(auto-translated)

Matt Robison 00:00
Hey Mike, what do you do if you're facing an emergency?

Mike Morton 00:05
Run and scream.

Matt Robison 00:08
That's the right answer. Hey, I'm Matt Robison, and this is Five Minute Finance. That was the very calm, level-headed voice of Mike Morton, our certified financial planner, the one who just gets you logical, easy to understand, implementable, practical answers on how to get things off your to-do list and move on with the rest of your life. And today we are talking about emergency funds. You know, the standard advice, Mike, is you need three to six months of stockpiled money. That's the answer, right? We're done.

Mike Morton 00:40
That's it, man. This has been Five Minute Finance,

Matt Robison 00:43
right? This has been five second finance. All right. So, in an emergency, or if you have a sudden financial need, that's what we're going to walk through today. Like what to do, how to plan for it, how much you need, etc.

Mike Morton 00:57
Yeah. How much cash do you really need? What's an emergency fund? How to think about it? How much do you actually need here in 2026? That rule of thumb: three to six months, Matt. I'm I'm calling cap on that. I think it's outdated.

Matt Robison 01:11
Interesting. And there are some other things you're going to go through here, right? Like there's a Joker fund in here. I love this.

Mike Morton 01:18
The Joker fund. That's that's from our previous podcast, the Joker fund. So you got to look back in the feed for that. So the old rule. We're going to talk about a new rule. Why the old rule doesn't make sense. We're going to talk about two piles, two jobs. We're going to talk about is 18 months the new standard? The AI, you know, in the AI era, where your money actually lives for this emergency fund, and when cash might become one of your bigger risks.

Matt Robison 01:43
Ooh, I feel very titillated. But if you're not feeling quite titillated enough yet, then hang on for all of that plus the listener question, which is about an accusation from a spouse. That's how dare that. That's pretty pointed. I it's this is a harrowing thing to hear from one's spouse. Also, our worth knowing discussion about estate tax break hiding in your money market fund. Ooh, sounds like that clown from it. And finally, our weekly one thing about taking a walk sounds nice. Should we get to it, Mike?

Mike Morton 02:18
Short walk. Yeah, let's do it.

Matt Robison 02:20
All right, so we're gonna break down everything you ever needed to know about emergency funds in just a few quick minutes. Let's start with something you teased a moment ago. This idea of two piles, two jobs. What do you mean?

Mike Morton 02:35
Yeah, so you got to be careful because when people say emergency funds, they tend to conflate like what's an actual emergency versus things that are irregular expenses that are irregular, but they're going to happen. Like your water heater is going to break, and you're going to have to replace your water heater. I hope it's 10 years from now for you, but it's going to happen. That's not an emergency that we know is going to happen, and so this was the Joker fund. You can look that up in the in the previous episodes. was a great episode, but really, what we want to do here is for true emergencies, and this is kind of the loss of a job is the classic one where like I'm not expecting to leave my job. You suddenly lose your job, then you have a true financial emergency where you need money available to cover expenses. So make sure that when we're talking about emergency funds today, this is the true. Hey, I'm not expecting to ever have to spend this money, but if I do, I want it available.

Matt Robison 03:41
My wife and I talk about this all the time about unexpected expenses, which are really expected expenses. It's like, oh, we didn't realize we were going to have to pay $800 to repair our car, and it's like, yes, we did. Of course, we did. You know, like we pay a certain amount every year for auto expenses, and pay our property taxes every six months, or maybe it's quarterly. I don't know. Don't don't prosecute me. So the point is, two piles of money. I love piles of money, but keep two piles of money for two different purposes, and don't kid yourself about what's unexpected versus what's truly unexpected.

Mike Morton 04:20
There you go. Exactly.

Matt Robison 04:22
Got a five minute task for this.

Mike Morton 04:23
Five minute task, man. Making sure to open up your bank account app and create, you know, this true emergency fund. Well, you can do kind of one of two things. If you need the Joker fund, you know, for these unexpected expected costs, go ahead and set that up, and then for this emergency, go ahead and set that up. Banking apps now make it super easy to open up other accounts, and then name it. Here's the tip: name the account for what it's for. You can even you know you can name it after the podcast. Call it the Joker Fund,

Matt Robison 04:56
and you don't have to have like a set transfer. Going in there, this is just set the money aside. Can it be a like a one-time deal, or is that the kind of thing that you want to build up?

