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THE BUSINESS OF ARCHITECTURE

WORKSHOP 8: LIFE MANAGEMENT – FINANCIAL HEALTH & WELL-BEING

INTRODUCTION

This is a very personal subject, and one that needs to be dealt with in a very sensitive and mindful manner.

Many years ago, chatting to a friend who owned and ran a factory, he told me that nearly 70 % of his labour force had a garnishee order on their salaries. A garnishee order, which is also known as an emoluments attachment order, is a court order, served by the sheriff of the court, that instructs an employer to deduct money from an employee's salary or wages to pay off and settle the debt owed.

The conversation revealed a vast chasm in our education, starting from our earliest schooling and remaining unfulfilled even until to the completion of our tertiary studies; namely, how to manage money.

WHY ME?

I am not a financial or investment guru. As in my previous workshops, my advice will be largely anecdotal and based on my personal experience. I will provide whatever templates and documentation I can that may help you to lower yourself gently and easily into the dull abyss. There will be themes and topics that I have covered or alluded to in previous workshops. In this workshop I will embellish on them with an emphasis, not on their impact upon our business or our practice, but their impact upon the financial wellbeing and security of our lives and our families.

THE PRIMARY GOALS OF FINANCIAL MANAGEMENT

BACKGROUND

It needs to be pointed out that this is a workshop on Personal Finance, it is not a workshop on how to get rich quickly or on how to find the most lucrative investments. This workshop is about managing the money we *do* have wisely. It seeks to share some skills and wisdom that will empower us and enable us to manage our money in a sustainable and profitable manner.

"Do not save what is left after spending, but spend what is left after saving." – Warren Buffett

The fundamental principles of successful money management were well understood and carefully detailed over 6 000 years ago in ancient Babylon. They were uncovered by archaeologists and captured in a small book written in 1926; *George S. Clason*'s "The Richest Man in Babylon". Although the complexity of interest, insurance and taxation has grown over the millennia, the foundations of fiscal prudence remain unchanged. I wish to provide the means to apply these well-founded concepts of how we manage our money in a direct and pragmatic way.

3.8 Financial Health & Wellbeing

The only major addition to the subject of personal finance is the spending and budgetary pie chart. All subsequent books and tutorials about personal finances are just a rehash of these rules or a more detailed investigation of one or some of them. I have provided a budget template that overlaps the main principals of these objectives and automatically built them directly into the DNA of my spreadsheet.

Overview

The 3 primary goals of financial management are:

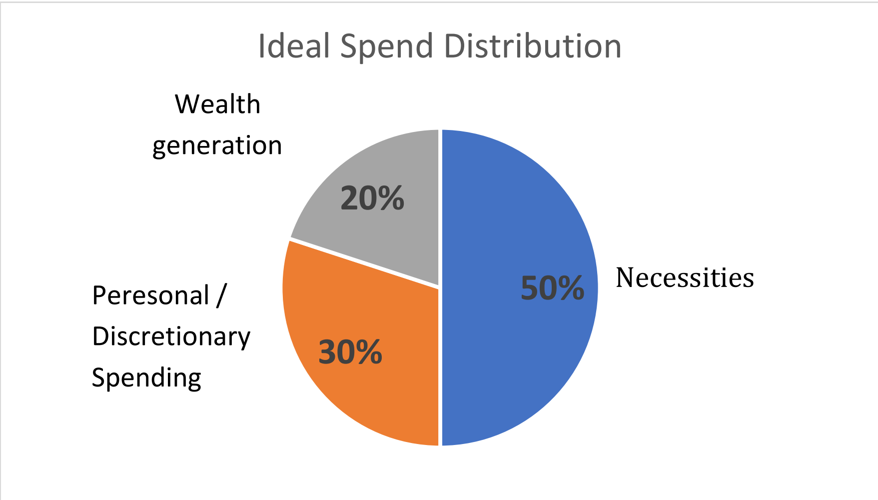
- Pay ourselves.
- Increase our ability to earn.
- Manage our spend.

The generally accepted IDEAL distribution for spend planning is as follows-

50% - Necessities: 'Needs' e.g. home rentals/bond repayments, food, transport, non-investment debt repayments, retirement/pension, war chest savings, school fees, etc.

