

Setting Up a Personal or Household Budget

One of the best ways to reduce or avoid money worries is to set up a realistic personal budget. A budget is a tool that will help you understand your income and expenses and achieve your financial goals.

Taking charge of your finances

The first step to managing your money is recognizing that you have some control over your finances. It's easy to blame money problems on things you can't control—that your job pays less than you'd like, taxes are too high, or family members aren't spending money carefully. Those realities may leave little flexibility in your budget. But there is usually *some* room to maneuver, and there are always steps you can take to improve your financial health.

There are two basic steps to gaining control of your personal finances:

1. **Understand where you are now.** How does your money come in and go out? Are you spending more than you earn? Are you saving enough for the future?
2. **Understand where you want to be.** How would you like your money to work for you? What are your financial goals?

Both of these steps will be easier to take if you break them down into small parts that will help you gain control over financial concerns that seem unmanageable.

Understanding where you are now with your money

Gaining control over your money begins with understanding your current situation—how much you earn, spend, have, and owe. To do this, you will need to gather facts about your finances. This may take some work and cooperation from others in your household. But it will give a clearer picture of where you stand that can guide you as you think about choices for change.

The worksheet at the end of this article will help you understand how your money comes in and goes out each month and will let you see your income and expenses. It isn't an official report that needs to be accurate to the penny. "Pretty good" information is better than no information at all if it helps you see what's driving a monthly shortfall or find ways to increase your ability to save.

Monthly income and expenses

Start out by filling in the information you know. Then look at those items you left blank or guessed at without much confidence. You can fill in some of these missing numbers by looking through bills you've paid, including credit card statements, or by sorting through bank statements to find debit charges and canceled cheques. Cash spending will take more effort to track. Spending on seasonal items, too, or those for which your payments vary greatly from

month to month, will take some extra research and calculation to work them into a monthly format.

Tracking cash spending

One way to find out how you spend your cash is to pay careful attention to your spending for two weeks or a month. One week may not be enough to get a full picture, and a longer sample may seem like too much work. Keep receipts for every cash expense during that time period, or note spending on an electronic organizer or pocket-sized pad of paper. At the end of the period, sort the receipts or review your notes and add up how much you spent on lunches, groceries, movies, laundry, gas, and other categories on the worksheet. If you've tracked spending for two weeks, multiply the amounts by 2.16 to get a monthly spending estimate.

Calculating seasonal and occasional expenses

Some bills are due once a year, such as car registration fees; some may be due quarterly, such as property taxes; and some, such as heating bills, may be high in some months and low in others. Other spending—on clothing, car repairs, and gifts—occurs unevenly, with big expenses in some months and few or none in others. For all of these expenses, you will need to find copies of past bills or other spending records and estimate what you would set aside each month if the payments were spread throughout the year.

- **For a quarterly bill**, this is a simple matter of dividing the last payment by three (since the bill covered a three-month period).
- **For bills due just once a year**, divide by 12 to get a monthly average.
- **For seasonal and occasional expenses**, find out what you paid during all of last year by looking through bills, bank statements, and credit card statements, or simply by estimating cash payments. Then divide that annual total by 12.
- **For weekly expenses**, multiply by 4.33 to get an estimate of monthly spending.

Adding it all together

Once you've completed the worksheet, subtract monthly spending from monthly income. This gives you a snapshot of how you're managing your money.

- **If your income is greater than your expenses**, you can start to put aside money each month for savings or focus on paying off debt.
- **If your expenses are greater than your income**, the work you've done in completing the worksheet can help you see what might be causing the shortfall and what changes to income or expenses are possible.

Understanding where you want to be with your money

After finding out *where you are* with your money and your budget, the next step is to understand where you'd like to be.

Short-term adjustments

Depending on what you found out when you looked at your monthly budget, you probably will want to focus on one of three initial goals:

Save money. If you have money left over at the end of the month, you'll want to track your savings and try to increase the amount you put away toward achieving a specific amount of savings to reach your financial goals.

Reduce debt. If you have money left over at the end of the month, consider how you might pay debt down more aggressively using these resources.

Stop deficit spending. If you end up in the red at the end of the month, you may need to cut expenses and/or increase income to have enough left to save or pay off debt.

Using the right-hand column on the budget worksheet, set a budget for the year to come by predicting how much you'll need for each expense. Factor in any increases you expect—a raise at work, a rent increase, or higher property tax rates. And look at where you might trim your expenses. You might:

- Reduce entertainment expenses.
- Use money-saving coupons when grocery shopping. Buy store brands. Buy in bulk.
- Bring your lunches to work/school and reduce other eating out.
- Carpool, ride a bike, or use public transportation.
- Cut back on convenience store purchases.
- Drop premium cable channels.
- Cancel a rarely read magazine subscription.
- Set the thermostat three degrees cooler during the winter.
- Switch to a less expensive phone plan.

Consider small expense reductions in multiple areas rather than cutting things out completely —“all or nothing” planning is unrealistic and a set-up for failure. Every small success can lead to another success. For every dollar cut, plan to channel that dollar into repaying debts or adding to savings. If your employer can deposit part of your paycheque directly into a savings vehicle, take advantage of this to reduce the temptation to spend. Otherwise, put money earmarked for savings into the bank immediately.

