



Understanding the Financial Planning Process

Chapter 1

Learning Goals

LG1

Identify the benefits of using personal financial planning techniques to manage your finances.

LG2

Describe the personal financial planning process and define your goals.

LG3

Explain the life cycle of financial plans, their role in achieving your financial goals, how to deal with special planning concerns, and the use of professional financial planners.

LG4

Examine the economic environment's influence on personal financial planning.

LG5

Evaluate the impact of age, education, and geographic location on personal income.

LG6

Understand the importance of career choices and their relationship to personal financial planning.



How Will this Affect Me

- The heart of financial planning is making sure your values line up with how you spend and save.
- An informed financial plan should reflect uncertainties and more.
- This chapter overviews the financial planning process and explains its context.



Financial Facts or Fantasies?

- ▶ Your income level depends on your age, education, and career choice
- ▶ Over the long run, gaining only an extra percent or two on an investment makes little difference in the amount of earnings generated
- ▶ Personal financial planning involves translating personal financial goals into specific plans and arrangements that put these plans into action.
- ▶ A savings account is an example of a tangible asset because it represents something on deposit at a bank or other financial institution.
- ▶ An improved standard of living is one of the payoffs of sound personal financial planning.



Personal Financial Planning

- A systematic process that considers important elements of an individual's financial affairs in order to fulfill financial goals.

Six-Steps Financial Planning Process

1. Define financial goals.

2. Develop financial plans and strategies to achieve goals.

3. Implement financial plans and strategies.

4. Periodically develop and implement budgets to monitor and control progress toward goals.

5. Use financial statements to evaluate results of plans and budgets, taking corrective action as required.

6. Redefine goals and revise plans and strategies as personal circumstances change.



Rewards of Sound Financial Planning

- Flexibility
- Improved Standard of Living
- Spend money more wisely
- Accumulate Wealth

Organizational Planning Model





Financial Goals

- ▶ Results that an individual wants to attain, such as buying a home, building a college fund, or achieving financial independence.
- ▶ Examples:
 - ▶ Controlling living expenses
 - ▶ Retirement planning
 - ▶ College Education for kids



Financial Goals Myths

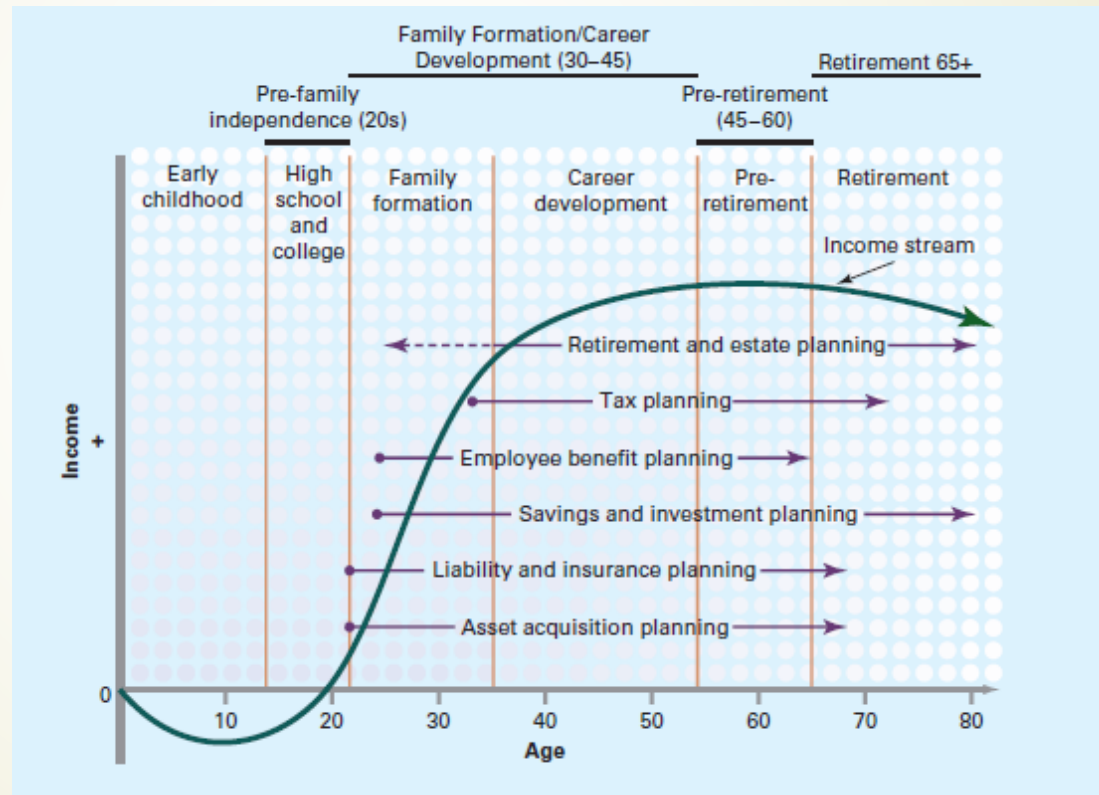
- ▶ A Emergency Fund that lasts three months should be adequate
- ▶ I will be able to retire at 65 and should have plenty to live on in retirement
- ▶ Saving a few thousand dollars a year should provide enough to fund my child's education.
- ▶ I am relying on the rule of thumb that I will need only 70 Percent of my pre-retirement income to manage nicely in retirement.

