

201

8

Budgeting for Beginners

Table of Contents

Introduction.....	3
Welcome.....	3
What is Included?	3
Disclaimer	3
Building a Budget.....	4
Analyzing Your Cash Flow	4
What is Cash Flow?	4
Why Cash Flow?.....	4
Calculating Income:	5
Calculating Expenses:.....	5
Positive Cash Flow?.....	6
Implementing a Budget	7
How should I set up the Budget? What needs to be included?	7
Be reasonable, but include everything	7
Itemize	8
Start Now, Adjust Later.....	8
Tips for Budgeting.....	9
Don't Ignore Saving.....	9
Avoid Over-Spending	9
Be Yourself.....	9
Be Humble	9
Celebrate	9
Start Yesterday	9

Introduction

Welcome

Thanks for downloading my first e-book. I am honored to provide you with important information about your personal finances. I started blogging in August 2011 when I realized that it is so difficult to find quality information for the beginner. I have always been fairly responsible with my finances. Part of this is due to my parents' upbringing and part of it is due to just a general interest in finances. I love being able to optimize my time and money. I want to be intentional with every penny and want to share the information that I have learned (and still learning) with as many others as I can.

What is Included?

This book includes three major parts that any individual or family would have to conquer when starting to budget. This is by no means a comprehensive book or list of things to conquer to be the master of your personal finances. This is just the beginning. These three items are what seem to be fundamental aspects of budgeting.

Here the brief outline:

1. Analyzing Your Cash Flow
2. Implementing Your Budget
3. Tips for Budgeting

It starts from the very beginning, analyzing your income and expenses and end with practical suggestions on becoming more efficient at budgeting. I strive to make it as simple as possible. I explain the details of what can be complicated. My goal is to make this seemingly daunting financial challenge as easy as possible.



Disclaimer

I should also note that I am not a professional financial advisor. While I make every effort to give you accurate information, major decisions require your own sound judgment. I recommend that you seek professional advice to confirm any information presented here or on www.20sfinances.com. [20's Finances](#), nor any of its authors, can be held responsible for loss or damages that result from any advice presented.

Building a Budget

Analyzing Your Cash Flow

An important question to ask is where to begin? If you are new to managing your personal finances, this can be one of the most difficult questions to ask. The answer to this important question is simple: your cash flow.

What is Cash Flow?

One of the last things I want to do is to throw hard-to-understand financial jargon at you. Cash flow is the difference between what you earn each month and how much you spend. Some investors use this term to talk of the profit from their real estate investments, but it refers to the same basic formula:

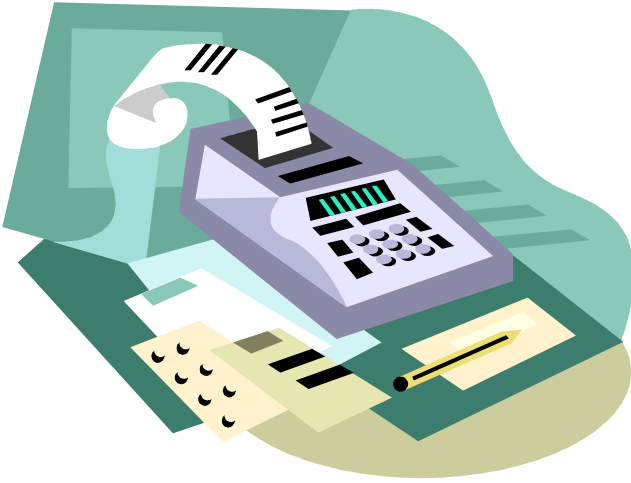
$$\text{Income} - \text{Expenses} = \text{Cash Flow}$$

Why Cash Flow?

Out of all the places within the realm of personal finances to start, why would I start here? This is a great question. I believe that managing your personal finances revolves around a couple of basic principles. The first is resisting the rampant consumerism or impulse purchases. You see this everywhere. Everyone wants the latest technology or fastest, most efficient item that there is on the market. Learning how to say no to this urge to have the latest, fastest, best product is the key to financial success. Learning how much cash flow you have each month gives you a great foundation for evaluating whether you are financially able to buy the item that you really want. For example, if you are just making ends meet (or have a cash flow of \$0) each month, you really shouldn't be purchasing items based on desire. A person who is aware that their cash flow is zero is more likely to resist that impulse buy than the individual who has no clue where they stand.



