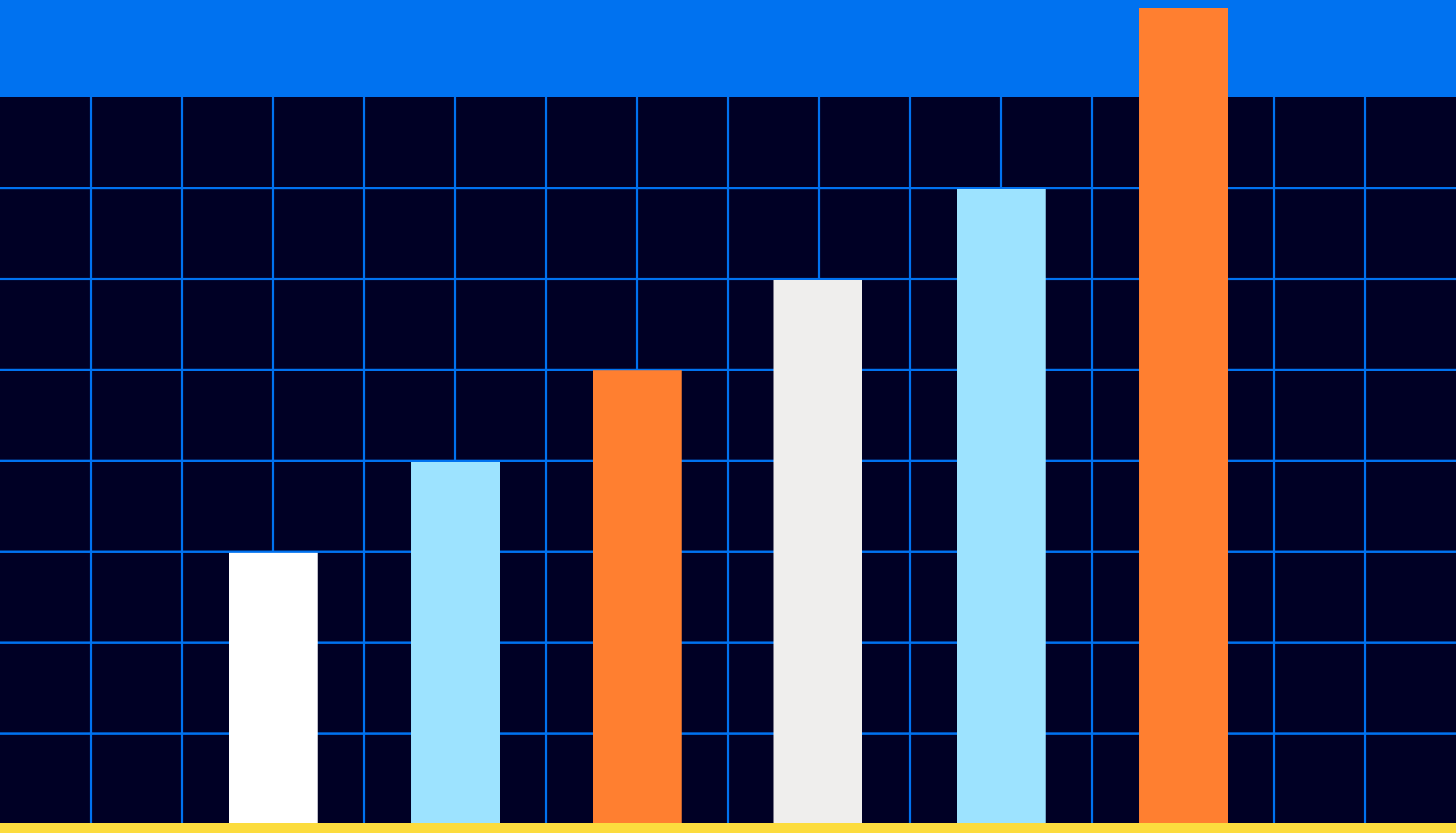
ATB WEALTH™

# FINANCIAL MANAGEMENT FUNDAMENTALS

Reference Guide



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# WHAT IS FINANCIAL MANAGEMENT?

Financial management is the foundation of any comprehensive financial plan. It is the process of ensuring your current cash flow is adequate for achieving your financial and wealth goals. If you do not have adequate financial resources or available cash flow, you will not be able to accomplish your other financial planning goals.

It might be helpful to think of your own personal financial management as being similar to the cash management functions performed by the treasurer in a large organization. Essentially, you are ensuring you have enough cash and liquid assets to:

- Maintain ongoing household operations.
- Ensure that illiquidity does not become an issue.
- Have a sufficient emergency fund for unexpected situations.
- Build a reserve for large or discretionary expenses.

Your personal circumstances will dictate what your specific financial management goals might be:

### Are you spending more than you make?

You'll need to eliminate negative cash flow.

