

F1 – Project-Stage1: Gearing up

TCHE322

Lawrence et al (2011). Chapter 1

Thomas (2009). Chapter 1

CFP Handbook (2015). Chapter 6

Lecture of Shahnawaz Ali

Schedule of lectures

Project topic covered

- The rewards of a sound financial planning
- The financial planning processes
- Setting financial goals

Groupwork project activities

- Group formation
- What-Why-When-How activities

Rewards of Sound Financial Planning

- Improving your **standard of living**
- Spending money wisely
- Accumulating **wealth** – an abundance of money and other financial resources.

Financial success – achievement of financial aspiration.

Financial security – being able to fulfil any needs and most wants.

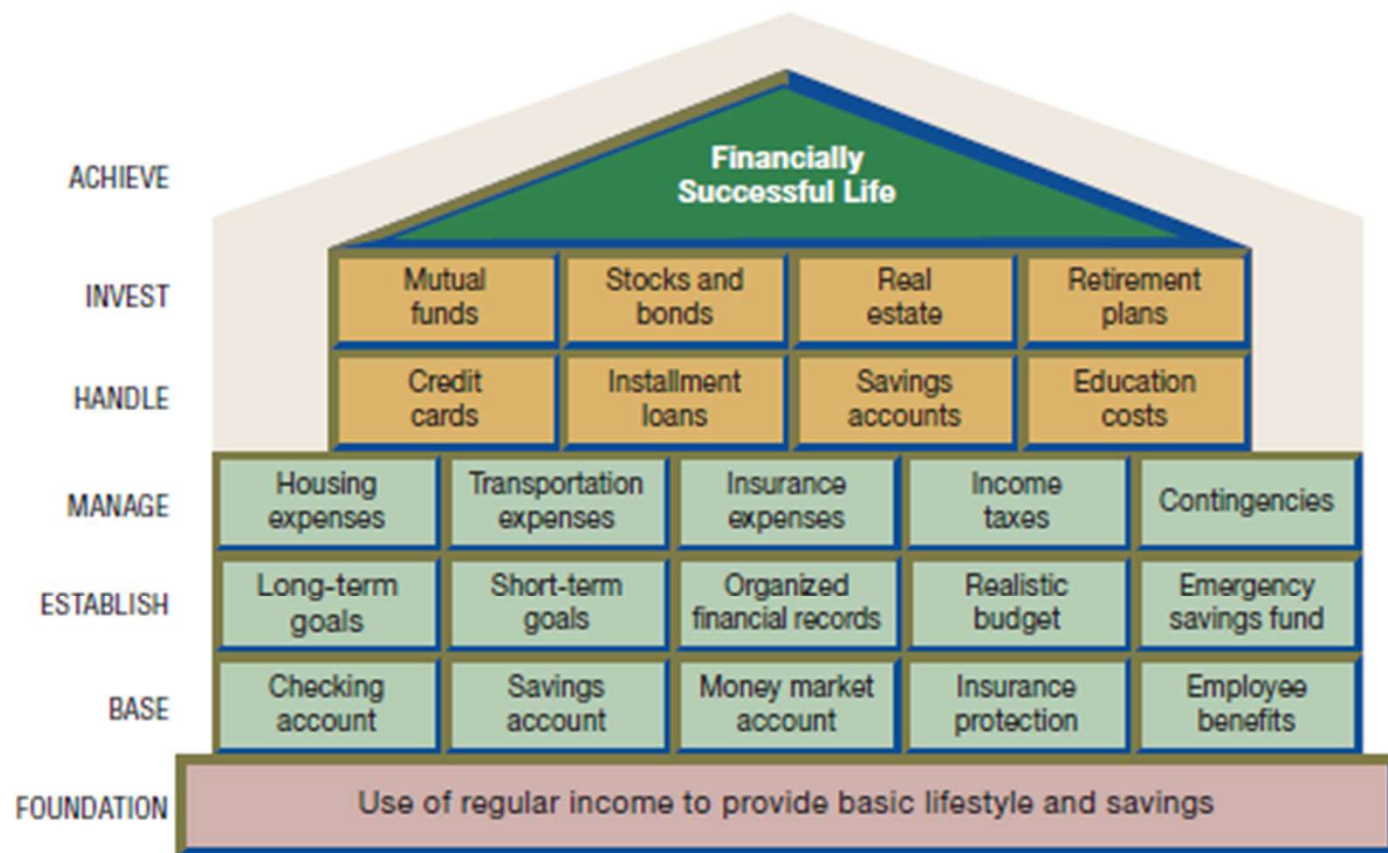
Financial freedom – the state where work is an option, you choose.
Not compelled to opt.