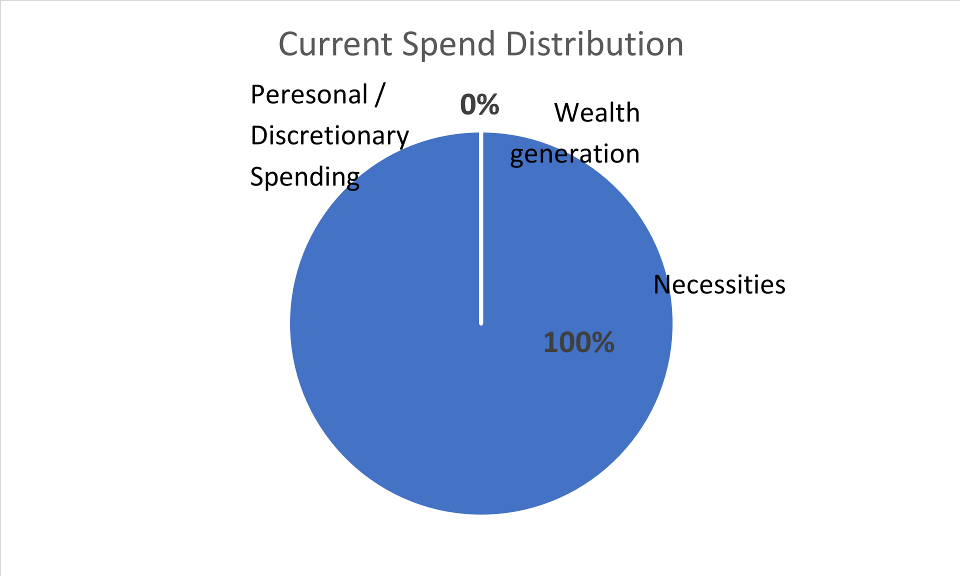
30% - Personal and or discretionary Spending: 'Wants', e.g. future projects, weddings, funerals, family holidays, etc

20% - Wealth Generation: 'Ideals', e.g. investing so our money can grow by itself



However, for a lot of us our pie chart may presently look like this:

- 100% Necessities made up of non-investment debt
- 0% Personal /Discretionary Spending
- 0% Wealth generation



Once we populate the template of our budget (attached), we will be able to see graphically how far along the transition our present situation is. My objective for this course is provide some tools so that we can take control of our finances and begin the journey from our current position to the ideal position.

OUR BUDGET

Why a Budget?

It needs to be said right up front, this is in fact not a 'Budget' in the semantically correct sense of the word. Companies use Budgets as forecasts and then compare their performance against their 'budgeted' forecast. A 'Household Budget' is more of a collation of historical data to make us aware of patterns in our income and spending. We can then use that data to manage and modify future behaviour accordingly. The use of the word 'Budget' in the context of this workshop refers to the collation of that data.

As the 'Time Sheet' is the fundamental tool of the 'Cost of Sales' exercise for the effective management and running of any business, so is the Household Budget the fundamental tool for the effective management and smooth running of our personal finances.

Generally, people are terrified by money. Money gives rise to enormous anxiety and even dread. Sometimes people will borrow and save at the same time, having no clear plan and making decisions without a holistic and coordinated understanding of their financial situation.

The primary purpose of a comprehensive and accurate monthly budget is to create an unambiguous 'map' of our income and expenditure from which we can make better and well-informed financial decisions. Our Budget is the single most powerful tool in achieving financial security and even financial success.

Drafting a Budget

Traditionally, financial budgets are based on The Income Statement format where Turnover is our top line and as one progresses down the document, so the expenses etc. are subtracted, ultimately reaching the last or 'Bottom Line', the profit or loss value of our enterprise.

My template looks and works differently. This is not how our financial advisor would set out our budget, but I do have specific reasons why I use this layout.

3.8 Financial Health & Wellbeing

The Excel template provides us with a broad range of the monthly income, costs and expenses we can typically expect. I have tried to provide a broad-ranging budget suitable for a simple family budget up to a template to accommodate for more vehicles, properties, and investments. Choose the one that closet fits your requirement.

Populating our Budget

To generate a budget can initially be a tedious task, the logical organization of our accounts can be confusing. The quickest and simplest way to capture our income and spending is to simply take a recent monthly payslip and a recent bank statement and begin to populate the fields on the spreadsheet with the information taken directly from those two sources.

It is essential to be completely candid and accurate with our allocations; manipulated data simply undermines the entire point of the exercise. Our un-documented red wine expenditure may well come back to haunt us!

Once one month's expenditure and income has been captured, go back through the previous 12 months bank statements if they are available and make sure all those ad hoc items; gifts, licences (TV), once a year app payments, etc have been incorporated. These too need to be included in the budget for specific months, divided by 12 to make provision for those that are annual renewals.

INCOME

Like a traditional 'Income Sheet', income is at the top and the general expenses, deductions etc are below. However, I place the expenses relating directly to an income stream adjacent to the income values so that I can readily see the final, inclusive and real value of that income stream without having to hunt further down the spreadsheet to locate all the costs associated with it and then manually deduct them. The true return of the investment can be seen immediately.

The start of the spreadsheet makes provision for the various income streams the family may have available. Be it two salaries, a business, a property investment and dividends paid out on stocks and shares.

Salaries

The PAYE and other deductions must be subtracted from the gross income immediately so the income brought forward represents what is available to the budget.

Provision for the deduction of Retirement Annuities and Pension can be excluded here if they are paid for by the Employer, or in a later section if they are privately managed policies.

Our Business

If we run our own business, only include the salary / dividend / loan repayment paid to us by the business. The expenses associated with this business will form part of the business' books and must be handled by our bookkeeper/ financial consultant. Remember, our business is a separate financial entity.

Properties:

Our Home

The initial example shows a primary residence that includes a work from home office. It therefore shows an income Expenses relating to that particular property are itemized against income to give a final and inclusive cost.

Investment Properties

As above, income and expenses have been shown adjacent to one another for an investment property, should we have one. Allowance is made for renting agent and maintenance costs converted to an average monthly cost. Should the property become vacant, then for that month on our Budget we would show zero income. A vacancy factor is built into the spreadsheet since it is a reality of property ownership, it would be remiss not to make some provision for such an occurrence.