### Do you have any large upcoming expenses that you cannot fund out of your current cash flow?

You'll need to plan for these major cash purchases.

### Do you have more debt than you should? Are you paying the lowest interest rate possible?

Evaluating your debts and interest rates and restructuring your debt will be essential.

### Are you saving for your retirement or other long term goals?

You may have to identify current expenses that can be reduced / eliminated so that funds can be redirected toward financial goals and increase the amount available for savings and investments.

Setting and prioritizing your own personal financial management goals will help ensure the process is personal and motivate you to take the appropriate actions required.

# DO YOU KNOW WHERE YOUR MONEY IS GOING?

Once your goals have been identified, the next step is to determine your cash flow, that is, where your money is coming from and going to. Tracking your income and expenses is critical to achieving your financial management objectives. Every dollar you spend limits your ability to apply funds to your other financial goals.

The **ATB budget worksheet** is a great interactive tool for summarizing both your income and expenses, essentially your current cash flow. It can also be used for estimating your future cash flow, creating your budget and ultimately determining if you are on track to meet your goals.

Regardless of the tool you use, you will need to summarize all your income, expenses and savings and allot these amounts to each budget category (groceries, entertainment, utilities, investments etc.). You'll have to collect data from your bills, bank and credit card statements, and any cash receipts.

Tracking your income and expenses for two or three months will create a clearer picture of your current cash flow. Are you spending in non-essential areas? In what areas can you reduce your spending? Is your cash flow positive or negative? In other words, do you earn more than you spend and have money left over, or are you spending more than you make?

In working towards building your wealth, it is recommended that once you've summarized your income and expenses, divide your expenditures into three categories, needs, wants and goals. Knowing the difference between these three will be key to developing a smart budget.

**NEEDS**

Needs are the things that are necessary, required or essential. Like your rent, mortgage, utilities, taxes, groceries and transportation.

**WANTS**

Wants are the things that you'd like but don't necessarily need, like dining out, shopping, or entertainment.

**GOALS**

Goals are your desired financial objectives like paying off debt, putting money into an emergency fund or saving for your retirement.

# HOW TO TAKE CONTROL OF YOUR FINANCES

A solid budget can be the key to better financial health. A budget helps you better manage the money you receive, spend and invest. It will direct your spending to ensure your most important financial goals are achieved. A budget is essential if you:

- Feel like your finances are out of control.
- Have issues with paying off debt.
- Have an upcoming large purchase or life event.
- Have problems saving.
- Feel overwhelmed by financial issues.
- Want to be more efficient with your money.

Budgeting isn't about eliminating the things you want to have, it's about understanding where you're spending your money so you can achieve your goals.

You'll need to identify your financial management goals and incorporate those goals into your budget. Your goals should include both short-term and long-term objectives and may include:

### Short-term goals

- Reducing your expenses.
- Paying off your credit cards.
- Building an emergency fund.
- Saving for a vacation.

### Long-term goals

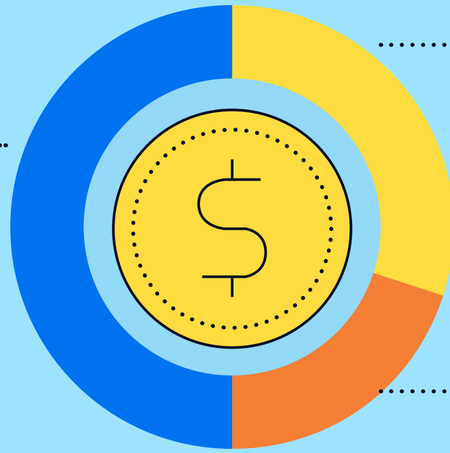
- Purchasing a vacation property.
- Paying off your mortgage.
- Saving for your retirement.
- Being debt-free.
- Funding your children's education.

You may want to consider the 50/30/20 rule, allotting your expenditures into the three categories discussed earlier:

**50%**

**NEEDS**

50 percent of your income goes towards necessities, like your rent or mortgage, utilities, taxes, groceries and transportation.



**30%**

**WANTS**

30 percent of your income should be allocated to wants, which would include items like dining out, shopping or entertainment.

**20%**

**GOALS**

20 percent will then go towards your financial goals, like paying off debt, putting money into an emergency fund or saving for your retirement.

## Steps to take control of your finances

### 1 Establish spending targets

From the information you summarized in your cash flow analysis, set target expense amounts for next month for each budget category. You will need realistic targets that reduce spending in particular categories and increasing investment in others.

### 2 Track actual spending

The next step is to keep track of your actual expenditures during your chosen time frame.

### 3 Compare the results

Evaluating your debts and interest rates and restructuring your debt will be essential.

### 4 Repeat

Make the necessary adjustments and repeat for the following month.

