Budgeting and Financial Planning Tools Documentation

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Sections:

1. Bill Schedule
2. Flow Budget
3. Stock Budget
4. Investment Planning
5. Incentives Plan
6. Lifestyle Adjustment Plan
7. Comments
8. Rev 2/28/16

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1 – Bill Schedule

The bill schedule is an enhancement to the traditional budget because it gives us an idea of the fluctuations of bills over time. This allows more flexible and dynamic saving and consumption over time, in contrast to the more traditional approach of setting aside relatively fixed portions of income each period.

The bill schedule approach in this toolset is also sensitive to the fact that there are different kinds of cyclical costs which occur over different time frames. To keep things clear, we use three separate bill schedules, which we will later address with three or more separate income treatments.

The recommended approach for this toolset is to look at incomes and expenditures over three time frames: weekly, monthly, and yearly.

The bill schedule is the groundwork for the flow and stock budgets, which in turn provide the groundwork for the rest of the financial planning process.

2 – Flow budget

The flow budget looks at income and expenditure over a particular timeframe. This is very much a traditional budget, except that the current level of debt or savings is ignored.

The key idea of the flow budget is that cash flow should be positive. The purpose of the flow budget is to ensure a stable, positive cash flow, but it is not to maximize cashflow.

The flow budget includes minimum, target, and stretch goal budgets values. Using a range of potential values allows the budget to better capture variable income and expenditure.

If you are able to work with statistical models then these three values can be replaced with an expected value along with an arbitrary confidence interval chosen to match your preferred risk or confidence level.

3 – Stock budget

The stock budget accounts for the current level of debt and savings.

4 – Savings and Investment Plan

The savings and investment plan is perhaps the most important part of the budgeting process. This plan takes in two input groups and produces one output. The first input group is the set of three previously completed plans. The second input group is the set of any investment opportunities an individual is interested in potentially executing.

The savings plan will allow a person to determine their possible levels of income at a variety of points in time by looking at the financial return of taking various actions. Such actions include paying off current debt, taking on new investment, or even taking out new loans to increase current wealth at the costs of cash flow and later wealth.

5 – Incentives Plan

The incentives plan has two purposes. First, the incentives plan includes plans for long-term goals which clarify the purpose and use of the savings and investment plan in real terms rather than strictly financial terms.

Secondly, the incentives plan includes budgeted rewards and punishments which encourage individuals to meet their own goals.

6 – Lifestyle Adjustment Plan

The lifestyle adjustment plan is an optional planning tool which is used for three purposes. First, it can be used to plan reductions to lifestyle costs, which are notoriously stubborn and difficult to reduce.

Secondly, the plan can be used to plan out lifestyle cost increases, such as the increase associated with the birth of a new child.

Finally, the plan includes an introspective analysis which may help an individual translate subjective or qualitative lifestyle information into cost-equivalent data which can then be roughly analyzed in the context of a cost-benefit analysis.

7 – Comments

I would like to make three comments regarding the toolset as a whole. First, using the toolset with hypothetical scenarios, in parallel to real use, is immensely helpful. Viewed this way, almost like a game, it can help to uncover the general principles in play.

Secondly, regarding the frequency of updating each plan, I think the weekly and monthly budget should be reviewed weekly, and the larger-scale planning tools should be briefly reviewed monthly and intensely reviewed about once each quarter.

8 – Revisions

* Set the budget and check-up on the budget
  + Set the budget once a month. It all starts with the monthly budget, which is our core tool.
  + Check-up weekly.
  + Redo the budget as needed. Generally, follow the “3 Strikes and You’re Out” rule. See: <http://www.afterecon.com/economics-and-finance/when-to-re-do-your-budget/>
* When setting the monthly budget you should revisit all 7 or 8 plans, in this order:
  1. Monthly Budget (A cash flow budget)
  2. Weekly Budget
  3. Stock Budget (This is a Wealth Budget which is a stock, not a flow like others)
  4. Yearly Budget
  5. Savings Plan
  6. Events Plan
  7. Incentives Plan
  8. Lifestyle Adjustment Plan
* Incentives and Lifestyle planning are optional. Incentives planning is generally recommended, and lifestyle planning is only recommended as needed.
* It’s important to remember why we budget. The yearly, savings, and events, and incentives plans represent planning for various goals:
  + Paying off debts is one key goal.
    - The yearly budget gives us an ETA until debts are paid off, and then it helps us figure out positive wealth over time after those debts are paid.
  + Financial comfort, independence, or retirement is the next goal.
    - The savings budget helps us accelerate that ETA to pay off debts by identifying opportunities for increased cash flow or positive interest. This budget also helps us translate wealth into an income estimate for retirement planning.
  + After we are financially stable or comfortable, our final broad goal is to pursue our life’s purpose(s). Event planning can be used to support that pursuit, in any of its many forms.
    - Everything which is not a regular part of your budget can be considered an event.
    - Retirement can be treated as an event. Buying a house or a new car is an event.
    - Giving to charity, starting a business, going on a mission, and adopting can all be considered events.
    - Small, irregular cost or income windfalls can be considered events.
    - Birthday spending, Christmas spending, bonus income, going on vacation, or paying taxes are all examples of events.
    - Giving to charity on a one-time basis is an event, but if it’s an ongoing sponsorship it should be moved into the budget.
* Broadly, there are two ways to improve your budget. Increase earnings or cut costs.
  + Increasing earnings can be done well by gaining new skills and furthering or transitioning your career.
  + Maybe I need to create a career plan framework and fit that into the budget with expected pay increases and so on.
  + Increasing revenue with myriad projects can be done for now under the savings budget, where some project is treated as an investment.
  + For example, going back to school or creating a startup can be treated as an investment with some dollar cost, time cost, risk, and expected return on investment.
* Once we collect a sufficiently large sample of weekly or monthly data we can start to do some forecasting!
* Doing a budget and handling money well are not the same thing, although they do help each other. If you are already good with money you can start to benefit from learning this budget method in 3-5 months. If you are bad with money we can work on that too, but don’t be surprised if that behavioral change takes much longer. It can take you perhaps 3-5 years to get good with money and that wouldn’t be abnormal.
* If you are looking for a budget method which will fix your life in two months, this is not it. I expect you will probably mess up the budget for the first couple months and my working response to that issue is that it is fine and don’t sweat it.
* Having done the budget for a couple months, you can improve the budget each time. By the third month you should have a decent budget. From then on you can use my golden rule of budgeting: When in doubt, budget whatever you budgeted last month, unless you have a good reason to change the budget.
* Consistency is key in budgeting. Some things can be budgeted in different ways. For example, you could create a budget line for coffee and budget your morning coffee, or you could include it in your eating out budget, or include it as part of your spending money budget. Any of those is fine as long as you keep measuring it the same way from month to month. You can’t improve if you keep shifting it around and all of your numbers get crazy and incomparable like apples and oranges.