The budget also makes provision for the details of the bond and the growing equity. This is just to help maintain an awareness of the status of the bond. Each time we receive a bond statement or notice of change in the bond repayment costs (a change in the interest rate), we can update these details accordingly.

Investments:

Should we hold a portfolio of stocks or shares that yield an annual or monthly dividend, a table is provided to quantify their value, yield and equity (that should be regularly updated).

EXPENSES

Our budget and therefore this template, seeks to encompass all typical costs that we can expect in our daily lives, including debts, loans, savings and provision for retirement.

Data Groups

The information is deliberately grouped into specific sections. This data will be collated into visuals on the 'dashboard' to provide a clear comparative indication of the performance of our budget against the 'ideal' pie chart shown earlier in the notes. This forms the fundamental objective of this workshop.

With this information we can scrutinize our spending habits and develop strategies to best improve our financial management.

Estimated Monthly Costs

The fields that need to be filled are coloured blue, please populate those with data. Sometimes this data will be approximate for sums that will perhaps not be the same for each month, such as our electricity account or how much we spent on eating out. These fields can be populated with a reasonable monthly average.

Some of the fields are not to be filled out – these are uncoloured and they will populate themselves as part of the calculation process.

Schedules

Where debts and loans are itemized on the spreadsheet, a schedule has been provided alongside the item that will allow us to include additional information. The purpose of these schedules is to provide us with a real-time status as to the progress of that loan payment, permitting us to make time allocations for the settlement of that particular loan, and then apply long term planning to our cash flow thereafter. Additionally, provision has been made to capture Provider details, and renewal dates for service and products as required.

Equity Calculator

I have provided the opportunity to continuously keep track of the financial equity value of our large assets. For the purposes of the budget, equity is the difference in value between what we owe on properties, and what the market value of that property is i.e. Equity = Asset value - Liability value. It is only a rough guide as property market values are presently extremely volatile.

Motor vehicles provide no real equity as they tend to remain a liability. I will cover this in a dedicated section.

Equity includes the value of stocks you own, based on an averaged market value.

Savings, Emergency Fund and Debt Rehabilitation

Built into the spreadsheet is automatic provision for the set-aside of monthly savings, and for a structured rehabilitation of debt. This is the manifestation of the goals of financial management, the creation of a sustainable financial plan.

IMPLEMENTING THE PLAN

Now we have the data well captured and clearly presented, we can go about applying strategies to achieve financial peace of mind.

MANAGE OUR EXPENDITURE RIGOROUSLY:

Create a spend strategy, the Spending Rule of Thumb:

As mentioned in the introduction, and illustrated in the pie-charts, ideally, the generally accepted distribution for spend planning is as follows-

<u>50 % - Necessities</u>

Essential costs or 'Needs' such as home rental or bond payments, food, insurance, transport costs, non-investment loans (existing debt repayments beside home loan), retirement / pension funds, school fees and funds set aside to create a 3-month 'war-chest'.

<u>30 % - Personal and discretionary spending:</u>

Non-essential spending and covers the costs of our 'Wants'. Do not confuse necessary expenditure with desires. Provision can be made for setting aside savings for holidays and other large expenses (a wedding, buying a caravan), also known as the 'big bill prevention rule'. We set aside savings for future projects in order to avoid using credit and its associated costs. The spending of previous years can be analysed to make proper planning for these projects (family holiday). It is also the place where most adjustments can be made to manage our expenditure.

<u>20 % - Wealth Generation:</u>

Money spent on investments with the direct intention of those investments being used to generate money for us to invest further. This is not be confused with saving for a particular item, project or event!

Expenditure: Necessities

I wish to discuss the major features of this type of expenditure prioritizing them in terms of their size and impact on our budget. Most of these expenses are non-negotiable, and so we need to administer them with care and diligence. We can make large improvements to our budgets by applying careful scrutiny to how we choose to spend this money.

3.8 Financial Health & Wellbeing

Your Home:

To Rent or Buy?

There will always be a compelling logic to rather be paying our own bond on a property that we own ourselves, rather than paying rent to a third party who will use that income to pay off their own bond. The main driving forces for renting are as follows:

Commitment – getting a firm grasp on life's larger questions; do I want to settle in this area, this city, this country? Am I going to start a family, need schools, be near to my own family? Will my career path carry me elsewhere? It takes some time for some of these options to bed down.

Access to credit – it takes a while as a young earner to achieve the criteria the banks require before we can qualify for a home loan.

Purchase power – renting will make a lot more square-meterage available for a lot less monthly cost. This is indisputable, and it takes long, unemotional scrutiny of the bigger financial picture of our personal wealth growth to be prepared to make that sacrifice.

Renting a Property:

In the short term, all young adults will most likely go through the process of property rental. It is a completely necessary part of the property journey as it brings some awareness and knowledge to the challenges of property ownership from the point of view as a homeowner and perhaps later as the owner of rental property investments.

