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Financial Briefs

NOVEMBER 2024

What's Better: Saving or Paying Down Debt?

Debt can be dangerous to your financial health. Thus, is it better to save or pay down your debt first?

The answer depends on a lot of factors that are unique to each individual, such as your age, how much you've already saved, what rate of interest you're paying, and more.

A review of the basics of financial planning is a good way to approach the subject. Here we outline how you should use income not dedicated to day-to-day expenses, in order of priority.

First Priority: Insurance

One of the best routes to financial ruin is to not have adequate insurance, so your first priority should be to have the right kinds of policies in the right amounts to protect you and your family.

If you're young and unmarried, this means having basic health insurance. Beyond that, if you have a family, you should have life insurance as well as short- and long-term disability insurance. In each case, you're looking to provide yourself or your survivors with a replacement for income you and they count on.

The bottom line: if you have debt, consider making only the minimum payments until you're properly insured and you have the next two priorities covered as well.

Second Priority: An Emergency Fund

Even if you don't have a family, you need to protect yourself against a job loss or major unexpected expense. The rule of thumb is to create an emergency savings fund equal to three to six months of your income. Not only does this give you breathing space against hardships, it also affords you the flexibility to move in connection with a job change you might want to make.

You should make creating an emergency savings fund a priority. If you can't take care of priorities one and two while also paying

for basic necessities, like groceries and gasoline, you're living beyond your means and should cut back on your spending.

Third Priority: Retirement Savings

Finally, it's imperative to start saving for retirement as soon as possible. Time is both the best ally and worst enemy of the saver. Start saving too late, and it's possible that you'll need a rate of return you can only achieve in your dreams to accumulate enough for a worry-free retirement. On the other hand, even small amounts — as little as \$25 a month — put away early enough

Continued on page 2

How to Improve Your Credit Rating

Credit scores are important because they determine your ability to get a loan, which most people need to buy a house or a car and maybe even to send a child to college. Credit scores also impact the interest rate and fees you will pay on that loan. Additionally, it can affect whether a landlord will rent to you, an employer will hire you, an insurance company will cover you, and if utility companies will turn on services. While you need credit to get credit, having healthy credit is a balancing act.

What Is a Good Credit Score?

While creditors use different

credit scoring models, the following provides a good example of score ranges:

750 and above	Excellent
700–749	Good
650–699	Fair
550–649	Poor
550 and below	Bad

The scoring models use five key factors in determining your credit score, including:

- **Payment history** determines how much of a risk you are to creditors in your ability to make timely payments.
- **Amount of debt** shows how

Continued on page 3

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What's Better?

Continued from page 1

can grow to sizable amounts by the time you're ready to retire.

With these three priorities covered, if and when you have money left over, it's time to consider making extra payments to tackle your debt.

Guidelines for Debt Reduction

There are a number of factors to consider when you're ready to start accelerating the pace at which you pay down debt:

- **Start with the highest interest-rate debt.** Instead of paying more on every one of your debts, concentrate on the one that charges the highest interest rate. In general, these will be store credit cards, followed by bank credit cards like Visa and MasterCard. Use all your spare cash flow to pay down one at a time.
- **Is it tax deductible?** Debt that you can write off against your taxes is generally considered good debt. In effect, the tax deduction reduces the interest rate by your marginal tax rate. In most cases, this means home mortgage interest.
- **What rate of return can you expect?** The most important consideration is whether you can earn more by investing your money than the interest rate you're being charged on your debt. If you can earn more in the financial markets than your interest rate, you should invest your money instead of paying off debt. If not, it's worth it to pay off debt.
- **How long until you retire?** This is a key consideration when you're thinking of paying off your mortgage, especially if it's near the end of its term. At that point, the tax benefits are minimal because most of your payments consist of principal, not interest. In addition, if you're 50 or older, the monthly cash flow you'd free up could be devoted to the extra \$5,000 a year you can contribute, pretax, to an IRA or

Paying Off Your Mortgage

There are advantages and disadvantages to paying off your mortgage. On the positive side, any extra money sent with your mortgage payment is applied to the outstanding principal, which can significantly reduce your total interest cost. This reduces your interest expense deduction on your tax return, but you are paying most of the cost anyway. For instance, if you're in the 24% tax bracket, you save 24 cents in taxes for every dollar of interest, but you're still paying the remaining 76 cents.

When paying down principal, you are effectively earning a pretax return equal to your mortgage interest rate, which is a guaranteed return with no risk. Most mortgages allow you to add as much to the payment as you like.

On the other hand, instead of prepaying your mortgage, you might want to use additional funds to invest in investments with the potential to earn higher returns.

