

Personal Financial Budgeting (Budgeting)

By:

Charles Danso, Ph.D.

Assistant Professor of Finance

CSU, Los Angeles

Agenda

- Beginning Survey
- Presentation
- Ending Survey
- Questions & Answers (Q&A)

Please complete the questions

The link is in the chat

Outline of Presentation

- Anonymous Polls
- Importance of Budgeting
- Wealth Building Equations
- Budgeting Approaches
- Quick overview of Financial Documents

Budgeting Polls

- Please complete these polls questions related to the presentation

Importance of budgeting: Giving Context

- A budget details a spending plan of income
 - This allows one to track spending and adjust accordingly to fit their goals.
- How many people will be able cover a cash emergency of \$400 without taking on debt or selling something. See [Link](#).
 - There were two studies with different results. One found about 40% saying they could not.
 - However, another study found that less than 20% did not have \$400 in bank accounts.
 - Debt obligations was a reason for the discrepancy. Please read article for explanation

Takeaway:

- Individuals should strive to have some emergency fund they can cover without using debt (where possible).
 - Tracking expenses through budgeting can help attain this over time if you can afford to make some changes to spending.
 - The key word is “afford”. I am very aware at some stage that most expenses may be needs. This is where income may not be enough to pay for expenses for some people; I do not want to be insensitive to these situations.

Equation(s) to Wealth Building

- The path to building wealth starts with getting a Positive cash flow (CF)
 - Then channel the CF towards income generating assets.

Some Equations:

- Take home pay (i.e. net income)-fixed expenses = discretionary income
 - [Discretionary income – variable expenses]
 - This will yield surplus (positive CF) or a deficit (negative CF)

Using Excess CF:

- Save/invest the surplus to acquire assets.
- A general goal will be to make assets generate cash flow/increase in value to help you with expenses now or later.

Some Financial Documents

- Personal Income statement
- Statement of Personal Wealth
- Budgeting Sheet

- You can get some Excel templates from this website:

<https://www.vertex42.com/ExcelTemplates/>

Generating more income

- Is pointless if you still spend more
- **“Lifestyle Inflation”** tends to occur with increases in income. See [Article](#) on lifestyle inflation
- So there are behavioral aspect to budgeting that requires being self-disciplined
 - Accountability is key
- However, sometimes you cannot do anything in your situation at that time.
 - It may be important to evaluate what you can do to change that in the long-term.
 - This may include moving to low cost areas, finding additional ways to generate more income, etc.
 - Let’s be honest, everyone can benefit from a high income starting out, but that is not the reality for most people.

Some approaches to Budgeting

- The percentage breakdown (X-Y-Z method)
 - Needs (X)-Wants (Y)-*Financial Future (Z)
 - Example: 50/30/20
 - Example: 70/20/10
- *Financial future can include savings, investments, etc.
- Zero Based Budgeting
 - Goal is to have income minus all expenses (including debts) equal to 0

How I call/group the remaining approaches:

- Fixed versus Variable Expenses
- Categorical
 - where you lump expenses in groups (in bank accounts & apps)

Which Approach is better?

- The **best** approach is what fits best within your goals & personality.
 - See [Link](#) for differences in budgeting across economic classes and over time.

Getting more leftover money (Requires behavior change):

- Percentage breakdown
 - Reduce spending on “wants”
- For Fixed v Variable expense approach
 - Reduce/control spending on variable cost
- For categorical approach (Combines 2 strategies)
 - Modify spending in categories with larger expenses (if they are not needs)
 - Or think of some lifestyle changes if they are needs. For example, do you need a two bedroom in a place like LA by yourself if you could split the room or get a one-bedroom for cheaper?

Using Technology in Budgeting

- Several apps and functions within bank accounts have been created to help with this.
 - Popular apps include Acorns, Qapital, Digit, ClarityMoney
 - Please note that these are not advertisements for them, but to indicate that there is technology to help.