When applying to sign a lease for a rental property, the agent will undertake a credit check on us, the most salient part of that check to determine whether we have the financial means to service the rental and municipal services. Typically, they are looking to ensure that 30 % of our gross monthly income will cover these costs. However, we never receive our Gross Income, only our Net, so it makes sense to make our own calculations based on our Net Income, the actual amount that is deposited into our bank account.

Keep in mind when signing a lease that we will need to make the following payments up front:

- First months' rental.
- One month's deposit.
- Administrative and lease costs.
- Utilities deposit.

Once we have a lease, we may have to pay the following monthly expenses:

- Electricity
- Water
- Sewage
- Refuse removal
- City gas
- Security
- Data connectivity

Remember to factor all these costs into our monthly expenses, they can be a substantial part of the total rental account. Should we be in the process of renting, I would like to suggest a few additional considerations:

- Use this lease as a steppingstone, for no more than 24 months if possible. Keep a long term goal in mind.
- We should try and find a rental that is somewhere between 20 and 25 % of our gross monthly income.
- We can take the shortfall between our actual rental and the 30% and place it in a separate savings account. The purpose of this account is to create the basis for our deposit, transfer costs and bond raising costs to buy our own home.

Owning a Property:

Explore the Investment Value of Your Own Home:

In Workshop 4 of this program I go into a lot of detail regarding the benefits of owning our own property, and also using property as an excellent investment tool by putting our training and talents as Architects to use property to create our own wealth.

For virtually every single person, buying a fixed property will most likely be the most money we will ever spend in a single event in our lives. It is a daunting undertaking, and most people find the task intimidating. What if we get it wrong? What if we have paid too much? What if the building is unsound? What if the area is declining?

Our skills and training as an Architect endows us with a wide range of knowledge and abilities not enjoyed by members of the general public. For Architects, such considerations are the currency of our trade.

Owning our own property has the following financial advantages:

- Each penny spent is invested back into our own future wealth.
- Our skills as an architect give us the opportunity to add tangible and redeemable value to the property.
- All improvements to the building and garden are for our own benefit in terms of immediate enjoyment as well as long-term value.
- We start to build a strong credit history with the banks upon which we can leverage future business or property investment credit, the value of this cannot be sufficiently stressed.
- If we work from home, all the above benefits compound remarkably, plus many other less obvious advantages (covered in great detail in Workshop 4)

3.8 Financial Health & Wellbeing

Should we invest in our own property?

Fundamentally, it becomes clear to ask, is property a good place to invest to create our own wealth? <u>This is my own opinion on the matter</u>, one based on a long view and not the daily headlines. I am not an economist and probably not well equipped to answer this question. I will share the reasons why I prefer to invest in property.

- I back my own horse. Having chosen Architecture as a career, it seems appropriate.
- I have faith that the building industry in a developing country like South Africa will remain vibrant.
- The banks are happier to finance property over all other asset classes, making capital and access to credit far more accessible.
- I back bricks and mortar over paper (stocks and shares) – I play to my strengths and skills. To quote South African property investment guru Jason Lee; "It allows the investor the added benefit of being able to control the investment decision, as well as the process and outcome." (Unlike with stocks and shares). Furthermore, bricks and mortar are more difficult to liquidate into thin air. The value of the materials and labour is intrinsically attached to its physical substance.
- We must pay attention and monitor the value fluctuations in the area we are invested.
- Property prices in South Africa are exceptionally low compared to other countries in respect to the buying power of their respective currencies.
- Over the last five years the Rand has stabilized substantially against foreign currencies and the prime interest rate is being carefully managed.
- As the South African middle class grows and diversifies, which it is doing at a healthy rate, it is creating a huge housing shortage.
- Additionally, as this emerging middle class grows and invests, the security of land tenure stabilizes. No ruling political party will (sensibly) nationalize private property when such a high percentage of our population is now invested in land ownership and has so much to lose.

Our own home is our primary investment in our future wealth. It is a significant decision that comes with significant diligence and application. As Architects, we have a tremendous advantage over 99 % of the remaining population in how we go about this kind of investment, and doubtless, it would be a negligent lack of opportunity to not employ our skills accordingly.

Budgetary Considerations:

Owning our own property comes with the following budgetary considerations:

- All utilities as listed in the renting section, plus service and supply costs over usage:
- Monthly home loan payments
- Homeowners insurance
- Municipal rates
- Estate levies if in an estate
- Security costs
- Maintenance (plumber, electrician, garden, repairs etc.)

Transport

For some, this will be a fixed cost based on the availability of public transport. Ride shares and car pools can be manner in which to reduce costs if such an opportunity exists. Nevertheless, before buying a motor vehicle, it makes sense to investigate the costs of alternative transport. It gives us the opportunity to compare costs, or reconsider what kind of vehicle we need to buy as it may affect our usage and needs.

The ownership of a private motor vehicle will form a significant portion of our monthly spend, possibly even more than the cost of our home. There is no doubt that a motor vehicle is a deeply emotional and sometimes even an impulsive purchase. Because it represents such a large portion of our monthly expenses, it is critical that a rigorous decision-making process is implemented when choosing to purchase or replace the family automobile.

A motor vehicle is NOT an asset, unless one is a highly experienced trader in sought-after exotics, a motor vehicle will forever be an expense and must be treated as such. Peer pressure and social pressure has to be held at bay, so the simplest way to undertake such a transaction is to apply certain rules and limits in the form of a template.