Consider the following factors before prepaying your mortgage:

- **Are all components of your financial plan in place?** Before prepaying your mortgage, make provisions for things like disability insurance, life insurance, and an emergency reserve fund.
- **Is all your consumer debt paid off?** Consumer debt typically carries interest rates that are higher than your mortgage rate, and interest payments are not typically tax deductible, unless it's a home-equity loan. Thus, you should probably pay off your consumer debt first.
- **Are you maximizing contributions to qualified retirement plans?** Make sure you are con-

tributing the maximum to your 401(k) plan, especially if your employer matches funds, or are fully funding other qualified plans and individual retirement accounts.

- **Have you investigated other investment alternatives?** Look into other investments whose potential returns may exceed the return from prepaying your mortgage. However, make sure you actually make those investments. You don't want to just spend any money that could have gone toward your mortgage.
- **Are you nearing retirement?** As you approach retirement age, the idea of entering retirement with no debts may make prepaying your mortgage a more attractive alternative. Or you may like the certainty of positive returns that comes from prepaying your mortgage.

If you decide to prepay your mortgage, consider these strategies:

- Switch from a 30-year to a 15-year mortgage. By paying the mortgage off 15 years sooner, you save a significant amount of interest.
- Pay half your mortgage payment every two weeks. Over the course of a year, that equals 26 payments or 13 monthly installments. Check with your lender to make sure this option is offered.
- Add additional amounts to your monthly mortgage payment. This option is the most flexible since you decide on a monthly basis how much to add to your payment. ■■■

401(k). On the other hand, if you have 10 years or more to go on your mortgage, it could be smarter to keep making the minimum payments to retain the tax advantages.

Smart debt management is often overlooked as a way to improve your finances, yet it can be as powerful as smart investment management. Please call if you'd like to discuss this in more detail. ■■■

How to Improve

Continued from page 1

much credit you have available and how much you are using. If you are holding a lot of debt, creditors worry about your ability to take on more and where they will fall on your payment priority list.

- **Age of accounts** provides creditors with a good understanding of how you manage debt.
- **Account mix** shows lenders how you handle different types of credit; so if you only have credit cards, this may keep your score from rising.
- **History of credit applications** shows how often you are applying for credit and if you are overextending yourself.

If your credit score falls into the fair, poor, or bad range, it's probably time to work on improving that score.

Look at Your Credit Report

The first step to improve your credit score is to review your credit reports from all three of the major credit bureaus. If you find inaccuracies on any of your reports, contact the bureau to find out their process for disputes and resolution.

If your credit reports are accurate and your score is suffering, the following steps can help bring your score into the healthy range:

Pay on Time, Every Time

If you are late or missing payments, you need to set up a plan to make sure your payments are made on time. If your bill comes in at a time during the month when you are low on cash, most lenders and creditors will allow you to change the due date.

Ask for Forgiveness

If you are late with a payment, call your credit card issuer or lender to see if they will forgive the late payment. If you have a consistent track record of on-time payments, they will most likely work with you.

If you have an ongoing debt on your report, contact the lender or creditor to see if they will stop reporting the debt to the credit bu-

Do You Have Too Much Debt?

Various rules of thumb exist to help determine when debt levels are excessive. For instance, one rule of thumb states your total debt payments, including your mortgage and credit card bills, should not exceed 36% of your gross monthly income. The problem with rules of thumb, however, is they don't take into account your unique circumstances. Look for these signs that your debt level may be getting too high:

- **You have no money left over at the end of the month.** If you have nothing left to save after paying your bills every month, your debt may be too high. Be especially concerned if you have to dip into savings to pay bills.
- **You've reached your maximum credit limit.** If you've maxed out your credit card limits or are considering obtaining new cards for additional credit, your debt may be getting out of hand. Credit cards should be used as a convenience, not to finance an

unaffordable lifestyle.

- **You're only making minimum payments.** Required minimum payments on credit card debt are so low that it can take decades to pay off the debt. It will be difficult to get your debt under control if you are only making minimum payments.
- **You don't have an emergency fund.** Ideally, you should set aside three to six months of living expenses in case of emergencies, such as a job loss or major home or car repair. If you can't maintain that due to debt payments, your debt level is probably too high.
- **You're not comfortable.** The ultimate test of whether your debt level is too high is your comfort with that debt and the payments that must be made.

If your debt level is too high, take steps now to get your debt under control. Please call if you'd like help with your debt. ■■■

reus if you pay the debt in full.

Consider Your Credit Mix

If you only have one type of credit, it will impact your score. If you've never had a credit card, it may be time to get one. Just make sure you pay your balance off on a monthly basis or make on-time payments.

If your poor credit score is preventing you from getting a credit card, see if you can get a secured credit card from your financial institution. With this type of card, you can secure a line of credit based on deposits into a checking account. For example, if you open a checking account with a \$500 deposit, they will extend a line of credit for \$500. Adding a new account with a positive payment history goes a long way in improving your score.