Mike Morton 05:08
Well, okay, two piles of money, two jobs. The unexpected, expected costs, the Joker fund that you might want to add money every month. You might want to set up like some automatic stuff in there for these. Oh, a car repair you know things of that nature water heater house expenses that are you know unknown when they're going to happen but you know you're going to have to pay five grand a year so you want to sort of have that money in there so you could do that one and then the other ones for true emergencies that should be a one time set it and forget it because again you shouldn't really you hope to never have to spend this money,

Matt Robison 05:44
right? Right. It's like buying fire insurance or whatever. Okay, makes a lot of sense. All right, let's get to the heart of this here. We teased it long enough. Three to six months. I feel like I've been hearing this ever since I gained any financial awareness whatsoever. It's like, oh, always have three to six months of expenses stored away, and you're telling me that's bullshit. Why?

Mike Morton 06:10
Well, that kind of worked in the you know previous decades where we had more stable careers and stable jobs, and you'd sort of and it's a nice rule of thumb because it's easy. Hey, three to six months. You just take out. Hey, I'm. You'll normally spend 10 grand a month, and so I need 30 to 60 grand just in case something happens. What's nice about the rule is that it's an easy rule, so that's perfect. You know, it's easy to follow. You can multiply your expenses, you know, by the number of months, and then just set that aside. But it's in reality that's not the right number to use for two reasons. One, so we want to think about floor and runway instead of three to six months. Floor and runway, floor being what you really need is to cover your expenses that you

cannot get rid of. So if you lose a job in a true financial emergency, there might be a bunch of expenses you can get rid of. All right, that you don't have to spend. You like to spend things like, hey, we're going out to the movies or we're going out to the concert or whatever it is. You don't have to spend that money. You just like to while you have a job. But in a true emergency, you probably cut a lot of those things. So the floor is all your expenses that you cannot cut, like your mortgage or your rent or the bare minimum grocery shopping, you know, to feed your family, you know, or school costs, like hey, kids got to stay in school or whatever it is. So you want to calculate that. That's the floor, all right. So you need that's your monthly expense that we're going to start with, and then the runway is how long you want to keep having that go. So is that one month, three months, 12 months? And I'd argue in the new AI era, it's going to be a longer runway that you're going to need. So floor times runway.

Matt Robison 07:56
All right, I want to follow up in just a moment on this new AI era because it sounds really promising. Like we're all going to lose our jobs and maybe die. But speaking of all losing our jobs, I like hearing the speech. You know, Matt, jobs aren't as stable as they used to be. It sounds like a precursor to me getting fired. I want to just stab at something though. Here, I what kind of emergency funds are we referring to? Because the way I think I learned it was, oh, keep it in a totally liquid source like your checking account, not a really tied up source like an IRA, for example. But I think of it as there's liquid, illiquid, and semi-liquid. You know, for example, I have retirement savings that are invested, and they're in a target date fund in in a low-cost index fund, and they're semi-liquid. I could access them at any time. It's just that I would pay a capital gains tax for accessing those funds. So, do those funds count, or do only funds that are in a totally liquid source count?

Mike Morton 09:12
Well, now you're skipping ahead, Matt, because it is true that we, when you're first starting off, we want to hold that money in a true, totally liquid, not semi-liquid, semi-stuck. All right, totally liquid. So in your bank, literally, as you're for in your 20s and you're building up this emergency fund, it's in your banking app. You've named it emergency fund. You're depositing money in there to build it up, and at some point, you're like, great, I got my 25 grand, and in case I lose a job when I'm 28 years old, it's sitting right there in my bank. Now, as we get more sophisticated, like you're mentioning, hey, I'm a little bit older. I've got retirement accounts. I've got sort of a bigger balance. This 40 grand of emergency fund is getting. Relatively small compared to you know the the 401k, the IRAs, my extra saving in my brokerage. Then in that case, you do not want to separate emergency funds into a completely separate account and fund. You need to think of it in your overall investments. Now, it still, in my opinion, should be in a money market account or a checking or saving or CD account. But that 50 grand that is your emergency savings is part of your overall portfolio. I like to be 80% stocks because I'm still accumulating. You can now count the emergency fund because of what we said at the top. You do not expect to spend

this money, it is true emergency. You don't expect to spend it, so it can be part of the overall investment retirement portfolio.