Purchasing Guidelines for Motor Vehicles:

Place a 20% deposit. This can be in cash or a trade-in on our previous vehicle. A simple rule is that if we are unable to achieve this, the vehicle you desire is probably beyond our financial means.

Combined vehicle costs <u>should never exceed 10 % of our gross monthly salary</u>, we must make sure our repayments fall into our spend allowance and do not exceed our budget. Car finance is reasonably expensive, it is worth making every effort to keep our spend to the minimum. Fight for a good finance deal. Trawl the banks, be shameless, it is amazing what can be achieved playing the banks against one another.

It is useful to limit our finance to a maximum of 4.5 years (54 months). This facilitates payments remaining ahead of the depreciating value of the vehicle to avoid a situation of negative equity. Should the vehicle be destroyed, stolen, or sold, we will still be obliged to settle the bank on the outstanding loan before we can purchase a replacement vehicle, now without the benefit of a 20 % deposit. Premier brand motor vehicles tend to have a calamitous dip in value in the first 24 months of ownership.

Avoid 'balloon' finance deals at all costs, these are used to bring vehicles that are beyond our purchasing power to within our budget, the net result being that we are effectively doing nothing more than renting the vehicle for the duration, and run the risk of being left with a large portion of negative equity at the end of the deal.

A new vehicle vs second-hand vehicle?

The financial arithmetic can be complex; a new vehicle carries a premier price tag, whereas the ownership of a second-hand vehicle may work out cheaper if we take into account annual maintenance costs compared to monthly repayments on a new vehicle. Again, a brand-new vehicle has a precipitous drop in value once it is driven off the show-room floor.

Loan Settlement:

Once a vehicle is completely paid off – it will be much more cost effective to run and maintain than to start the whole payment cycle again with a brand-new car. At some point the use of a fully owned vehicle become more valuable to you than its trade-in value.

Expiry of the Warranty or Service Plan:

A common reason for buying a new vehicle is on expiry of the service contract. There is a noticeable drop-off in the value of a motor vehicle when this point is reached, prompting owners to recycle their vehicle prior to this point.

Motor vehicle finance experts agree that this is a very poor decision - rather renew the service contract, a new vehicle will require this expenditure in any case. Alternatively, we can continue to service the vehicle at our own expense, this will prove a far more cost effective solution than taking on the finance costs of a new vehicle purchase.

Replacing a vehicle:

Typically, it is our changing needs as a family or individual that drives our need to replace a vehicle. Consider them carefully before spending the money in order to ensure the purchase is a good fit and the money is well spent:

- A single person getting married
- Having children or additional children
- Looking after aging parents
- Changing workplace and travelling distances
- Long-distance travelling requirement
- Specific work requirements, i.e. off-road capability
- Additional needs – utility such as towing a caravan or a boat trailer
- Downscaling family requirements
- Physical limitations such as needing to change from a manual to an automatic
- Huge improvement in finances as a result of this workshop
- Downscaling expenses as a result of this workshop

Additional significant costs of Vehicle Ownership:

Over and above finance repayments and fuel costs, the following costs must be budgeted for:

- Insurance
- Regular servicing & Maintenance
- Tyres
- Parking
- Tolls

SARS:

Plan correctly for tax – an unexpected tax bill can be financially devastating. Mark provisional tax payment dates in your diary, make provision for the anticipated payment of tax in your budget. I advise the use of an accountant, they generally can best organize your finances to achieve the best results in tax compliance. A general rule of thumb is to allow for 27 % for tax on each income stream (after the deduction of expenses).

BLACK TAX:
When discussing personal finance in South Africa, the subject of Black Tax cannot be ignored.

A monthly contribution to the greater family is an expected duty. It is necessary to have a strategy in place with which to perform this duty that will enable it to be a sustainable for us and our family:

- The demands cannot be financially ruinous to the contributor, it is imperative they remain sustainable as a source of income.
- A basic monthly contribution is worked into your monthly budget and is determined by what your budget can sustain.
- Individual requests for additional amounts are judged (and refused as the case may be) on merit, and also on what funds are available that month depending on our budget,
- From the outset, individual requests are a gift with no expectation of repayment – budget accordingly.
- <u>Do not sign Sureties!!</u> There is always the possibility that the borrower lacks the ability to maintain the repayments. Using us as insurance, they may feel enabled to default and allow us to finance the outfall. Basically, the moment one signs surety, the loan is OUR responsibility, and the financial institution will come after us. Any consequences reflect on our credit record.

DEBT:
It is widely agreed that the priority of any financial strategy is to seek to settle all our existing debts. South Africa has relatively high lending rates, so it is extremely useful to be numerate and understand the significance and impact that compounding interest has on the cost of borrowing.

It is essential that we quantify and understand our debt burden:

Debt Types:
Unavoidable debt:
Clearly, there is a necessary requirement to incur debt should we need to purchase a home. Equally, the purchase of a motor vehicle will necessitate the need to raise credit. I have discussed strategies for undertaking these purchases to get the best value for money. It is also imperative to manage these debt agreements in diligent and responsible manner.

