Activity:
Debt Risk Assessment

This activity guides you to assess your current debt risk. Going through this process can help you identify areas in your budget where you need to make changes to improve your overall financial health.

First, make a list of all your monthly debt payments. Include the following:

- mortgage or rent payments
- credit cards
- installment debt
- car loans
- student loans
- consumer lines of credit
- and any other payment that shows up on your credit report.

Don't include other living expenses like groceries or utility bills in this list; just stick strictly to your debt payments. For the most part, if the debt does not show up on your credit report, then do not include it as a "debt" in your list.

Then determine the level of risk each debt poses. If the debt is unsecured and represents a large proportion of your monthly expenses, it probably represents high risk. But also consider the consequences of non-payment in your risk assessment. Defaulting on a credit card is really bad for your credit; it will prevent you from getting new loans or good interest rates in the future. However, in comparison, defaulting on your mortgage can result in the loss of your home. These two examples represent different metrics of "risk" – that is, one is a financial risk and the other is a financial AND a survival risk. You need a place to live in order to survive.

Loan Name	Risk Level	Monthly Payment Amount
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$
	◯ High ◯ Moderate ◯ Low	$

Total: $ ________________

Now perform your Debt Service Ratio calculation with a calculator by following these steps:

1. Enter your total debt payment number into the calculator
2. Click the divide "÷" or "/" button
3. Enter your gross monthly income (before taxes) into the calculator
4. Click the equal "=" button

The number that is displayed is your Debt Service Ratio. For example, if the monthly expenses that show up on your credit report total $2,000 and your income is $4,000, your Debt Service Ratio is 50% – that is, half of your money goes to pay scheduled debt. The lower the number, the better your ratio.

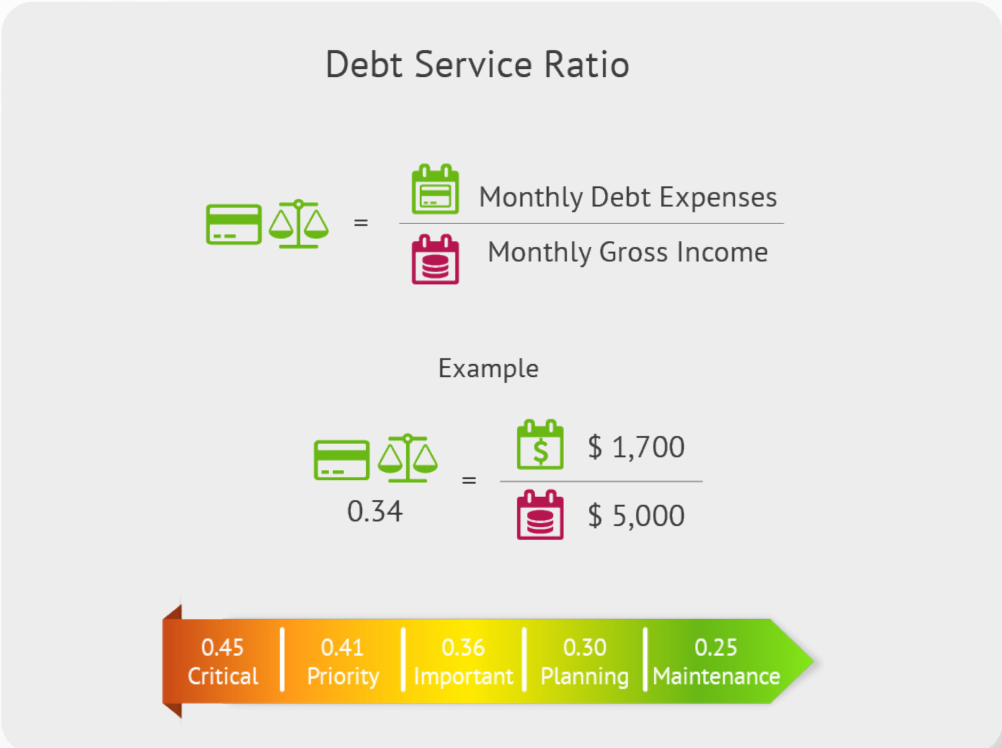
Here are some examples:

You have $1,000 total debt expenses. You have $3,000 gross income.

$$\frac{1000}{3000} = 0.33\text{; A reasonable debt-to-income ratio}$$

You have $2,300 total debt expenses. You have $4,000 in gross income.

$$\frac{2300}{4000} = 0.58\text{; A critically poor debt-to-income ratio.}$$



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When you make the effort to calculate your Debt Service Ratio, you should be better able to identify those areas where you need to make modifications and improvements to your budget. Staying on top of your ratios and working to improve them gradually over time can assist you to move closer to your long-term financial goals. Prioritize creation and implementation of a budgeting plan to address the highest risk, highest interest rate debt first.