Putting Target Dates on Financial Goals

- ▶ Long-term
6 years or more
- ▶ Intermediate-term
the next 2-5 years
- ▶ Short-term
in the next year



The Personal Financial Planning Life Cycle



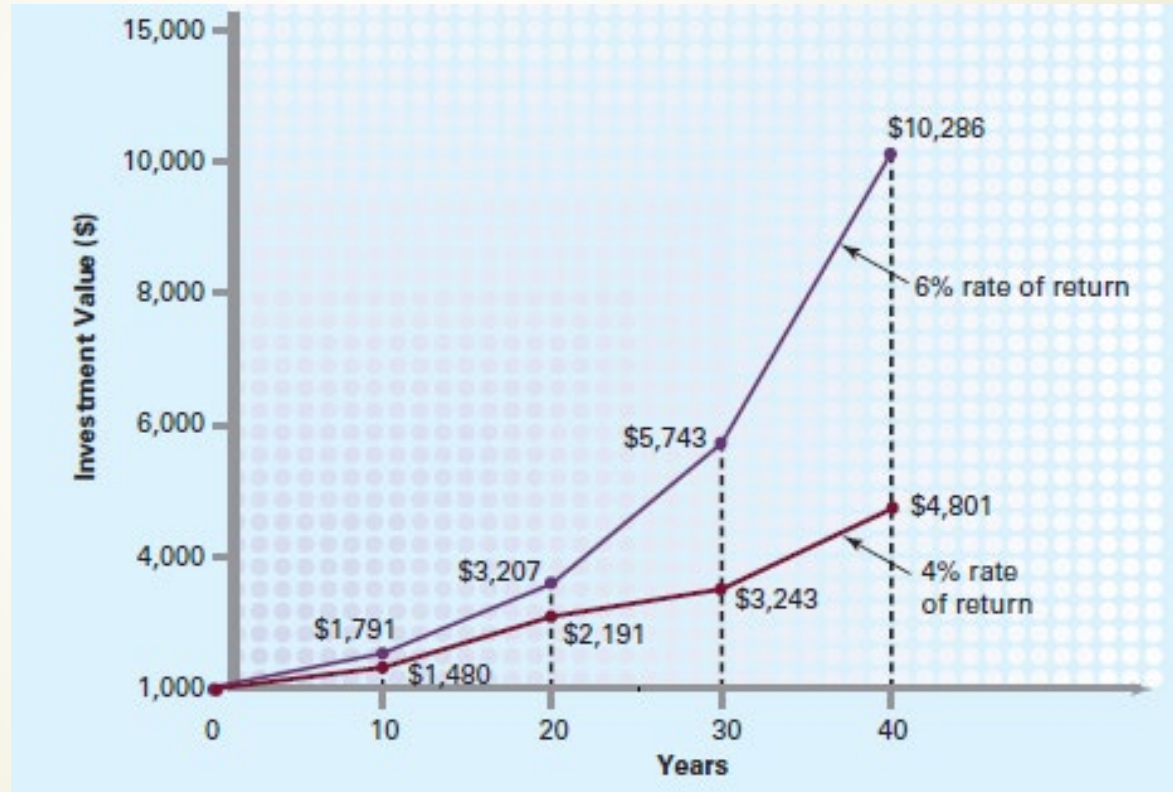
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Retirement Planning

Example: The sooner you start an IRA, the better

If you start investing for retirement at age 40 and put only \$2,000 a year in an IRA earning 5 percent for 25 years, you will have \$95,454 at age 65. However, if you start the same retirement plan 10 years earlier at age 30, **you will have \$180,641** at age 65!