Matt Robison 10:49
Got it. Well, I want to keep. I realize I I now skipped ahead of your kind of intended order here, but let's keep parking that AI era question for for just a second here. So, like, just going back to this idea of there's a floor and a runway. How do I figure out what those are for me? Like, is there again? We love five minute tasks. Is there a five minute task version of this? Yeah,

Mike Morton 11:12
yeah. I would definitely go through five minute tasks for this one to figure out the floor is going to be pull some statements. You know, the last month or two months of credit card and checking account. That's usually where everyone's got all their expenses coming out of. Just scrub through that and highlight. You know, hey, here's something I can't get rid of. This is the mortgage. This is my rent. You know, this is my groceries. Oh, but here's the here's the Whole Foods grocery. I could probably skip that and just go to like the Stop and Shop. You know, groceries. So you just kind of highlight all the things that you you couldn't skip if you were truly you know trying to cut way back, add those up, and there's your floor. Got it.

Matt Robison 11:51
All right, and I mean again, oh boy, I'm maybe this isn't sort of like the the order you had in mind, but what you really just set up is this question of like there there are trade offs to all of this right because you're talking about your overall savings and part of what you just said in the first five minute task is that 80% of the job is just labeling is just you being aware and being very intentional about I know that I have designated emergency funds, and by knowing that, I'm not going to touch them, and I'm going to ensure that they're there. But it says less about where they live, and the risk here is that you take those funds and you put them into a totally liquid place that are ready to go, but then you're you're missing out on savings and investment and and interest, so like how how do you think about that trade off?

Mike Morton 12:46
That's exactly right. So the real trade off there is inflation risk or the risk of cash. People love cash, and you know it feels great. I've got 100 grand sitting like in my bank account. It makes me feel wonderful, and I want you to feel wonderful, but the downside of having 100 grand of cash is you are losing purchasing power to inflation. We all know cars. When I bought my previous car 10 years ago, was like 20 grand. Now they're like 50 grand. All right. So if I just had 50 grand of cash 10 years ago, that would have bought a couple of cars. Now buys one car, so you're losing out on how much that cash is going to purchase, even if you're getting some interest on it. All right, so that's the real risk of cash. And so what I said before is really true. Once you've got some good savings in 401k's and IRAs and brokerage account and your bank account, which

has had your emergency fund, you want to look at the big pie chart. Do not separate your emergency fund that's 40 grand or 80 grand from the overall, because you're also going to have some safe bonds and cash in that target date fund. That target date fund is 80% stocks, so you need to put the cash for the emergency fund into your overall portfolio, so you don't have that drag, and you're able to keep up with inflation.

Matt Robison 14:09
Right, right. So there's like an intermediate place, but it's labeled. I mean, that really resonates with me. This idea of you're really making sure that you have that reserve, so that nothing happens to it, and you're also making sure you remember at the beginning of COVID when everyone started talking about well, you need to have a go bag. But your point is, yes, you should have a financial go bag, but beyond that, there is this kind of realm of intermediate. You know, they're they're invested, they're semi semi liquid. They're not in the go bag. They're you know, and you're not undertaking this cash risk.

Mike Morton 14:45
Yeah, let me sum it up here. When you're young and just building emergency fund, just lives in your bank account. Great, build it up, get there. Once you've got a good portfolio, include it in your portfolio allocation. And Matt, I would keep it in liquid funds. I would keep it in the checking account, the money market account, the brokerage account in cash, so that it is liquid, ready to go. I would not put it into the IRA, the 401k. That's not where your emergency fund should live.

Matt Robison 15:16
And before we exit the topic completely, since we did tease it and put it in the parking lot. Let's just talk about whether things have fundamentally shifted in the AI era. I'm not sure I understand what AI has to do with it, other than we're all going to be living atop a mountain of skulls. Why in the AI era are things different?

Mike Morton 15:38
So things are a little bit different at the moment, and this shifts, you know, all the time. But getting jobs is now becoming a little bit trickier, and losing jobs, people have the sense that it's happening more often. It is happening more often in some industries. So that's what I mean about the AI era. So this gets back to so in the AI era, era might be more likely to lose a job. So you're feeling like, geez, I can get cut at any time, and then finding a job could take longer, you know, because companies are really sorting out how are we using AI, where are we using it, do I need to hire people, and again, this is like constantly shifting. So back to the this is the runway. How long you got the floor, and now you need to figure out like, hey, do I need three months, six months, 12 months? What's my runway going to be? This also, this dial in the in the runway. You can think of it like a dial. Hey, we've got two two working parents that have very stable jobs. Say you're like, you know, working as elementary school teachers. You know, pretty stable. You

know, I'm in the union. Like, unlikely I'm gonna lose a job. Great, you can you can dial it down. You know, maybe you only want six months. On the other hand, we've got one worker, one stay-at-home parent. They're in the tech industry that's getting totally disrupted by AI. People are like, you know, you just we're at the water cooler and hearing the chatter of like, you know, downsizing, right-sizing AI. You're like, maybe I want 18 months. You know, maybe the dial is going the other way for your emergency fund. So you know, look at the runway and the dial based on on kind of where you are.