Exhibit 1.1 Organizational Planning Model



Figure 1.1

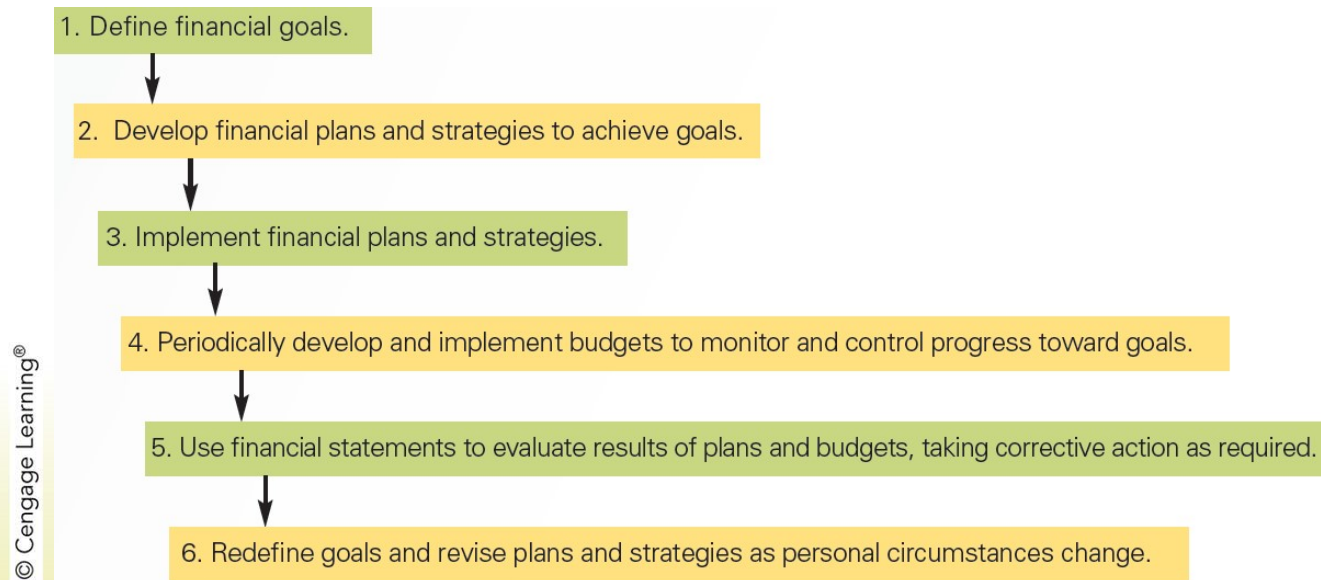
The Building Blocks of Your Financial Success



The financial planning processes

- Systematic process that considers important elements of an individual's financial affairs to fulfill financial goals
- The process translates personal financial goals into specific financial plans, which then helps you implement those plans through financial strategies.

Exhibit 1.3 The Six-Step Financial Planning Process



The financial planning processes

The personal financial planning process as defined by the *Financial Planning Practice Standards*.

