The Ultimate Beginner's Guide to Financial Planning

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Introduction

Ask most people about the role financial planning plays in their life and they will likely tell you that good financial planning helps pave the way to success. Financial planning not only helps you to reach major goals in your life, but it can also help you stay stress-free as you go through life. Having clarity around your finances is critical. Without clarity, it can be extremely difficult to achieve your goals, have financial security, and live a fulfilling satisfying life. That is because the financial stresses of life can take over and leave you strapped for cash and barely meeting your basic needs.

Having a financial plan can do more than just ensure your basic needs are met, it can:

- help you achieve your financial goals
- prepare you for emergencies
- give you a better understanding of how money works
- improve your standard of living
- provide you with the financial security you and your family need
- secure the financial independence you need in retirement.

Financial planning can help guide you through complicated financial decisions, so you can have less stress, more confidence, and more time to focus on other things. No matter what stage you are in life, financial planning can help you reach your goals and provide financial security for you and your family.

Use the Ultimate Guide to Financial Planning to help you get your financial planning underway.

Section I

Understand Your Current Financial State And Define Your Goals

The first step in financial planning is knowing your current financial situation. This is your financial journey, and it will impact you and everything you do. It's important that you know what you're working with to be able to determine your capabilities and your limits. Ask yourself the following questions: Do I spend more money than I make? What is my credit score? Will I be financially sound in retirement? If you don't have a definite answer to any of those questions, you're in trouble. If you do know the answers and they reflect negatively, you're still in trouble. It's time to understand your current situation, and from there you can set goals for where you're trying to go.

Understand Your Current Financial Situation

Know Your Income

When was the last time you took a good look at the deductions coming out of your paycheck? There are numerous deductions taken from your gross pay (hours multiplied by your hourly wage). That means your take-home pay is less than what you actually earn. While you may be aware of that, be knowledgeable about the type of deductions coming out and why they're coming out. If there are opportunities to lessen the number of deductions in a way that increases the pay you bring home (net pay) and legitimizes your payroll statement, pursue it. Your net pay is the amount of money you receive after deductions are taken.

Standard deductions include federal income tax, state taxes (some states withhold state income taxes), social security, and Medicare. Of the three, federal tax is the one that can change based on your situation. Federal tax is what you pay the federal government and is not only based on your pay but the number of exemptions you claim on your W-4. The W-4 has to be completed by anyone who starts a new job. An exemption is a deduction that allows a certain amount of income to be excluded to avoid or reduce taxation. Exemptions may be for the individual and family members the individual supports.

Other deductions could include retirement contributions, health insurance, life insurance, wage garnishments, etc. Some of these plans require a matching commitment from the employer, others don't. In the end, regardless of what your hourly pay or salary is, you may fall short on what you anticipate bringing home every month because of deductions.

You should review your pay stub every time you get paid to ensure it is correct, that all deductions are accounted for, and no additional ones are added. When it comes to your exemptions, this number could change depending on the number of dependents you have during a tax year. You want to make sure you update this form as needed, as often as needed. It could drastically affect how much is deducted from your pay for taxes.

When it comes to your deductions, make sure you understand each one, and that proper amounts are deducted. Report any discrepancies to your employer immediately. If you have questions, meet with a human resources representative to go over the details of your company's benefits or talk with your employer if your company doesn't have a human resources department.

Know Where Your Money Is Going

Many people do a good job at evaluating their finances when it comes to making a major purchase, like a vehicle, home, or family vacation. It's not only a good idea to evaluate your finances in dire situations when so much depends on it, but all the time, in any situation.

Track your expenses by reviewing your checkbook register, store receipts, and billing statements to see where your money is going. Hold on to all your receipts until you've accounted for how all of your money was spent during the month. Include fixed expenses (rent, auto, student loans, etc.) that must be paid each month. Also include discretionary expenses (food, clothing, entertainment, etc.) that can change from month to month.

When you know where your hard-earned money is already going, it makes it that much easier to determine where you may need to cut back.

Know Your Credit Worthiness

A credit report is a collection of information about you and your credit history and will have a significant impact on your financial future, and ultimately your goals. For instance, if you have a poor credit score, you may not be allowed the credit you'll need to buy that home, boat, or dream vehicle. On the other hand, if you have a good or near excellent credit score, you can have access to almost anything. Your credit score determines your creditworthiness. A low credit score will tell lenders they cannot trust you to pay back what they loan you, but a good credit score says the opposite.

Your credit score impacts your future with so many lenders: landlords, potential and current employers, government licensing agencies, insurance underwriters, etc. Be sure to get a free copy of your credit report from any of the three major credit reporting agencies: Equifax – www.equifax.com; TransUnion – www.transunion.com; Experian – www.experian.com or download a credit app to your phone so you can always know your credit worthiness.