Matt Robison 17:12
Well, I see that you had one more handy, practical, and very useful five minute task, but I don't want to do it yet. I don't want you to give it yet because you also happen to get a highly related listener question this week, and I think the five-minute task goes after the listener question. So, should we move to our listener question?

Mike Morton 17:36
Let's do it.

Matt Robison 17:37
All right. As always, I'll remind everyone that if you're a client of Mike's, I suggest carrier pigeons. That's the technology of yesteryear. Send him a message by carrier pigeon. It will arrive in 1902, and he will get an answer to you. Otherwise, you can email at pod@mortonfa.com with your listener question. This is this week's, and obviously, I can see that you've stored it up just for this episode, and it is we keep 12 months of expenses in cash. It's the only reason I sleep at night. My spouse says we're bleeding money to inflation, and we should invest half of it. Who's right?

Mike Morton 18:18
You're bleeding cash. It's literally bleeding. No, I'm just kidding. The answer is,

Matt Robison 18:23
yeah. I thought you were sucking up to the wife in in that one. Yeah,

Mike Morton 18:28
bleeding cash. You are both congratulations. You're both right. We often say on this show the sleep at night factor kind of trumps a lot of things, and I truly believe that. Of course, we don't want it to, you know. You can't make sort of quote unquote like bad decisions for you or your family that are going to be, you know, aren't going to be successful. Like, oh, I'm just going to spend this amount of money every month and run out of money in five months. Like that's not going to work. But I will say, as long as the you've got a sound judgment on what you're doing and the future looks fine, kind of 50-51 way or the other. The sleep at night factor definitely always wins. So if it makes you feel great having 12 months of expenses in cash, and it's not

going to disrupt your financial future, great. That's perfect. I love that. Sleep at night, it's wonderful. We all need sleep. All right. The flip side is 12 months of cash, as we've talked about earlier in the show. It is losing purchasing power. Okay. Now, if the 12 months fits nicely in your overall investment portfolio, maybe it's five to 10% of your entire retirement fund. Remember, this is money you don't expect to spend, all right. So you're not going to spend this 12 months of cash. So if it's five or 10 percent of your overall investment portfolio, that seems like a pretty healthy balance. That seems great. If it's in addition, if you're like, well, we're in the target date fund. Matt mentioned earlier we're in a target date fund, and that's got 25 percent, you know, cash and. Bonds and and when I look at my overall brokerage, I got you know about 25% cash in bonds, and I also have this 12 month sitting over here, you know this 150 grand, you know kind of sitting outside. That's too much. Now you have too much cash. Okay, when you total the whole thing up, so make sure you're taking a look at the total investment portfolio and make sure it's the right balance, and I love that you're sleeping at night.

Matt Robison 20:24
And it sounds to me like there's a potential for a Solomon-like compromise here, where maybe you don't keep 12 months in cash, maybe you keep six months in cash and six months in one of these intermediate options that you laid out before, and you know you're just lessening the hit. So there's there's probably compromises available. There are compromises, but be

Mike Morton 20:43
careful. Yes, be careful when your spouse

Matt Robison 20:47
is. I for for the husband involved, just just let it go, man. Let it go. She's right.

Mike Morton 20:52
Exactly. Let it go. And by the way, this is the five minute

Matt Robison 20:55
task though that can also help resolve this. That that I teased a moment ago. You did have one about trying to figure out like what's the floor, what's the ceiling, what's the runway, what's the right amount, and and it was writing down a single sentence. What what was that five minute task that can help resolve problems like

Mike Morton 21:13
this? Keep keep so you can write down a single sentence and put it where your mind yourself. We keep and you write it in. We keep 12 months of our fixed costs in cash because, and then write out the end of that sentence. All right, and that way it'll help you guys with. Oh yeah, we're on the same page. This is why we keep the money. So for the spouse is sleeping well at night.

Congratulations. That's why we got 12 months. And for the other spouse, it's like. Oh, I understand. We have it because it helps my wife sleep at night, which makes our family life fantastic.