Long-term goals

The next step is to ask yourself what your “big-picture” financial goals are. How would you like your money to work for you, now and in the future? Do you hope to retire at age 65 with a comfortable retirement income? Would you like to have savings to cover your expenses for a few months if you ever lose your job or choose to leave? Do you want to buy your own home? Move to a bigger house or apartment or to a different community? Travel? Set aside money for your child's education? Do you simply want to get out of a cycle of ever-increasing debt?

Test those goals by asking yourself whether you're prepared to do whatever it takes to reach them. If you're not, they aren't your most important goals. Pare the list down to the goals that you'd make sacrifices to reach.

Agreeing on goals as a household

If you share financial responsibilities with another person, talk about the future together. Have each member of the household think about his or her financial goals, then compare and discuss them. Find out where you agree and disagree. Talk about your saving and spending patterns and whether you all agree that your choices are helping you reach your most important goals. Aim to come to some agreement about priorities and spending. This may take time, but it's time well spent. A shared budget needs to reflect shared goals in order to succeed.

Test your goals

As you start to gain awareness of your budget and money, continue to test your goals. If you aren't making progress toward a particular goal, ask yourself whether it is still important. And if some people in the household are having trouble staying on track, you need to review your goals together as a group.

Sticking to your budget and reaching your goals

Recognize what you can and can't control. As you draw up a plan to ease your budget problems, it can be helpful to break down expenses into those you can and can't control.

Your monthly rent or mortgage payments, for example, are probably difficult to change, at least in the short term. Refinancing your mortgage or moving to less expensive housing may be options, but both involve time and additional expense.

Your spending on snacks and luxury items, on the other hand, probably is within your control. And it's often the little cash expenses—magazines, take out, coffee, treats for the kids, lunches—that knock the budget out of balance. Being mindful of these small expenses can make a big difference to your budget.

Take charge of credit card spending

Credit-card debt is among the most expensive debt to carry, with interest rates that are often far higher than those available in other types of loans. Even if the APR on a credit card is lower than what's offered on a personal loan, the formula used to calculate credit card interest make the total interest cost much higher. Fortunately, credit card spending is within your control.

Keep your credit cards in a secure place at home and use them carefully. Save them for emergencies and for purchases that require them, such as car rentals and airline tickets. When you pay the balance in full each month, a credit card is a low-cost way to pay for expenses. But as soon as you pay only part of the balance, the card turns into a high-interest money drain. If you have unpaid balances on more than one card, it may make sense to consolidate that debt onto a

single, lower-interest card and plan to pay the balance off. If you need to use a credit card, never use the card with the unpaid balance. Use a second card and be sure to pay the entire balance when due.

Plan for the unexpected

“Budget busters” often arrive in the form of unexpected expenses—the car needs some repair work, the dog has a big vet bill, or a roof leak requires fixing. The best way to plan for these is to set aside some money every month or every paycheck for unplanned expenses. Having an emergency fund is the greatest defense against future debt. To start, set a target amount of savings for emergencies, maybe start with \$1,000. Ultimately, emergency fund savings of 3 to 6 months of monthly expenses is recommended.

Track your progress

Once you’ve agreed on a budget plan, start tracking your progress. Focus on the areas you’re trying hardest to change, such as reducing credit card debt, and measure your progress there. You might keep a record—on an electronic organizer or a pad of paper that fits in your pocket or pocketbook—of how much you spend on “extras”—movies, meals out, or whatever you’ve identified as the source of your budget problems. Or you might put cash in envelopes for different types of expenses and write down whenever you spend more than you’d planned. Every few months you might redo your budget worksheet to see how the entire money plan is taking shape.

Stick with it

As you begin to manage your money on a budget, you’re bound to hit bumps. Do your best to stick with your plan. Uneven progress, even falling behind, doesn’t mean that the plan has failed or that you don’t have the discipline to succeed. If several members of a household are working together toward a budget, it’s unlikely that each of you will meet all your goals each month. The change may be hard to get used to at first, and it’s normal to relax your grip on the budget goals from time to time. Just keep recording your progress and congratulate yourself and each other for the positive steps you do take.

You might find that your goals were too ambitious. When you check in together to record your spending, ask how it’s going. Does the plan seem manageable? Now that you see what it will take, do the goals still seem realistic? Is everyone still willing to make the agreed-on changes and sacrifices? If you’ve reached too far too fast with your plan, adjust it to a more realistic scale.

Keep in mind that your expenses may change unexpectedly, and this will affect your budget. If you’ve filled out your budget worksheet you have the tool you need for figuring out where to make changes in your budget. Change the income or expense numbers to reflect the new situation and work out a new plan. With an awareness of your finances, you can figure out just what the change means for you and adjust your plan before you reach the crisis point.

As you work on your plan, prepare yourself for setbacks along with successes. Be realistic. Be willing to settle for Plan B if Plan A doesn't work out. Celebrate the small successes along the way, and keep your eye on the ultimate goal of regaining control of your finances.

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