Your credit score is impacted by the following things: how promptly you pay your bills; how many credit cards you hold, the total amount of credit that has been extended to you; how much is owed on all your outstanding accounts.

The most commonly used credit score is the FICO score provided by Fair Isaac Corporation. This score is based only on credit information (personal factors are not considered). FICO scores consider five components of the credit history weighting some higher than others:

- Payment history – 35%
- Debt owed – 30%
- Length of credit history – 15%
- New credit – 10%
- Types of credit used – 10%

Know Your Credit Worthiness

FICO scores range from a low of 300 to a maximum of 850. If you're in the middle, you're average. You want to be always above average, seeking a credit score of 700 or better. If you find that you have a low credit score, focus on making it better. Here are some ways you can do that:

- Pay your bills on time.
- Do not put yourself in further debt. Do not apply for any more loans.
- Pay more than the minimum on all credit cards.
- Only use a credit card for emergencies. If it's not an emergency and you cannot pay with cash, reconsider making the purchase.

Define Your Goals

One of the reasons financial planning is so important is that it helps you achieve your financial goals. Goals are what give us direction in life. When you have clear goals in mind and on paper, you feel more geared to work towards them. Now is the time to start focusing on your financial goals.

Financial goals are important for people to have when it comes to having a stable and enjoyable life. Personal finances are an intimate part of every person's life because money is often a medium to help people achieve their most cherished life goals. It's particularly important to balance short-term and long-term goals with your finances.

Here are a few recommendations for setting and achieving solid financial goals:

- Personalize your goals: Your goals should be geared towards the life you want for yourself.
- Align your goals with your values: When goals are aligned with your values it creates a much stronger motivation to accomplish them. When you have a strong enough "why" behind the goals you are seeking to accomplish, you will find a way to make the goal happen.
- Set SMART Goals: Make sure your goals are reasonable for what you'd like to do. SMART goals are specific goals that are measurable, achievable, relevant, and timely.
- Visualize your goals: The act of visualizing your goals before they happen is a powerful technique to help you gain momentum toward achieving them. Visualize your financial goals every day to make them a reality.
- Review your goals often: Review your goals often so you will always remember what it is you're trying to achieve. Also, in reviewing your goals you may see a need to make changes along the way. Life happens and things change that may cause us to have to modify some of the original goals.

Set Short-Term and Long-Term Goals

Financial planning is an ongoing thing. For as long as we live, we will need to be managing and planning for what's to come. Needless to say, some goals are farther in the future, but some are not so far away; some are right around the corner. When determining your goals, it's important to distinguish your short-term goals from your long-term goals. Short term goals are goals that will be achieved anywhere between the next three to five years. Long-term goals are goals beyond five years. Knowing a reasonable time frame for when you want to achieve a goal, helps direct your financial planning and makes achieving the goal more feasible. Ensure you have SMART goals. SMART is an acronym used to describe goals that are specific, measurable, achievable, relevant and time bound.

Specific: Your goal should be clear and specific, otherwise you won't be able to focus your efforts or feel truly motivated to achieve it. When drafting your goal, try to answer the five "W" questions:

- What do I want to accomplish?
- Why is this goal important?
- Who is involved?
- Where is it located?
- Which resources or limits are involved?

Measurable: It's important to have measurable goals, so you can track your progress and stay motivated. This will also help you stay focused, meet your deadlines, and feel the excitement of getting closer to achieving your goal. A measurable goal should address questions such as:

- How much?
- How many?
- How will I know when it is accomplished?

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Achievable: Your goal needs to be realistic and attainable to be successful. It should stretch your abilities but still remain possible. When you set an achievable goal, you may be able to identify previously overlooked opportunities or resources that can bring you closer to it.

An achievable goal will usually answer questions like:

- How can I accomplish this goal?
- How realistic is the goal, based on other constraints, such as financial factors?

Relevant: Relevance ensures that your goal matters to you, and that it also aligns with other relevant goals. A relevant goal can answer "yes" to these questions:

- Does this seem worthwhile?
- Is this the right time?
- Does this match my other efforts/needs?
- Am I the right person to reach this goal?
- Is it applicable in the current socio-economic environment?

Time-bound: Every goal needs a target date, so that you have a deadline to focus on and something to work toward. This part of the SMART goal criteria helps to prevent everyday tasks from taking priority over your longer-term goals. A time-bound goal will usually answer these questions:

- When?
- What can I do six months from now?
- What can I do six weeks from now?
- What can I do today?

