10 Basic steps when planning your finances

CASTLEFIELD

THE THOUGHTFUL INVESTOR

1. ‘Rainy day’ money

A sensible first step is to set money aside in cash form, maybe in a deposit account or cash ISA, to give you an immediate buffer to help you cope with the unexpected. Often called an emergency fund or ‘rainy day’ money, having this in place could prove very useful if, for example, you lost your job or you need to replace your car in a hurry. How much to set aside will depend upon your particular circumstances, but as a general rule around 6 months’ worth of your regular expenditure is about right for many people.

2. Check what you spend

Some people love it, some people hate it, but analysing what you spend now and what you may spend in the future can be a powerful way of helping you plan your finances. This can either be a one-off exercise or you could keep a note of what you spend and update it periodically. This will a) help you plan for the future, b) highlight areas where you spend more than you think you do (which, as a consequence, may help you to cut out waste), and c) guide you to what you can and can’t afford to do with your money. We have a template spreadsheet to share with you to make this easier.

3. Personal Protection

Consider putting in place personal protection if a turn for the worse could severely affect your family’s finances. For example, if you have modest savings, a mortgage, and dependent children, would your partner be able to cope financially if you died? Or what if you suffered a critical illness such as a stroke meaning your earning potential was severely impaired but perhaps your ongoing costs increase (say, if you’d have to pay for care)?

4. Save what you can

Putting money aside is essential to help you retire in financial comfort, as well as meet other financial goals such as saving for a house or paying for your children’s education. It’s often not easy to save as there are so many financial demands and pressures in life, but those that find a way, and apply a little discipline, seldom regret it. A generical planning approach is to set aside 10% of what you earn although what is right for you could be to save more or less than this.

5. Set goals

Compartmentalising your money adds a further level of sophistication to your financial planning. Saving into a pension for your retirement is an obvious, specific goal to work towards, but you may benefit from setting and aiming to achieve a number of other goals too. Sometimes these may be interlinked, for example, you may wish to retire early and plan to pay off your mortgage at the same time. This could involve saving a sufficient amount for your retirement but also making over-payments to your mortgage to make this work.

6. Tax

It is fair and reasonable to pay tax and all of us see the benefits of doing so, be it via education, the health service or other publicly available benefits. However, if you plan poorly you can end up paying much more tax than others in similar situations to yourself. Taking simple steps such as paying into ISAs or pensions make sense, although there are a myriad of other reasonable ways to save paying too much tax such as planning the timings of contributions and withdrawals, and taking advantage of other allowances such as your Capital Gains Tax Allowance.

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7. Risk

If you save into something that isn't cash based, such as a stocks and shares ISA, the likelihood is that it will be at risk of losing money and well as making it. And the more you want the chance of it making a high return, the bigger the risk of it making a large loss. Knowing how much or how little risk to take isn't easy and may need professional guidance, but a couple of useful tips are a) can you afford to take the risk, and b) think timescales.

If things don't go to plan and your investment loses money rather than makes it, what is the impact on you? If it's unfortunate but not critical you may be able to take on that risk. On the other hand, if making a loss had dire consequences (for example, you could then no longer pay off a debt you were due to settle) it is probably best avoided.

And try to think short, medium or long term. For a short term goal, for example, saving for a house deposit that you'll need in two years' time, you probably shouldn't take any risk. On the other hand, if you are due to retire in 30 years' time, any losses to your pension plan have plenty of time to recover, and therefore you can most likely afford to take a degree of financial risk.

8. Research

There is endless advice and guidance available online, including this guide! Educating yourself as a first step is to be encouraged, and armed with your new-found knowledge it may be all you need to help you plan. One particular source to consider is the Government's 'Money Advice Service' which offers all sorts of free guides on subjects such as borrowing, budgeting and pensions.

9. Think of others

Planning for yourself and your family is important for us all, but thinking beyond ourselves is also important too. When you invest money, ultimately profits are made by the businesses and organisations that your money becomes invested in, which is then in part returned to you as the returns your investments make. However, how that money is made can have a positive or negative impact on society and the world at large, and ultimately will impact on you and your inheritors; for example investing in businesses that destroy the environment and lead to climate change is likely to be far worse for us in the long term than any short term gain. Think about investing thoughtfully.

Or for many, giving money to charity or other worthy causes within their lifetime or on death is also important. There are various tax-efficient ways to do this and considering how much you can afford to give whilst still keeping yourself financially secure is also something that can be factored into a good financial plan.

10. Seek advice

Financial advice from a qualified professional can be an expensive undertaking and something you need to think carefully about. However, structured, impartial, expert advice can have many benefits which build on many of the steps listed in this guide. A financial adviser can help you tidy your financial affairs, set and achieve certain goals, save tax, manage financial and other risks, be aware of and comply with various legislation and other rules, and ultimately give you peace of mind when it comes to your money.