From the financial planners' perspective

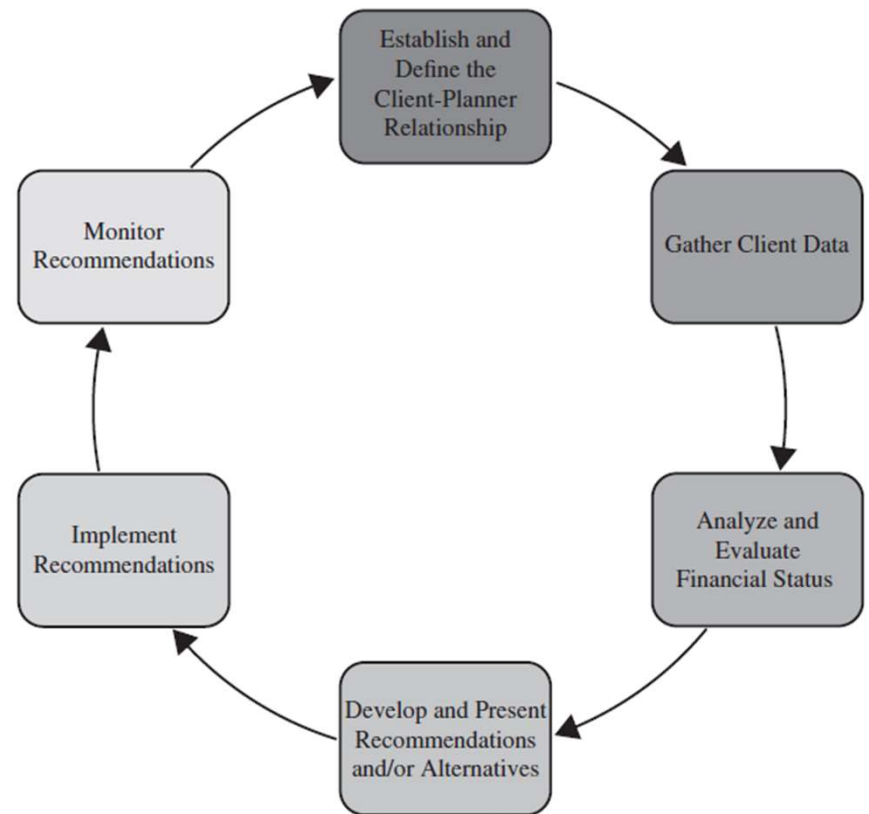


FIGURE 6.1 The Systematic Financial Planning Process

Breakdown the financial planning processes

Develop/gather data of financial goal

Is it more important to spend your money now or to save for the future?

Would you rather get a job right after high school or continue your education?

Will your chosen career require additional training or education in the future?

Do your personal values affect your financial decisions?