Some Useful Financial Tech Applications

- Albert: <https://albert.com/>
- EARN: <https://about.saverlife.org/>
- Scratch: <https://www.scratch.fi/>

Takeaways

- Budgeting helps to track where income goes
- It can be documented formally or mentally
- Budgeting can help in positively affecting the overall wealth of an individual
- It requires discipline. Income increase does not imply good budgeting ability

Some Popular Books In Personal Finance & Budgeting

- The Art of Exceptional Living by Jim Rohn
- Love Your Life, Not Theirs by Rachel Cruze
- The Total Money Makeover by Dave Ramsey
- Rich Dad Poor Dad by Robert Kiyosaki
- The Millionaire Next Door by Thomas Stanley
- I Will Teach You To Be Rich by Ramit Sethi
- The Compound Effect by Darren Hardy .

Reflection Questions

- Based on presentation, consider these questions:
 - 1) How would you summarize generating wealth using Assets, liabilities, cash flow?
 - 2) How may your income and expenses play into obtaining net wealth and how may budgeting help with that?
 - 3) Does having a higher/increased income, or separately/jointly more assets equate to a positive net wealth? Consider Why or Why not?

QUESTIONS?

Poll Questions

1. I am able to save some money when I get paid.
2. I have bought something I wanted immediately instead of waiting for when price goes down (i.e. sales event).
3. I know of budgeting techniques.
4. In my life now, I consider these a WANT
 - A car
 - Individual living space
 - Traveling
 - Designer clothes
 - Build a stock portfolio
5. In my life now, from the previous list (in q4), I consider these a NEED

Phase 1: Assess Your Current Situation

In this preliminary phase, your main tasks are to:

- Measure your current financial position
- Determine your personal needs, values, and life situation

Phase 2: Plan Your Financial Direction

The actual budgeting activities occur in this phase with:

- Step 1: Set Financial Goals
- Step 2: Estimate Income
- Step 3: Budget an Emergency Fund and Savings
- Step 4: Budget Fixed Expenses
- Step 5: Budget Variable Expenses

Phase 3: Implement Your Budget

As you select and use your budgeting system, this phase involves:

- Step 6: Record Spending Amounts

Phase 4: Evaluate Your Budget Program

The final phase of the process calls for you to:

- Step 7: Review Spending and Saving Patterns

With the completion of the process, possible revisions of financial goals and budget allocations should be considered.