Another fundamental of personal finances is not just on the defensive, but on the offensive: what to constructively do with your money. In order to begin to answer this question, you have to first understand how much money you have to invest (or how much cash flow you have).



Calculating Income:

The most logical place to start with calculating your cash flow is to understand your monthly income. This can be quite confusing when first starting out. The easiest way to do this by looking at your pay stub. Your pay stub will feature a lot of acronyms that are important to understand, but for the time being, we are going to focus on two items: gross vs. net income. Gross income is the amount of amount of money that you earn before taxes. This is often the amount that is advertised (if it is advertised) on a job listing. Net income is the amount you take home. It is the amount that you earn after taxes are deducted. For the purpose of budgeting, I recommend using your net income as opposed to the gross amount. If you are paid monthly, it is easy to calculate how much you earn for that month. If you are paid weekly or bi-weekly, simply add up the net income for your current month. You have already figured out how much money you have to spend! You are well on your way to successfully managing your finances.

Calculating Expenses:

Expenses are not as easy to determine as income. I wish, for your sake, that there was just one way to look to determine how much you are spending. It is helpful to know that there are two types of expenses: mandatory and optional.

The major difficulty that people face in managing their finances is misclassifying an expense as mandatory or required when they are really optional. For example, a good friend of mine would almost certainly classify his daily cappuccino from the local coffee shop as a mandatory expense, but most of us understand this is not the case. Some examples of mandatory costs are: housing, transportation, insurance. These are the things, that as “mandatory” suggests, you can’t live

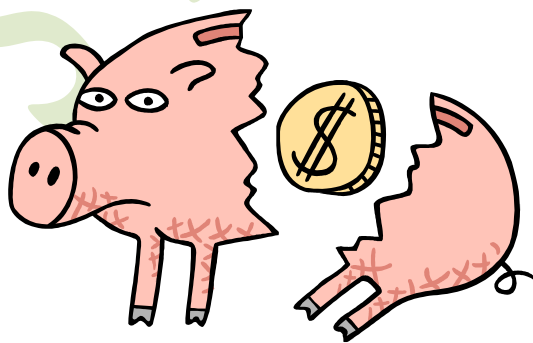
“...a good friend of mine would almost certainly classify his daily cappuccino from the local coffee shop as a mandatory expense...”

without. Optional expenses would include: entertainment, eating out, etc. It is also important to point out that even what I have deemed mandatory costs are flexible as well. For example, if you determine that you are spending too much for housing, you can always move to a smaller house or apartment to save money. These are classified as mandatory because they are often unavoidable costs. You have to live somewhere and you have to eat. I think you get the picture.

An easy way to figure out how much you are spending on a regular month is to track your purchases for a month or two. Some people suggest writing down every expense when it you pay for it. While I usually prefer to use my credit card for everything (and then use my credit card statement to review my spending), for the time being, I will suggest simply writing everything down. If you want to reap the benefits that credit cards offer, read my article on effectively using [Credit Cards](#).

Positive Cash Flow?

Once you determine your expenses, subtract that from your income. If you are spending more than you make, there is a problem. In an ideal situation, you should never have a negative cash flow. If you are spending less than you make, you are in a great starting place to begin analyzing how to save more money. In either position, anyone can significantly improve their finances by recognizing their current cash flow. If you have figured out these two things, you have already accomplished the first step in managing your finances. Keep up the good work!



Implementing a Budget

Once you have established your cash flow and you have committed to be responsible with your finances, one of the first things that you want to do is to set up a budget. To some, this can be an overwhelming task. I want to help walk you through the basic steps.



How should I set up the Budget? What needs to be included?

These are important questions to ask, but it should not prevent you from getting started. In fact, the first thing to do is to start small. Don't try to have so many details or things that you get overwhelmed and sick of budgeting with your first attempt. While I encourage people to start small, the best word of advice is to use as

“Expenses come up, and a budget will help you prepare for it when it happens.”

much information as you feel comfortable with. For those of you like me, who enjoy budgeting and tracking expenses (I understand this may be rare), you may want to get as detailed as possible. Even if you are not as excited as I am, you should try to celebrate your achievements as you progress. Making sure that you enjoy managing your personal finances improves your situation significantly.