Credit is a powerful tool and a fragile privilege. It should be used with great care and consideration. If it is abused, or used negligently, our access to credit will be revoked – sometimes permanently. Banks are risk-averse organizations with scrupulous record keeping. It is therefore vital to manage our home and vehicle finance with diligence. Ensure that whatever we borrow, we can comfortably service each month.

Avoidable debt – 'Needs':
If we find ourselves in a position where we use our credit card to buy groceries by necessity and not choice, then we may be in the midst of a debt crisis. This can be further exacerbated if we are only paying the minimum revolving interest payment on that credit card. Effectively, the credit card will soon max out and will be of no further use to us and will now require the payment of an additional monthly settlement to cover card fees, interest and facility costs.

This unhappy situation often escalates to the need to source a 'month-end' loan, lenders being happy to forward a small loan using our next salary check as collateral. This quickly descends into a 'debt spiral', an income not covering existing expenses now being stretched to cover the costs of an additional loan.

One suggested way to manage this is to have our salary deposited into a savings account or a separate debit card from which we then pay ourselves a 'salary' for the week into a spending account. This weekly payment is to include the value of all our debit orders and necessary expenses for the week. We then refrain from spending more than the 'salary' amount that is in our spending account. Additional expenditure must wait until the following week. It is easier to do manage a budget on a weekly basis than over an entire month.

Avoidable debt – 'Wants':
Simple test – 'Can I live without it?' I have provided a reasonably accurate compound interest and loan cost calculator. It can be used to run the monthly repayment costs on a loan of any type at any interest rate and period. It also makes provision for the various costs associated with buying items on credit. The worksheet is provided to allow us to *explore* possibilities. There are numerous calculators financial service providers host on their websites. Make use of these tools too.

The workbook's primary purpose is to graphically illustrate the devastating cost of credit, and why creating a disciplined savings plan is so rewarding. The Garnishee Orders experienced by my friend's staff were nearly without exception raised as a result of the purchase of a household item, a bed, a settee or a television. In nearly all of these cases the purchase could have been delayed until savings were made and the item bought for cash.

An unjust and crippling legacy of Apartheid is the lack of access to credit for the major portion of our population. Previously disadvantaged citizens cannot meet the draconian qualification barriers imposed by the high-street banks and are forced to seek credit elsewhere at much higher interest rates and at times illegal terms and conditions, the gap in this market being provided by unscrupulous furniture stores and informal loan-sharks.

Hire Purchase:
This is a popular method of purchasing goods that should be avoided if at all possible. In a 'hire purchase' agreement, ownership is **not transferred to the purchaser**, we are basically hiring the item until <u>all</u> payments are made – it is not an extension of credit as would be the case with a loan.

The material difference is that the ownership of the goods remains with the lender, meaning that should the borrower default on payments, the lender can retrieve his property, then charge us additional damages and costs over and above what we have already paid towards the item and the outstanding amount. In many instances, there is also a hidden balloon payment that will also need to be settled. Additionally, in these agreements it is illegal for us to sell this item before we have paid it off.

This method of lending has come under criticism from the Consumer Protection Act as it is intrinsically unjust and is often abused.

Rehabilitating Debt:

While avoiding debt is first prize, rehabilitating existing debt is always our priority.

This simple strategy can be started by considering our smallest debt. We set about clearing this debt by putting in any additional money we can. Once it is cleared, we pay the amount we were spending on this debt into the next smallest debt until it too is paid off.

We continue this process until we are paying all our previous loan repayment amounts into our biggest non-investment debt. We can attack the repayment of this debt using the repayment savings of all the previous debts combined. As the process progresses on a month-by-month basis it gathers momentum.

- The settlement of each debt provides a huge boost and sense of relief, and slowly we begin to take ownership of our own income.
- We end up investing in ourselves in that we are reducing the stress that loans and debts put us through.
- We are moving towards the ideal spending rule-of-thumb ‘template’.
- When we take ‘ownership’ of our debt burden and begin to resolve it, the process starts to have a significant impact on how we spend or borrow money in the first place.

Should the servicing and management of our debt prove overwhelming, we can seek the services of a professional debt counsellor. They can create a plan to rectify the situation, negotiate new and favourable repayment terms on our behalf, and assist us in the management of our funds.

Make a ‘War Chest’:

It is widely agreed that the next priority once we have eliminated all practical debt is that we create a repository of an amount equal to 3 months of our salary as a ‘war chest’. This is to be used for emergency expenditure such as a major mechanical fault on a motor vehicle, unexpected medical emergencies (as opposed to additional medical expenses not paid for by your medical insurer), or a lockdown due to a pandemic. Having no funds available for such emergencies can result in even more catastrophic consequences, a broken car can result in the loss of a job.

Admission to hospital care from casualty demands a large cash deposit, often upwards of R 40 000.00, even if we have a medical aid policy in place. Not having funds or credit available can see medical help withheld from us or a loved one.

- The ‘war chest’ must be ‘ring fenced’ and not plundered for casual purposes.
- We should set these funds aside in a different account altogether.
- Should the fund be used in the case of an emergency, it should be fully replenished before any other savings proceed.

