency we're trying to fund is job loss, we need to look at the likelihood of that happening. Physicians, or tenured professors, for example, are typically not at a very high-risk for unexpected job loss and may not need as much money sitting around earning low interest.

Someone just starting out or in a highly cyclical industry may be more susceptible
and thus want to work hard at saving four-to- six months’ worth of fixed expenses. However, if they're just starting out, their fixed expenses should be lower, and finding a job replacement may be quicker than that of a professor or physician.

If you have questions or concerns about your emergency fund, reach out to us and let Gleba & Associates help you be prepared for a “worst case scenario.”