Many expenses such as large repairs, a vacation and annual property tax payments do not occur monthly. As a result, working toward building an annual budget can give you a more realistic forecast.

# TRACKING YOUR FINANCIAL PROGRESS

## Create a new worth statement

As you establish the foundation for your financial success, you'll want to track your progress. Creating a net worth statement is essential. Your net worth is the difference between total assets and total liabilities. Assets are things of value you own, while liabilities are debts you owe.

**Net worth = Assets - Liabilities**

**Calculating your net worth** once gives you a snapshot of your current financial position, but ongoing net worth calculations can show you if you're moving in the right direction. Many of us have a Fitbit or Apple Watch tracking everything from the number of steps we take to the hours of sleep we get. Your net worth statement is simply a tracker for your financial health. You should update your net worth at least annually. This will allow you to see the progress you are making in building your wealth and to be confident knowing you are moving in the right direction.

Preferably, you'll want your net worth to be positive, meaning you own more than you owe and have developed some wealth. If you have a negative net worth this means that you owe more than you own. It's not uncommon to start out with a negative net worth, especially if you have borrowed for a house, your education, or a car. But don't be discouraged, this is just your starting point.

If you have a net worth that is decreasing over time, this may be a warning sign that you need to start decreasing your debt levels and start investing in wealth producing assets. As your debts decrease over time, your assets grow in value, and you acquire more investments, your net worth should become positive and continue to increase.

# STRATEGIES FOR SUCCESSFUL FINANCIAL MANAGEMENT

Although the process of building your wealth may sound daunting, there are strategies you can implement to make the achievement of your financial management goals easier. Every dollar you spend limits your ability to apply funds to your other financial goals.

## Forced savings

A significant amount of discipline is required to save money for the future rather than spend it for today. Having savings taken care of automatically takes away that need for self-control. A pre-authorized contribution (PAC) is a recurring automatic withdrawal that transfers a pre-specified amount of money from your bank account to the investment account of your choice. As a result, establishing a monthly or bi-weekly PAC ensures your savings goals are being implemented. Also ensure you are taking advantage of any automatic payroll deductions for contributions to employer retirement plans or other savings programs.

## Establishing an emergency fund

Although establishing an emergency fund is often one of the goals of financial management, having an emergency fund is also a strategy for effective financial management. Having an emergency fund ensures you do not have to access high-interest debt in the event of an emergency. It is recommended that you have access to an amount equal to at least three months worth of take home pay. It should be maintained in a readily accessible form in a high interest savings account, money market fund or other short-term liquid security paying a competitive rate of interest. Alternatively, if you are disciplined to manage it properly, a low-interest line of credit could be used.

## Controlling your expenses

This may sound obvious but knowing the difference between needs, wants and goals should help you establish financial priorities and limit unnecessary spending. You may need to defer the purchase of a new vehicle, a vacation or other spending that does not contribute to building your wealth. Consider leaving your credit cards at home to reduce the possibility of impulse buying. Also consider deleting food delivery or online shopping apps to limit your access to online spending.

## Use credit wisely

Credit can be used to help you realize a significant goal. This may include purchasing a home or obtaining an education. Credit that is used to acquire an asset with growth potential or to increase your long-term earning capability is generally considered better debt. In contrast, utilizing debt for consumer purchases may be detrimental to your long-term financial plans.

## Debt restructuring

If existing debt is inhibiting your cash flow, restructuring your debt may enable you to move towards achieving your other financial planning goals. Some debt restructuring techniques include:

- Prioritize paying down the debt with the highest interest rate first before paying lower interest rate debt.
- Consider consolidating credit card debt into a personal line of credit or home equity loan to take advantage of lower interest rates.
- Weigh the pros and cons of leasing a car vs. buying. Your own specific circumstances and the terms of the lease will determine if leasing is a beneficial strategy.

## Being thoughtful about the assets you plan to purchase and evaluating those you currently own

If you are having cash flow problems you may wish to rethink ownership in:

- Discretionary assets such as luxury or recreational vehicles.
- Non-income producing investments that only offer capital appreciation, such as coins, art, jewelry, antiques or undeveloped land. Even though these assets may be considered good investments as a result of their potential for growth, they may not be the best choice if you are having issues with cash flow.

That being said, you should not be liquidating assets for the sole purpose of creating cash flow. This decision should be part of your bigger financial planning picture.

## Increasing your income

Increasing your income is another option for improving cash flow. Whether it's considering additional or alternative sources of employment income or choosing to invest in higher yielding investments that are appropriate for your risk tolerance and time horizon, increasing the income that comes in each month will increase your ability to meet your financial management goals.

Developing your financial management skills and having a strong financial foundation is key to achieving your other financial and lifestyle goals. While it might seem like there are a lot of moving parts, working with an ATB Wealth Advisor can help you maximize your cash flow and ensure you are on the right path to achieving your goals.