Personal and Discretionary Spending:

If money equals happiness, what kind of spending would bring us most happiness? The reality is no matter what we earn, no matter how ‘wealthy’ we are, there will always be unfulfilled desires. This is a standard human condition, and it forces us, by necessity, to make value choices. Understanding this, we can apply our minds critically to making good choices.

Discretionary spending is the one area of the budget where most adjustments can be made to manage our expenditure.

3.8 Financial Health & Wellbeing

The Allure of 'Stuff':
The biggest category of self-spend is on 'stuff'. It is driven by a well-funded and persuasive advertising industry to help prop up consumer demand and maintain the capitalistic economic model. It is a 'flat' reward and does not in fact bring happiness. When we bring clarity and critical attention to our spending, we spend less, up to 20% less, according to studies. According to Vicki Robin, a personal finance guru, our spending should reflect 'our true happiness and our sense of purpose and values'.

Change 'Stuff' for something else that perhaps brings 'Experiences', like dance lessons or hiking. These can be shared and provide a more meaningful and durable happiness. To be satisfied is a choice.

The 'Big Bill Prevention Rule':
Do not confuse necessary expenditure with desires. Provision can be made for setting aside savings for holidays and other large expenses (a wedding, buying a caravan), also known as the 'big bill prevention rule'.

The attached Interest Calculator will quickly prove the immense savings to be made by setting money aside for future projects to avoid using credit and its associated costs. We can analyse the spending of previous years to make proper and accurate planning for these projects (a family holiday for example). A known departure date with accurate cost forecasting using data from previous trips enables us to save purposefully in preparation.

Should our savings preclude the project, or we experience an emergency or even a more deserving project, the funds can be diverted where they are most needed before any costs or commitments have been incurred.

Conspicuous Wealth:
The purpose of rigorous budgeting is to bring into clear focus our spending habits. The need to exhibit our blessed good fortune can be quantified and scrutinized. The objective is not to prohibit spending, but to spend in a sustainable manner.

Entertainment:
Whenever budgets and savings are being thrown around, 'Entertainment' hides under the table, always being the first expense to face sacrifice! Ironically, the one budget that always faces the axe but never gets slaughtered is invariably 'Entertainment'! Why is that?

We would rather not replace school uniforms than give up our restaurants, mid-priced wines and decent braai meat. A budget can only work if we approach it in a realistic, honest way. The budget must represent who we are as people.

I would recommend that we leave Entertainment in the budget and increase it each year. Just as nobody stays on a diet that leaves them hungry and unhappy, nobody will subscribe to and adhere to a financial plan that makes them constantly miserable.

Let us be realistic about who we are and what we want and plan our finances accordingly.

Living a Life:

One of the fundamental uses of financial planning is to bring about prosperity and a financial 'sufficiency'. Most associate an exercise such as this with austerity and frugality, but oddly, its objective is quite the opposite. Once we have mastered the skills and implemented the discipline, money is no longer a scarcity. It is the liberation from debt and the freedom to use money constructively that is empowering.

In the broader perspective of those things that are important in our lives, the sacrifices required are not really sacrifices at all. The process merely requires a critical look at what we spend on and which of those expenses are worthy of the cost. The budget can reveal a startling contradiction as to who we think we are and how our spending depicts us.

WEALTH GENERATION

The desire to make and save money cannot be separated from a strong and definite will to do. This workshop is built around a discipline towards money that we grow and cultivate. As we implement the various strategies and habits, we become trained in the exercise and are greatly encouraged by results.

INVEST IN OURSELVES:

Very early on in this workshop I mentioned that we should literally set aside 10% of our income and literally pay it to ourselves. 'Paying ourselves' may sound obvious, but it is an indisputable reality, and as the second chart clearly reveals, that virtually all our income is deployed in covering nothing more than our monthly expenses.

This may seem like an odd course of action but it is deliberately conceived to initiate a change in our relationship to our income and what we do with it. In order to facilitate this 'allowance' we may be forced to reduce our living expenses by 10 % in order to make the money available.

The money set-aside actually has no other purpose than to form the seed for the growth of our wealth - this is the money that is set aside to start to work for us. We will seek to find suitable deployment for it and as it grows each month and with accruing interest or dividend, so it will compound and start to work for us even more. This will be discussed in detail in a later section.

That may seem like an insurmountable task, but it sets the habit of consciously managing our budget and creating good financial habits, it begins the process of engaging with our budget and starting to manipulate it in a deliberate way and with a definite goal.

Secondly, it starts to make us perceive our money as a tool. Setting aside money for our own discretionary use serves as a reward for our labour; an indispensable and self-propelling motivator. Psychologically it lays the foundation of a positive relationship with money and can promote our self-esteem and confidence.

Thirdly, money retained in this manner seems to create a life of its own, its very existence serving as a spark of opportunity and possibility.

INCREASE OUR ABILITY TO EARN:

The most immediate way to improve our ability to earn is to upgrade our education, knowledge and skills, continually and consciously. It is typical for working people to improve their earnings as they get older and progress through their careers. However, we can fast-track this process by creating a strategy to acquire the necessary skills and knowledge to accelerate our career progress.