Not Too Many Cards

Don't go overboard, because the more credit you apply for in a short period of time, the greater damage it

will do to your credit report. Also, it can be very attractive to get a discount for signing up for a store credit card, but realize your credit score will take a hit. When you apply for credit, it is considered a hard inquiry, which will impact your score regardless if you get approved or not; and it will remain on your report for 12 months. So if your score is in between tiers, too much credit can put you in a lower tier.

Watch How Much You Use

Your score will suffer if every month your credit card balances are more than 30% of your limit. Even if you pay off your balance each month, a higher utilization rate will negatively impact you. If you know your balance is going to be above 30% in a given month, prepay some or all of the balance so you will be in the safe zone.

Please call if you would like to discuss this in more detail. ■■■

Business Data

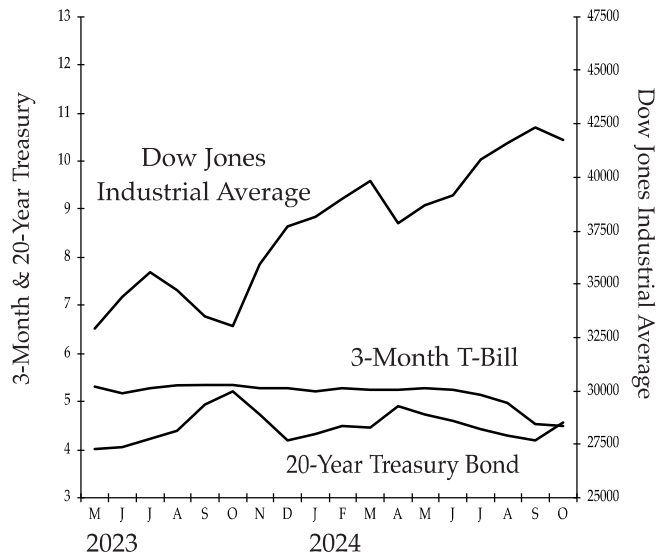


Indicator	Month-end				
	Aug-24	Sep-24	Oct-24	Dec-23	Oct-23
Prime rate	8.50	8.00	8.00	8.50	8.50
3-month T-bill yield	4.98	4.54	4.49	5.26	5.33
10-year T-note yield	3.91	3.81	4.28	3.88	4.88
20-year T-bond yield	4.28	4.19	4.58	4.20	5.21
Dow Jones Corp.	5.06	4.87	5.22	5.17	6.34
GDP (adj. annual rate)#	+1.60	+3.00	+2.80	+3.40	+4.90

Indicator	Month-end			% Change	
	Aug-24	Sep-24	Oct-24	YTD	12-Mon.
Dow Jones Industrials	41563.08	42330.15	41763.46	10.8%	26.4%
S&P 500	5648.40	5762.48	5705.45	19.6%	36.0%
Nasdaq Composite	17713.62	18189.17	18095.15	20.5%	40.8%
Gold	2513.35	2629.95	2734.15	32.2%	36.9%
Unemployment rate@	4.30	4.20	4.10	10.8%	7.9%
Consumer price index@	314.54	314.80	315.30	2.7%	2.4%

— 1st, 2nd, 3rd quarter @ — Jul, Aug, Sep Sources: Barron's, Wall Street Journal
Past performance is not a guarantee of future results.

18-Month Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield May 2023 to October 2024



News and Announcements

Borrow Wisely

- Use debt only for items that have the potential to increase in value, such as a home, college education, or home remodeling. Avoid incurring debt on items like clothing, vacations, or other luxuries.
- Consider a shorter term when applying for loans. Even though your monthly payment will be higher, you will incur much less interest over the life of the loan.
- Make as large a down payment as you can afford. If you can make prepayments without incurring a penalty, this can also significantly reduce the interest paid.
- Consolidate high interest-rate debts with lower-rate options. It is typically fairly easy to transfer balances from higher-rate to lower-rate credit cards. Another option is to obtain a home-equity loan to pay off your consumer debt. In

many cases, home-equity loan interest rates are lower than other forms of personal loans; and as long as the loan is used to buy, build, or substantially improve your home, interest payments are tax deductible.

- Compare loan terms with several lenders, since interest rates can vary significantly. Negotiate with the lender. Although most lenders have official rates for each type of loan, you can often convince them to give you a lower rate if you are a current customer or have outstanding credit. Review all your debt periodically, including mortgage, home equity, auto, and credit card debt, to see if less expensive options are available.
- Review your credit report before applying for a loan. You then have an opportunity to correct any errors that might be on the report. ■■■

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