Deciding Your Goals

If you're not sure how to decide your goals, here's a suggestion. Create a bucket list of things you desire. It doesn't have to be a specific number; it doesn't have to be specific things. Your bucket list consists of things that are meaningful to you that you would like to accomplish, based on the goal-setting tips described above.

Once you write your list, start converting those dreams into financial goals by making them specific and measurable with a date, and put a price on it like, how much it will take to accomplish that goal. After that, you can determine what you need to save to achieve your goals. For example, if you have a trip to Egypt on your list, your written financial goals can describe when you'd like to take that trip and through research you can determine how much it will cost. Once you know that, you can decide how much you will need to save yearly to take that trip.

Your goals can be viewed as flexible documents, meaning they are subject to change as needed. They'll change with time as your interests and life situation change. It's even safe to say that it may not seem that all your goals have a price attached to them. Some may be ambitions related to improving your health, relationships, community service, etc. But, even if you're trying to live healthier, that could require a gym membership, which involves money. Building relationships could mean spending more time with the people you love, which could mean spending money to go out more often. Community service activities could even have you coming out of pocket more to pay for gas to get there or to just give more. Many life goals have a financial foundation of some sort, whether it is saving, spending, or donating money.

Lastly, make sure to prioritize your goals in order of importance. Write down your financial goals, prioritize them, take action to achieve them, and review and revise them periodically as you develop spending plans (budgets) for the months ahead. Make financial goal-setting part of the budgeting process. If you know what you want to achieve and treat savings for financial goals as a fixed "expense," you'll be more likely to achieve success.

Create a Budget

A budget is a line-item accounting of all your income and expenses. The purpose of a budget is to see all your money in front of you in one place. Your budget will help you to stay on track as you're working to achieve your financial goals.

You've already accounted for your income to know how much money you're bringing into the home. You've tracked your expenses to know where your money is going. Those are the first steps to creating a budget. Your budget should include all your income sources, like child support, side hustles, investment accounts, etc., as well as every single expense.

How to Use Your Budget

You could go about using your budget in a couple of different ways. You can categorize your discretionary expenses and put a figure to each category. Since discretionary spending is not fixed, you have the ability to control your spending in these categories.

Another way to use your budget is to apply the 50/30/20 budgeting framework. With this approach, the goal is to spend 50% of your after-tax income on essential costs (e.g., rent/mortgage, food, car payments) and 30% on other needed expenses (phone, streaming, etc.) or “nice to haves” such as dining out. The final 20% is for savings: building your emergency reserves, putting away money for retirement and saving up enough funds for that next big thing you have already included in your goals.

In the end, it’s your budget. You can use it in the way that best helps you stay on track for your goals, even if that means playing around with the percentages in the budgeting framework.

Section III

Manage Your Debt

We all have a certain amount of debt. Many people would even say that debt is unavoidable. Although it may be unavoidable, it always needs to be managed, regardless of how big or small our debt is. That said, we don’t want to have more debt that we’re financially able to handle. So before agreeing to any loans or credit cards in the future, here are some helpful tips to consider.

Managing Loans

With any loan, you should consider several factors, including the interest rate, additional fees, and down payment. The interest rate is the amount you are charged to borrow money. When money is borrowed, you must repay the principal (the dollar amount you borrow), and the interest that accrues during the life of the loan. The higher the interest rate, the more you will pay. Interest rates may be fixed or variable. Fixed interest rates will remain the same throughout the term of the loan. Variable interest rates will periodically adjust as a result of current market conditions.

Some loans may require additional fees, like closing costs, auto insurance or warranties. Before agreeing to a loan, make sure you understand the payment requirements and all fees associated with the loan. It is important to know exactly how much you will be expected to pay.

Down payments are large payment amounts paid toward your purchase. Down payments minimize the amount you have to borrow. The more money paid up front toward the purchase, the more money you will save over the life of the loan. For most large purchases, it is recommended that you pay at least 20% for a down payment. Your monthly payment must fit into your budget. The new monthly payment must not cause your expenses to exceed your income, and thus ruin your budget.

Here are some additional guidelines to help you determine whether or not to borrow money:

- Housing expenses should not exceed 33 percent of your gross income.
- Many lending institutions look at this factor in determining your loan eligibility. Percentages may vary slightly between lenders.
- Loan installment payments, which include auto and student loans, credit cards, etc. should not exceed a combined total of 20 percent of your gross income.
- Remember to save money and have at least 6–12 months of emergency savings.

Managing Credit Cards

It is easy to get a credit card, but managing it isn't always as easy. Here are some helpful tips to better manage them:

- Credit cards are borrowed money. You must repay them, so don't spend more than you can afford to pay in full.
- If you do not pay your balance in full each month, interest will accrue and will be added to the total amount you owe.
- Careful use of your credit card will assist you in establishing a solid credit rating. Poor use of your credit card can rapidly place you into debt.

