NO PREP

How to Avoid Debt

Smart Money Habits for Teens

Includes: Student reading, case study, differentiated questions, teacher key

Name: Period: Date:

How to Avoid Debt: Smart Money Habits for Teens

Debt can feel like a heavy weight, especially when it grows faster than you can pay it off. For teens and young adults, building smart money habits early can make all the difference in staying financially healthy. By understanding the common causes of debt and learning strategies to avoid it, you can set yourself up for a lifetime of financial success. This guide will cover budgeting, emergency funds, and responsible credit use while highlighting the dangers of payday loans and impulse spending.

Understanding the Causes of Debt

Debt doesn't appear out of nowhere. For many young adults, debt begins with overspending or using credit without a plan to repay it. Credit cards, student loans, and even car payments are common sources of debt.

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Understanding the Causes of Debt

Debt doesn't appear out of nowhere. For many young adults, debt begins with overspending or using credit without a plan to repay it. Credit cards, student loans, and even car payments are common sources of debt. While some forms of debt, like student loans, can be considered an investment in your future, other types, such as high-interest credit card debt, can quickly spiral out of control. One of the biggest challenges for teens is the "buy now, pay later" mentality. It's easy to swipe a card or click "purchase" without thinking about how long it will take to repay the balance. If you only pay the minimum amount on your credit card each month, the unpaid balance will grow due to interest. Over time, you could end up paying far more than the original purchase price. Impulse buying is another trap. Social media ads, online shopping, and peer pressure can lead to unnecessary spending. Without a budget, it's easy to lose track of where your money is going, leaving you unable to cover essentials like rent, groceries, or gas.

The Role of Budgeting

A budget is one of the simplest and most effective tools for avoiding debt. At its core, a budget helps you track your income and expenses so you can live within your means. Start by listing all your monthly income, including allowances, part-time jobs, or gifts. Next, write down all your expenses, dividing them into "needs" (rent,

utilities, food) and "wants" (dining out, entertainment). A good rule of thumb is the 50/30/20 rule: 50% of your income should go toward needs. 30% can be spent on wants. 20% should be saved or used to pay off debt. Using this approach ensures you're covering necessities while setting aside money for the future. Budgeting apps like Mint or YNAB (You Need a Budget) can make the process easier, helping you see where your money goes in real-time.

Building an Emergency Fund

Life is full of surprises, and some of them are expensive. Without an emergency fund, unexpected expenses—like car repairs, medical bills, or losing a job—can force you to rely on credit. This is how many people fall into debt. An emergency fund is a savings account set aside specifically for unplanned expenses. Experts recommend saving at least three to six months' worth of living expenses. While this might seem like a lot, starting small is better than not starting at all. Aim to save $500 to $1,000 as a short-term goal. You can build an emergency fund by setting aside a small portion of your income each month. For example, if you save just $20 per week, you'll have over $1,000 by the end of the year. Keeping your emergency fund in a separate account can reduce the temptation to spend it on non-emergencies.

Responsible Credit Use

Credit cards can be a helpful financial tool, but they must be used responsibly to avoid debt. The key is to treat credit like cash—only spend what you can afford to pay off in full each month. This prevents interest from building up and keeps your credit score healthy. Your credit score is a number that reflects your financial trustworthiness. A high credit score can help you qualify for lower interest rates on loans, saving you money in the long run. To maintain a good credit score: Pay your bills on time. Keep your credit card balances low. Avoid opening too many accounts at once. One of the biggest mistakes teens make is using credit for things they don't need, such as expensive clothes, gadgets, or vacations. It's also important to avoid payday loans, which charge extremely high interest rates and can trap borrowers in a cycle of debt.

The Danger of Payday Loans

Payday loans are short-term loans designed to provide quick cash until your next paycheck. While they might seem convenient, they come with incredibly high

interest rates—often over 300%. Borrowers who can't repay the loan on time are charged additional fees, causing the debt to grow rapidly. For example, if you borrow $500 with a 300% annual interest rate, you'll owe over $1,500 in just a year. Avoiding payday loans and exploring alternatives, such as borrowing from family or using a low-interest credit card, can prevent you from falling into a debt spiral.

Conclusion

Avoiding debt isn't about never borrowing money—it's about using money wisely. By creating a budget, building an emergency fund, and using credit responsibly, you can stay in control of your finances and avoid common pitfalls. These habits take time to develop, but the sooner you start, the easier it will be to build a secure financial future.

Case Study: Sarah's Budgeting Journey

Sarah, a high school senior, started her first part-time job at a coffee shop. She earned $600 a month and decided to create a budget to avoid spending all her money on clothes and fast food. Using the 50/30/20 rule, Sarah allocated $300 for needs, $180 for wants, and $120 for savings. Over time, she built an emergency fund of $800 and started saving for a car. When her phone broke unexpectedly, Sarah was able to buy a new one using her emergency fund instead of charging it to her credit card.

1. How did Sarah's budgeting habits help her avoid debt?

2. If Sarah had not created an emergency fund, what might have happened when her phone broke?

Multiple Choice

1. What is one common cause of debt for young adults?

    a) Budgeting too carefully for every small purchase

    b) Paying bills on time

    c) Using credit without a plan to repay it

    d) Saving excessive amounts of money regularly

2. What is the recommended purpose of an emergency fund?

    a) To buy luxury items like designer sneakers and concert tickets

    b) To invest money in the stock market for future returns

    c) To pay for daily expenses

    d) To cover unexpected costs like medical bills or car repairs

3. What is a key benefit of the 50/30/20 budgeting rule?

    a) It ensures money is allocated for needs, wants, and savings

    b) It guarantees wealth and financial security in the future

    c) It prevents all types of debt and financial difficulties

    d) It eliminates the need for emergency funds

Matching

Write the letter of the correct definition on the line next to each term.

Term	Definition
1. ___ Helps manage spending	A) Credit score
2. ___ Avoids high-interest payday loans	B) Budget
3. ___ Tracks income and expenses	C) 50/30/20 rule
4. ___ Measures financial trustworthiness	D) Responsible credit use
5. ___ Prevents overspending	E) Emergency fund

Fill-in-the-Blank

1. The _____ rule suggests dividing income into needs, wants, and savings.

2. An _____ fund is used to cover unexpected expenses like medical bills or car repairs.

3. _____ loans charge extremely high interest rates and should be avoided.

Short Answer

Answer each question in 2-4 complete sentences.

1. Why is it important to set aside money in an emergency fund?

_____

_____

_____

2. How can budgeting apps help teens manage their money?

_____

_____

_____

3. Why should payday loans be avoided, and what are safer alternatives?

_____

_____

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