Steps In Creating & Implementing A Budget

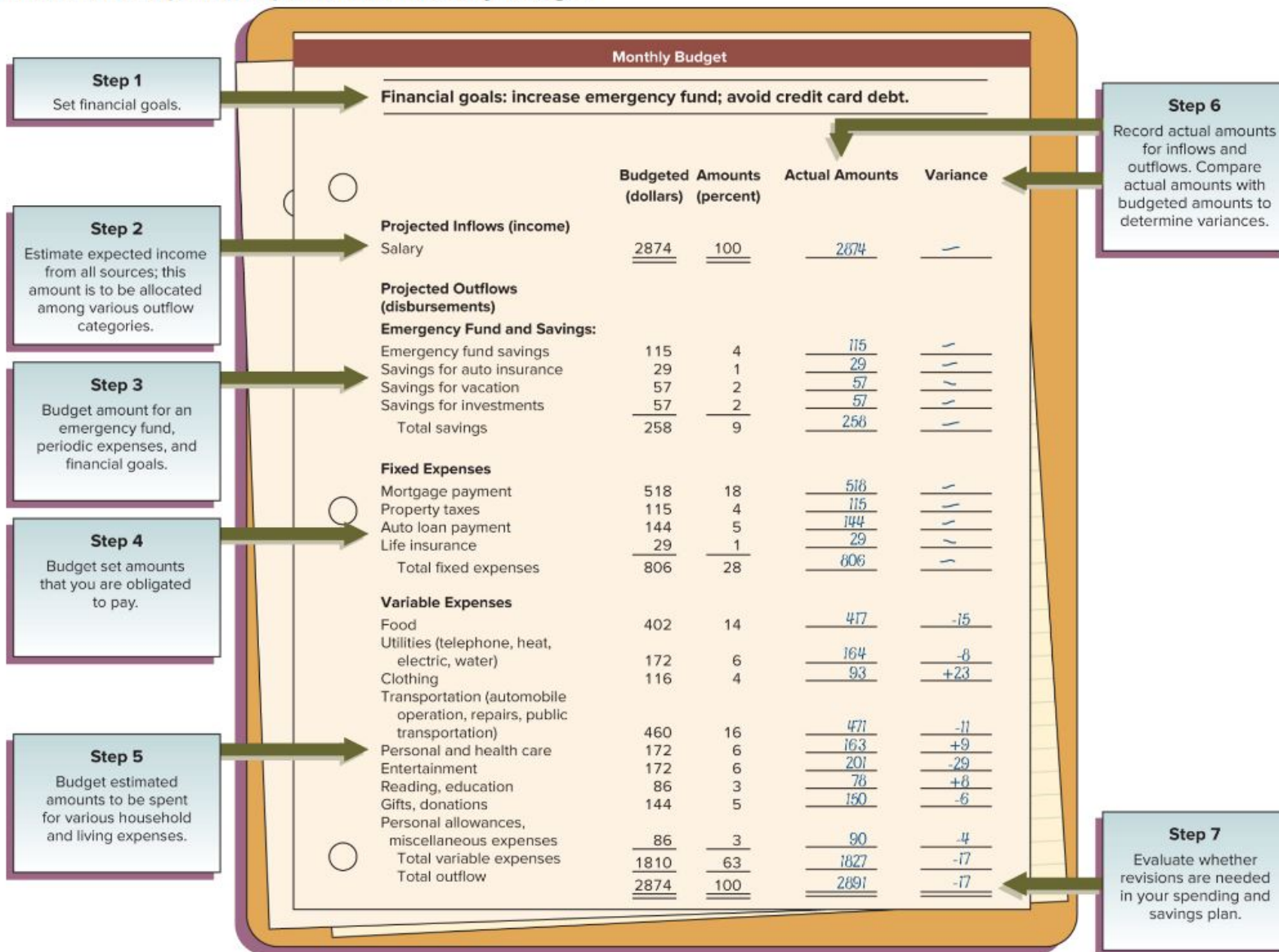
Examples of Common Financial Goals

Exhibit 3-6 Common financial goals

Personal Situation	Short-Term Goals (less than 1 year)	Intermediate Goals (1–5 years)	Long-Term Goals (over 5 years)
Single person	<ul style="list-style-type: none"> • Complete college • Pay off auto loan 	<ul style="list-style-type: none"> • Take a vacation to Europe • Pay off education loan • Attend graduate school 	<ul style="list-style-type: none"> • Buy a vacation home in the mountains • Provide for retirement income
Married couple (no children)	<ul style="list-style-type: none"> • Take an annual vacation • Buy a new car 	<ul style="list-style-type: none"> • Remodel home • Build a stock portfolio 	<ul style="list-style-type: none"> • Buy a retirement home • Provide for retirement income
Single parent (young children)	<ul style="list-style-type: none"> • Increase life insurance • Increase savings 	<ul style="list-style-type: none"> • Increase investments • Buy a new car 	<ul style="list-style-type: none"> • Accumulate a college fund for children • Move to a larger home

Budgeting in Action

Exhibit 3-7 The Fraziers develop and implement a monthly budget



Typical Budget Allocations based on life Cycle

Exhibit 3-8 Typical after-tax budget allocations for different life situations

Budget Category	Student	Working Single (no dependents)	Couple (children under 18)	Single Parent (young children)	Parents (children over 18 in college)	Couple (over 55, no dependent children)
Housing (rent or mortgage payment; utilities; furnishings and appliances)	0–25%	30–35%	25–35%	20–30%	25–30%	25–35%
Transportation	5–10	15–20	15–20	10–18	12–18	10–18
Food (at home and away from home)	15–20	15–25	15–25	13–20	15–20	18–25
Clothing	5–12	5–15	5–10	5–10	4–8	4–8
Personal and health care (including child care)	3–5	3–5	4–10	8–12	4–6	6–12
Entertainment and recreation	5–10	5–10	4–8	4–8	6–10	5–8
Reading and education	10–30	2–4	3–5	3–5	6–12	2–4
Personal insurance and pension payments	0–5	4–8	5–9	5–9	4–7	6–8
Gifts, donations, and contributions	4–6	5–8	3–5	3–5	4–8	3–5
Savings	0–10	4–15	5–10	5–8	2–4	3–5