- Choose wisely. When selecting a credit card, make certain you have selected one with the most affordable options and no hidden costs. When selecting a credit card, look for the following:
    - o A low annual percentage rate (APR). The lower the rate, the less interest you have to pay.
    - o Annual fees or any fees should not be charged. If the issuer charges an annual fee, ask them to waive it or do not accept the credit card.
    - o Late payment fees, transaction fees, over the limit fees, etc., will increase the total cost of your charges.
    - o A grace period is often provided if you agree to pay off your balance before interest charges begin to accrue. Other credit cards may charge interest from the day the charges appear on the account.
    - o Various services and features, such as cash rebates, frequent flier miles, extended warranties, etc., may have hidden future costs. Think carefully about the true cost of these programs.

Limit your number of credit cards. Having only a few (or one) credit cards will make it easier to manage your spending and prevent overspending. You will need to make a payment for each credit card with a balance, preferably to pay the balance in full each month.

Don't always carry your cards with you. Having a credit card can give you easy access to money you would not typically have. If you leave the card at home, you may think twice before using it to buy items you don't really need.

Section IV

Create a Savings Plan

It is always a good idea to save money. Established savings accounts are the best tools to have when dealing with unexpected or unplanned financial situations. For this reason, you should consider having at least two different savings accounts: one for personal savings and one for emergency spending. Your emergency spending account should have enough in it to cover six to 12 months of your monthly expenses. Depositing money into your savings accounts should take priority over any additional spending.

Here are some ways to make saving a little easier:

- As you pay your monthly bills, set money aside to deposit into your savings.
- Set up an automatic bank draft for every time you get paid that will transfer money into your savings accounts.

Section V

Investment Strategy

A savings account with compounding interest will help your account balance grow even farther. The interest that you earn on your savings account is added to the total balance of your account, which will result in more money earned.

Investing is a great way to have your money work for you but comes with risk. Before you start investing, it is important to understand the different options and the risks involved. Different investment options offer different rates of return. Generally, the higher the rate of return the higher the chance of losing your investment. The lower the rate of return, the lower the chance of losing your investment dollars.

Some of the different types of investment options are:

- **Money Market:** Money market accounts might earn a higher interest rate than a traditional savings account but usually have a minimum balance requirement.
- **Certificate of Deposits (CDs):** Your money is placed in a CD for a fixed period of time and has a fixed interest rate.
- **Stock:** When you purchase stocks, it gives you part ownership in a company and your growth potential changes with the stock market.
- **Bonds:** Bonds are a promise to repay from money loaned to a government or company, at a fixed rate of interest due on a specific date.
- **Mutual Funds:** Mutual funds are an investment in a professional managed fund that includes a combination of stocks and bonds with various risk factors.
- **Retirement:** Many different options exist to invest for retirement. Many employers offer a 401k, 403b, etc., and may even match your contributions. Take advantage of a contribution match any current or future employer provides. This match is provided as part of your compensation package and will help you meet your investment goals. You can also purchase an annuity that you have for a period so that it can pay you income, potentially, for the remainder of your life.

Prepare for Retirement

Even if you're nowhere near retirement, it's still time to start preparing for retirement. Saving for retirement is a lot easier when you start as early as possible. There's no one rule for how much you'll need to save for retirement, but a solid guideline is to have a multiple of your salary set aside at different ages. For example:

- In your 20s: Start saving at least 10% of your gross salary ASAP. If your place of employment has a retirement plan, opt in now. If they don't, open an IRA.
- In your 30s: Start contributing 15% of your gross salary.
- In your 40s: The recommendation is to have two to three times your annual salary saved in retirement funds.
- In your 50s: The recommendation is to have six to seven times your salary saved.
- In your 60s: The recommendation is to have eight to ten times your salary saved.

The best way to save for retirement is to use special accounts that give you valuable tax breaks. Take advantage of workplaces that offer retirement accounts (401(k)/403(b), etc.) or open your own account through an Individual Retirement Account (IRA).

There are lots of moving pieces to nail saving for retirement, but here's one thing for sure, the earlier you start, the more comfortable you'll be in retirement.

Financial Planning Consultation

At TCG Advisors, a HUB International company, we're structured to provide comprehensive, customized advice. We'll partner with our in-house specialists in taxes, estate planning and investing to build a tailor-made plan that's optimized for you. We'll look at every detail of your wealth to help ensure your complete financial picture is working as hard as it can for you, every day, year in and year out.

The first step is a brief conversation about how we can support your wealth management needs.

Find An Advisor