PUTTING OUR SAVINGS AND INVESTMENTS TO WORK

The ultimate goal of savings deployment is to create a passive income from which we may live a comfortable life. Understanding the growth mechanics of compounding interest can assist in achieving this. There are different types of savings to achieve different goals:

Short term savings:

'Short term' savings are generally set aside for specific purposes:

- Primarily to create a 3 month income 'war chest' emergency fund as detailed earlier.
- To save for a specific financial goal as described in the 'big bill prevention rule'; to pay for a wedding, family holiday etc. In this case there is a fixed known time allocated, and a budget. The savings can be itemized on our budget and the savings kept in a separate account if necessary.
- Assign tasks to all rands left over at month end, allocate them where they will be most useful.

It is necessary to point out that although savings stashed 'under-the-mattrass' (or 'in-the-sofa' as the case may be) will not actually reduce, the buying power of this money will reduce as a result of inflation. Even though Banks offer very small interest on positive balances and savings accounts, this interest will nevertheless slow the erosion of the 'buying power' of our money.

Long term savings:

To establish investments to employ each rand to generate income and growth, and for those additional rands to be employed in turn towards the goal of creating a passive income. The best time to start our retirement planning and begin saving is always 'yesterday'.

As illustrated in the ideal version of the spending pie chart earlier in the workshop, established wisdom states that 20% of our income should be set aside for this purpose, however; a holistic view is required when considering what portion of our income should be set aside as it must be viewed in the perspective of settling certain high-interest debts beforehand. That will always be a higher priority for the allocation of available funds.

When making long-term investments, we must exercise diligence and common sense to avoid unnecessary risk or loses with these savings and investments.

Exercise Prudence when Investing Your Nest Egg:

It is all very well stabilizing our finances and finding ourselves in a position to start saving money and perhaps even to create a substantial nest egg. Sometimes, we are even blessed with a windfall, a large final payment on a large project for example.

3.8 Financial Health & Wellbeing

The primary objective is to invest where our principal is safe, in other words, making a bad return on our investment is one thing, but to lose our original investment is disastrous. The following cautions are recommended:

- Perform due diligence – investigate carefully all that can be known about the investment proposal – will our principal remain safe?
- Take advise from proven and reliable sources, and vet them (and the advice) accordingly. This is why it is important to understand monetary terminology.
- Invest using specialists in the field – especially if we are investing in a particular industry, our advisors may understand their own trade but not know much about the mining sector that interests us.
- Use financial advisors that are free agents and not linked to any particular service provider, product or brand, if they are, their vested interest renders their advice tainted at best.
- Do not be over-confident of our own wisdom – having made money does not guarantee that we cannot lose it too. Have an awareness of that which we do know and that which we don't.
- Try to avoid investing with friends or family – it calls into question their own competence to advise us, there is an emotional element that can create unwelcome risk to the investment and may compromise our normal channels of recourse. If it goes wrong can or will they repay us? Will our principal be safe?
- Moderate our emotional responses – gains and loses need to be considered critically. It is necessary to keep a clear and rational head when assessing results.

BECOME NUMERATE

It is of no use doing the research, educating ourselves and seeking advice from qualified professionals if we don't properly understand accounting and economic terms. Become familiar with the language of money; capital, asset, liability, interest rate, loan terms, lending rate, down payments, service fee, cash flow, income statement, balance sheet, turnover, gross vs net, PAYE, SDL, UIF, income tax, business tax, compound interest and how it works, fixed and movable assets. Liquidity is not the state of the swimming pool.

It is crucial to understand the relationship between equity, liability and asset.

- EQUITY is the real value of an item.
- ASSET is the cash value one can convert the item into.
- LIABILITY is the outstanding amount still owed on the item.

Equity can be calculated by taking the value of the item should we sell it now, less the amount we still owe on the item. Thus, if the result is a negative value, you are making a loss on the item, if the result is a positive value, you are making an investment.

CONCLUSION

Investing in your Happiness

If Warren Buffet attended this workshop, he would probably agree in principal and give it a sage nod. Buffet is the international spokesman for fiscal prudence and due diligence. He is famous for his restraint, frugality, and extreme care.

In my opinion, Buffet is wrong about money. He famously lives in the house in which he grew up and drives a 20-year-old family Mercedes. Buffet's interest in money extends no further than his ability to accrue it as a pursuit to its own end, he does not seek to permit money to be a tool that can empower us and bring into reach things we aspire to.

Things we aspire to do not need to be fancy cars or material things at all – money can fulfil the desire to help others, uplift communities, learn another language, to play a musical instrument, get our children into a good school, travel, and very importantly, take time away from the mill to explore ourselves and grow as people. To make time for our loved ones.

In fact, in our profession, possibly the most valuable thing money can buy is time. An extremely precious commodity that is all too often desperately overlooked and, as it happens, is the subject for another Workshop.

The only urgent thing in our life is to take control of our finances NOW.

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Reference Reading:

- <u>Sam Beckbessinger:</u> "How to Manage your Finances like a F*cking Grown Up"
- <u>George Clasen:</u> "The Richest Man in Babylon"
- <u>Jason Lee:</u> "Making Money out of Property in South Africa"
- <u>Robert Kiyosaki:</u> "Rich Dad Poor Dad"