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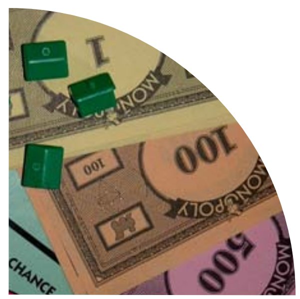
THE COST OF LIVING

YOUR FAMILY'S GUIDE TO MONEY



BEATING THE CREDIT CRUNCH

You don't need to be a financial expert to know that times are a little tougher for families across the UK. In the twelve months to August 2008, petrol prices rose by more than 17p a litre, and diesel rocketed by more than 27p. At the same time, food prices - even for basics like bread and milk - have steadily gone up, while gas and electricity bills have gone through the roof.

With this kind of inflation, the cost of feeding, clothing, transporting and housing a family is heading skywards. Without a pay rise or some savings in the bank, all but the most carefully managed family finances could soon unravel.

But salaries are staying put as long as our employers also feel the pinch, and not everyone has savings to draw on - so how do you ride out the current climate and enjoy family life without getting yourself into debt?

That's the question we've set out to answer in this e-book. In the next five chapters we'll talk you though the finances of your home, car, borrowings and savings, holidays (well, everyone's got to relax), and the other bits and bobs that make up family life. For each, we examine the biggest costs families face, and the biggest savings they can make. There's advice, top tips, and examples of families who've made great money-saving changes.

How do you enjoy family life without getting into debt?

True, it's not an easy time for family finances, but with a bit of careful budgeting, and the advice and examples contained in this e-book, we hope you'll beat the credit crunch, and be in even better shape when it's over.

CHAPTER 3
BORROWING AND SAVING

Soaring energy and food costs, inflation at a 16-year high and fears of a recession: it's no surprise that debt is becoming a major problem for many families.

Citizens Advice Bureaux in England and Wales have reported that mortgage arrears problems rose by 35% in the first two months of 2008 compared with the same period in 2007. And as the credit crunch continues to bite, there's every chance things could get worse before they get better.

MANAGING YOUR DEBT

How bad is your debt? Here are some warning signs that could mean your borrowing is out of control:

- Being unable to get out of your overdraft and into the black
- Missing payments for bills
- Regularly withdrawing cash on your credit card
- Taking out new credit cards because you've reached the credit limit on another card
- Using cards to pay off your loans
- Taking out loans to pay off credit cards and then spending on the credit card again

For more information and impartial advice try the **Citizens Advice**, **National Debtline** or the **Consumer Credit Counselling Service (CCCS)**.

Pay secured and priority creditors in full. Try not to obtain more credit when experiencing financial difficulties

Martin Bamford, joint managing director of financial advisors Informed Choice and a former chairman of the Society of Financial Advisers, urges consumers to prioritise their debt.

"Borrowing money is expensive and debt is a drag on your ability to meet your other financial objectives," he says. "By planning ahead you can save money to buy things for cash, which always works out much cheaper in the long term.

"Getting rid of your unsecured debt – things like credit card debt, personal loans and overdrafts – is an important first step when taking control over your financial planning."

Other tips for controlling your debts include:

- always pay secured and priority creditors in full;
- don't try to obtain more credit when in financial difficulty;
- maximise your income and claim all the benefits and grants to which you're entitled.

PRIORITISING YOUR DEBT

Try to pay off debts with the highest interest rates first. Spend as much as possible on paying off your most expensive debt while making the minimum payments on your other debts. Then tackle the next one, and the next one. Personal finance advice site **Fool.co.uk** calls this technique 'snowballing'. Once you've paid off your first target debt, you then use all that freed-up money to tackle the next one on your list.

Try to pay off debts with the highest interest rates first

CREDIT CARDS

Despite the credit crunch, it is possible to get good deals on credit cards. However, lenders are tightening their credit scoring, which means that it could be harder to get the best deals or the credit limit you want if you don't have the best credit history.

If you want to borrow with a credit card, rather than paying your balance in full each month, you could either opt for a card with an introductory 0% deal, or one with a permanent low rate. To make the most of a 0% deal, plan to pay off all of your debt during the special offer period. When the deal runs out the card will switch to a standard rate, which could wipe out any advantages that the 0% deal gave you in the first place.