Matt Robison 21:46
I love fantastic family life. That sounds like something that's very worthwhile. Speaking of things that are worthwhile, should we get to something worth knowing?

Mike Morton 21:55
Let's do it.

Matt Robison 21:56
I am really afraid of the Pennywise the Clown esque setup that you gave me for the thing worth knowing that is lurking somewhere here inside a money market. I don't know. I'm very frightened. Would you tell us what this

Mike Morton 22:11
is? Why are you so frightened about state? You know, state tax breaks. This is a this is an income tax break. So when you hold treasury bills or Treasury only money market funds-they do not get taxed by your state. All right, so Matt, we live in the state of Massachusetts, has about a five-6% income tax here in the state. So if you have 150,000 of earnings at you know three 3% or so, that's five grand of interest. And if you have five grand of interest that is not being taxed by the state, that's a few hundreds of dollars. So there's a nice couple of dinners out just by holding the correct money market in your brokerage account.

Matt Robison 22:55
So the upshot is, if you're going to do one of these intermediate options and you're looking for a money market, you should check out whether your state is among those that does not tax these treasury-only money market funds, and then you can take your wife out to dinner to apologize for the fact that you were so wrong about this whole 12-month issue.

Mike Morton 23:18
That's correct, and all states will not tax the treasuries, so that's true. Some states already don't have income tax, so you're not really. Oh, I see. Right, right. Yeah, you could move to New

Matt Robison 23:29
Hampshire,

Mike Morton 23:30

but if you're in California, if you're in California, it's like 10% state tax. So there, you got a couple of nice. Well, really, probably half a dinner because everything's really expensive out there to go out to dinner. But dude, I went

Matt Robison 23:41
in the wrong direction. I moved from New Hampshire to Massachusetts. Yo, there we go. Yeah, no, I like taxes, man. What can I say? I'm a Democrat. Hey, just a

Mike Morton 23:49
5% salary cut, you know, for this hosting job.

Matt Robison 23:53
I, I, I still feel like you implicitly threatened me with firing earlier. So yeah, I don't know. Well, I've been thinking salary cut.

Mike Morton 24:00
You know, I've been thinking about an AI host. I mean, I'm not sure. Like, that's why we're recording these, Matt. I could feed it into AI and just say, like, look, could you please copy Matt? And that'd be great. Oh,

Matt Robison 24:11
the joke's on you. I'm already Matt GPT. All right, let's get to our one thing. All right, you want to give me electric shocks? I love it.

Mike Morton 24:19
Electric shocks. All right, you need to go for a walk in the woods without the headphones. I, in fact, Matt, I gotta tell you, I was out. I went for an evening jog last night, and when I go in the evenings, I don't wear the the earbuds because it already kind of freaks me out to be like jogging through the woods in the evening, and I definitely need to hear everything that's rustling out in the woods. But that's what you got to do. You got to go without the headphones.

Matt Robison 24:43
Besides avoiding those kinds of attacks, are there other psychological benefits to running or walking without headphones?

Mike Morton 24:50
Absolutely. We've engineered boredom out of our lives. I love this experiment. This is electric shock experiment. So, Timothy Wilson at UVA, you probably might have heard this one. So good. So it's so good. He did. He put people in a in a room, all right, with their phones, and said they could do nothing but sit with their thoughts for between six to 15 minutes, and that's it. That's

the whole thing. Beforehand, he'd give them an electric shock and ask if they'd pay money to avoid feeling it again. And they said, "Yes, yes, I do not want to be shocked. All right. So yes, I would pay money to not get shocked again. He left them with a button in the room that could deliver the same shock. So now you're in a room. You've you've gotten shocked. You you said I would pay money to not get shocked again. Now I'm in a room for about 10 minutes, and I have a button, and two you know that can shock yourself. Otherwise, you just sit there. You just sit there. Those are your choices. You sit there for 10 minutes, or you can press the button. Two thirds of men shock themselves rather than sit There, two thirds, two thirds, Matt.

Mike Morton 25:58
You know, we're so anti-boredom. We've completely engineered it. We know attention spans have been cut in half like every five years for the last 15 years, down to just seconds. That's why TikToks are, you know, super short, and so walking in the woods, you know, without the headphones, increases creativity. Being bored is definitely part of human nature, and really brings alive a lot of who we are. So that's why I recommend it. Get out there, experience. You have to experience it and try it.

Matt Robison 26:33
On that, for Mike, I'm Matt, we'll see you next time.

Mike Morton 26:35
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