How a \$1,000 Investment Grows over Time



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Two Income Family Facts or Fantasies

- ▶ Two-income couples account for the majority of U.S. households
- ▶ Often a second income does not add as much as expected to the bottom line
- ▶ Two-income couples should have two checking accounts to keep earnings separate
- ▶ Second income is used only for investments
- ▶ Two-income couples have more stress and spend less time with family



Professional Financial Planner

- An individual or firm that helps clients establish financial goals and develop and implement financial plans to achieve those goals.

European Financial Advisor (EFA)

European Financial Planner (EFP)



Using Professional Financial Planners

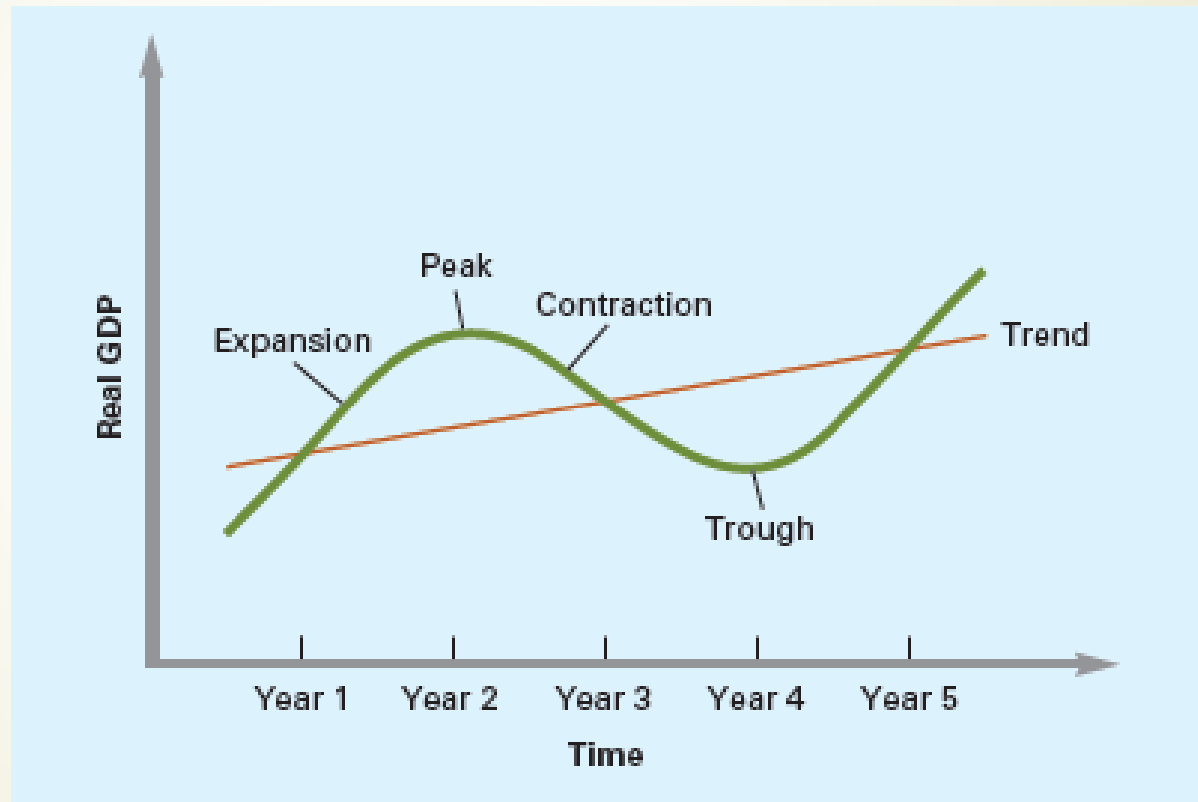
- ▶ Commission-based planners earn commission on selling financial products such as insurance or annuities.
- ▶ Fee-only planners charge fees based on complexity of prepared plans and time
- ▶ Hybrid approach involves both charging fees and collecting commissions.



The Planning Environment

- ▶ Financial planning takes place in a dynamic economic environment created by the actions of
 - ▶ Government – through regulation, expenditures and tax policies
 - ▶ Business – provide consumers with goods and services
 - ▶ Consumers – their choices determines the kinds of goods and services that businesses will provide

Business Cycle – Four stages: Expansion, Peak, Contraction, Trough





What Determines your Personal Income

- ▶ Your Education
- ▶ Where you Live
- ▶ Your Career
 - ▶ Examples of Average Annual Salary
 - ▶ Accountants -- \$73,760
 - ▶ Computer Programmer - \$82,690
 - ▶ Lawyer - \$133,470
 - ▶ Financial analyst - \$92,250
 - ▶ Teacher, elementary - \$56,830
- **How much income do professionals earn in your Country?**