If you're looking to transfer an existing credit card debt, shop around for a 0% deal – but be warned: the average transfer fee is now 3% of the balance and most cards don't cap these fees. If you don't want to switch again, go for a card with a low rate – either for an introductory period or for the 'life of balance'.

LOANS

Taking out a personal loan is a good idea only if you need to borrow at least £5,000 – perhaps to make a big purchase, or to pay off a costly overdraft or credit card debt charged at a higher rate of interest.

It can be cheaper for a homeowner to extend their mortgage borrowing rather than take out a personal loan, as mortgage interest rates tend to be lower than those rates applied to personal loans, credit cards or overdrafts. However, there are drawbacks: when you use your mortgage to borrow more money you tend to repay the loan over a longer term, and this can lead to higher total interest charges.

Mortgage lenders tend to be fairly relaxed about your reason for borrowing more money, but you will need to tell them why, and be able to demonstrate that you can comfortably afford the repayments.

Be warned that consolidating debt can be risky. If you transfer balances from credit or store cards to a loan, it can be tempting to carry on borrowing on the cards, which will lead you into further debt.

CASE STUDY

Edward (23) and Sarah (26) are planning to move into their own place around the time they get married in Summer 2009. They have been saving in earnest since Easter 2008.

They earn £30 - £32k a year between them and live with Edward's parents, paying £216 each per month.

They made a decision not to move into rented accommodation in order to save the maximum amount of money – around £500 between them each month.

Edward's parents match each month the money Edward and Sarah are able to save.

David, Edward's father, believes their arrangement is the best way for all parties to save responsibly.

He says: "We will have to give them money to get them out of the nest – the way to effect that and reduce the amount for us is to match what they are saving.

"This encourages them to save and reduces our overall contribution – because otherwise we would have to pay for it anyway.

"The good thing for us is it is coming out of my current and not from our savings – so it is not going to come out as a lump sum.

"In other words it's like 'save as you go'."

Sarah, who has one credit card, paid off the balance at the start of the saving programme, and only keeps it for emergencies.

She says: "I had to draw up a spreadsheet with what I get paid and with all my outgoings including what I spend and what comes out for direct debits.

"I know exactly what I have at any moment and when my bank statement comes it is never a shock."

Edward, who has cut his spending on all leisure, clothing and luxuries to around £150 a month, said: "I have cut back by buying less CDs and DVDs, and I go out in the evening less.

"Now I really appreciate the few things I buy."

PLANNING AHEAD AND SAVING

It's a great idea to build an emergency fund to cover emergencies and big purchases.

"If you build an emergency fund you can avoid having to get into debt for unexpected expenditure," says Martin Bamford. "When you know you are going to have to spend money, such as when you go on holiday, getting into debt is a case of bad planning. Plan ahead and you will be far better off in the long run."

Clare Evans, time-management coach, writer and personal finance expert, advises setting aside a minimum of 10% of your monthly salary. You'll find it easiest to save if you set up an automatic payment straight out of your account into a savings account.

"Once you've got into the habit of saving, you can then take the next step and start investing to make your money really work for you," she says.

Also consider taking advantage of tax-free accounts to make your savings go further: you won't pay tax on the interest you earn. You can invest up to £3,600 each tax year into a cash ISA (Individual Savings Account). You can take any or all of it back out again without any penalty, but you won't be able to pay it back in again.

The best way to understand the rules is to imagine saving £3,600, then withdrawing £2,000 towards the end of the tax year. Even though you'd only have £1,600 left in your ISA, you'd already have paid in the full £3,600 allowance and wouldn't be able to save more until the next tax year.

CHECK YOUR CREDIT RATING

The health of your credit rating will affect your ability to get a mortgage, loan or credit card.

Try **annualcreditreport.co.uk** to see how yours measures up. If it doesn't look good, take steps to improve it: make sure you are on the electoral roll, correct any errors on the report, pay debts on time and don't fire off too many credit applications at once.

TOP TIPS

PRIORITISE YOUR DEBTS – PAY OFF THE DEBT WITH THE HIGHEST INTEREST RATE FIRST

SWITCH CREDIT CARDS TO TAKE ADVANTAGE OF 0% INTEREST RATE OFFERS

PUT ASIDE A FUND TO COVER EMERGENCIES

CHECK YOUR CREDIT RATING AND WORK TO IMPROVE IT