Be reasonable, but include everything

The other thing to recognize is that a budget is also a tool to help limit your expenses. No one is capable of spending the exact same amount of money each month no matter how much planning is invested. Expenses come up, and a budget will help you prepare for it when it happens. Establishing a budget is a great way to prepare for the unexpected. By establishing a budget with total expenses less than your income, you will not only save money each month but prepare yourself for those surprise expenses like repairs to your cars.

Some people, when starting to budget, only worry about the big items like rent, food and travel. These are what really matter, right? Wrong! Responsible budgeting is about tracking those small expenses. You would be surprised to see how quickly those everyday expenses add up. If you don't include every daily expenses, your budget will not give you an accurate picture of your cash flow. As a result, you will most likely overspend.

Itemize

The first thing you want to do actually set up your budget is to break it down into smaller categories. Simply establishing that you are going to spend X amount of dollars the next month won't help you that much. Instead, separate it into logical categories. Here are the categories I use in my budget:

- Housing
- Transportation
- Insurance
- Food
- Personal Care
- Entertainment
- Gifts/Charity



It can also be helpful to include a miscellaneous category to make sure you are including everything as I mentioned above. I avoid this by having an even more detailed budget with sub-categories (which include an “other” subcategory for each large category).

Start Now, Adjust Later

You may find that you want to improve the format of your budget as you go along. This is okay! Take joy in the fact that you are being responsible with your finances as you improve your budget. Also, don't let this prevent you from starting today. Recognize that you will modify your budget as things change. I personally like to update the format of my budget each calendar year to make it do more calculations or more user-friendly.

A great way to start would be to download a sample budget. Microsoft offers templates with excel, but I have created a [Sample Budget](#) for you to use. By adding in your income and expenses for each month, you can not only view your cash flow (how much you are saving or over-spending) for each month, but can view the year's progress. The best part of it is that the spreadsheet does all the calculations for you. Don't ever spend the time to do all the numbers with a calculator. The sample budget doesn't have all the bells and whistles, but it is a great starting point.

Enjoy personalizing your own budget.

Tips for Budgeting

Don't Ignore Saving

It is easy to get in a routine of not worrying about how much you are saving each month and before you know it, you haven't saved any money for the entire year. Many experts suggest saving first. This is a great policy to have because it ensures that it is valued just like other expenses on your budget. I also like the idea of setting tangible goals with their associated costs. For example, if you know in about two years you will want to sell your current car and buy a newer one, calculate how much you want to save in the next two years and how much you should be saving each month. Doing this for multiple items ensures that saving money is not overlooked.

Avoid Over-Spending

Sometimes things do come up and you have to spend more money than you make each month. For example, I recently discovered that I needed to buy new tires for my car, which cost around \$500 for the set of four and installation. This was unexpected and my wife and I overspent our income by a couple hundred dollars for that month. However, if this is happening on a regular basis, you aren't budgeting correctly. I had someone just tell me that for years they were budgeting, but were never coming out with a positive cash flow. Budgeting isn't merely a task of tracking your expenses. It also consists of limiting your spending. You should be establishing manageable goals for your spending at the beginning of each month. Ensure, at the very least, that you have a positive cash flow most months (if not all).



Be Yourself

While it can be beneficial to use someone else's templates or system, it is best to experiment until you figure out what works for you. Once you have done that, you will be much happier than trying to follow someone else's steps. While I provide a free excel spreadsheet for a [Sample Budget](#), it is only that – a sample. Customize it and make it your own. This is the only way you will continue to budget in the future.

Be Humble

It is easy to become confident in your skills to manage your own money once you have been doing it for a while. This may lead you to become over-confident and ignoring the details or not being intentional about saving. Don't let this be you – stay committed.

Celebrate

When you think of budgeting, it should be something that is exciting. Take joy in your discipline and celebrate your achievements! Don't let it become too much of a chore that you end up discarding the whole process in a couple months.

Start Today

If you currently do not have a budget, start today. If you say you will start soon, you may end up doing that – but probably not. Why wait? Start today and enjoy the benefits of financial security.