Values – Beliefs and principles you consider important, correct and desirable

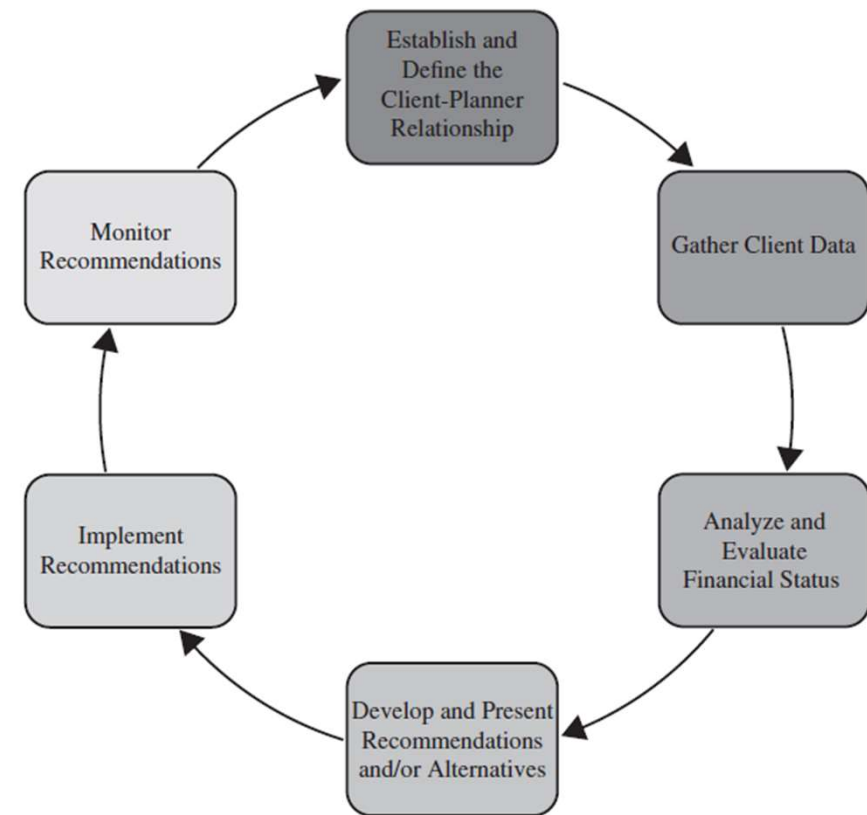


FIGURE 6.1 The Systematic Financial Planning Process

Breakdown the financial planning processes

Develop/gather data of financial goal

NEEDS VS. WANTS

NEEDS

Something you must have to survive

- Food
- Clothing
- _____

WANTS

Something you desire or would like to have or do

- _____
- _____
- _____

Personal values and financial decision making

Values – Beliefs and principles you consider important, correct and desirable

Talavera, O., Yin, S., & Zhang, M. (2018). **Age diversity, directors' personal values, and bank performance.** *International review of financial analysis*, 55, 60-79.

Delis, M. D., & Mylonidis, N. (2015). **Trust, happiness, and households' financial decisions.** *Journal of financial stability*, 20, 82-92.

Naeem, M. A., Farid, S., Faruk, B., & Shahzad, S. J. H. (2020). **Can happiness predict future volatility in stock markets?.** *Research in International Business and Finance*, 54, 101298.



Financial Goals

- Results that an individual wants to attain
- Utility and cost are to be considered when evaluating alternative qualities of life, spending patterns, and forms of wealth accumulation
 - *Money and utility are linked to psychological concepts of values, emotion, and personality*
- Financial planning is an important part of the conflict resolution process



Target Dates on Financial Goals

- **Goal dates:** Target dates in the future when certain financial objectives are expected to be completed
- Long-term goals
 - *Indicates wants and desires for a period covering about 6 years out to the next 30 or 40 years*
- Short-term financial goals
 - *Set each year and cover a 12-month period*
- Intermediate goals
 - *Bridge the gap between short- and long-term goals*

Breakdown the financial planning processes

Evaluate current financial status

Financial statement and ratios

Income statement:

monthly income,
monthly expenses

Balance sheet:

assets, including savings,
debts

➤ Your current net worth

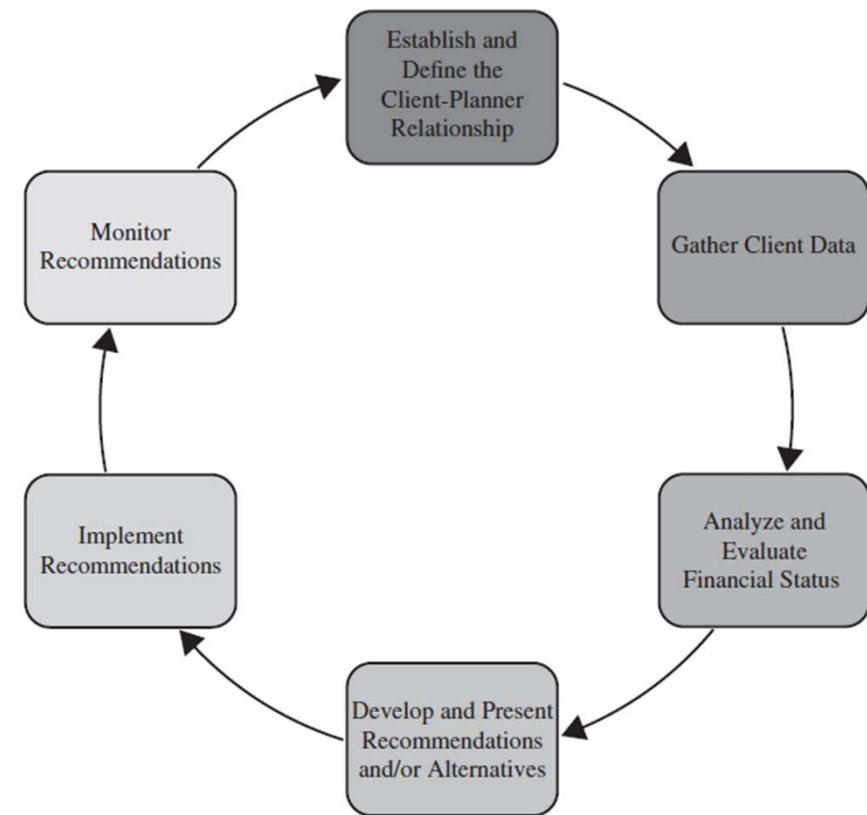


FIGURE 6.1 The Systematic Financial Planning Process

Breakdown the financial planning processes

Develop and evaluate alternatives

It is impossible to make a good decision unless you know your options

Consider the consequences and risks of each decision you make

➤ ***Make the decision on the planning***

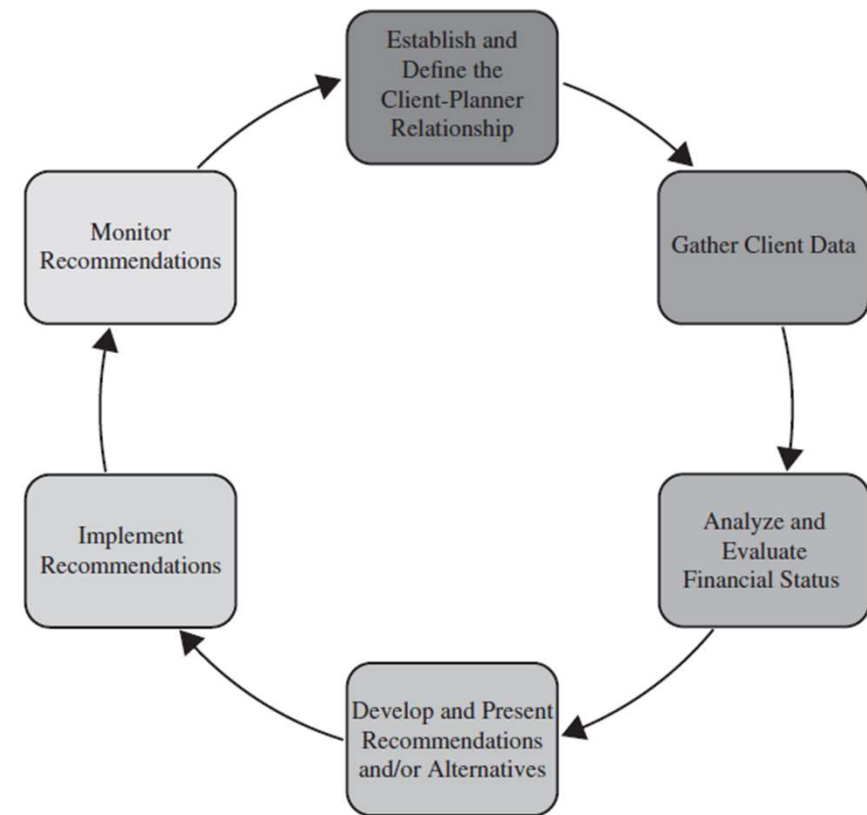


FIGURE 6.1 The Systematic Financial Planning Process

Opportunity costs and trade-off in decision making

Opportunity costs:

value/benefits of the next best alternative that must be foregone

it is what is given up when making a choice instead of another option

- *Choosing involves knowing what you would gain and knowing what you might give up*
- *Personal opportunity costs vs. financial opportunity cost*

Opportunity costs and trade-off in decision making

➤ **Personal opportunity costs vs. financial opportunity cost**

- *Personal opportunity costs* – making choices about how to spend your personal resources, health, time...

Do you study for a test or go to a concert you were invited to?

Not likely to do both because people have a limited amount of time

- *Financial opportunity cost* – making choices about how you use/spend your money

Do you buy a Iphone 15 for \$2,000 pus tax or do you save your money?

Opportunity costs and trade-off in decision making

Opportunity costs:

value/benefits of the next best alternative that must be foregone

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- *Choosing involves knowing what you would gain and knowing what you might give up*
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Evaluating risks – when making a financial decision, you also accept relevant financial risks.

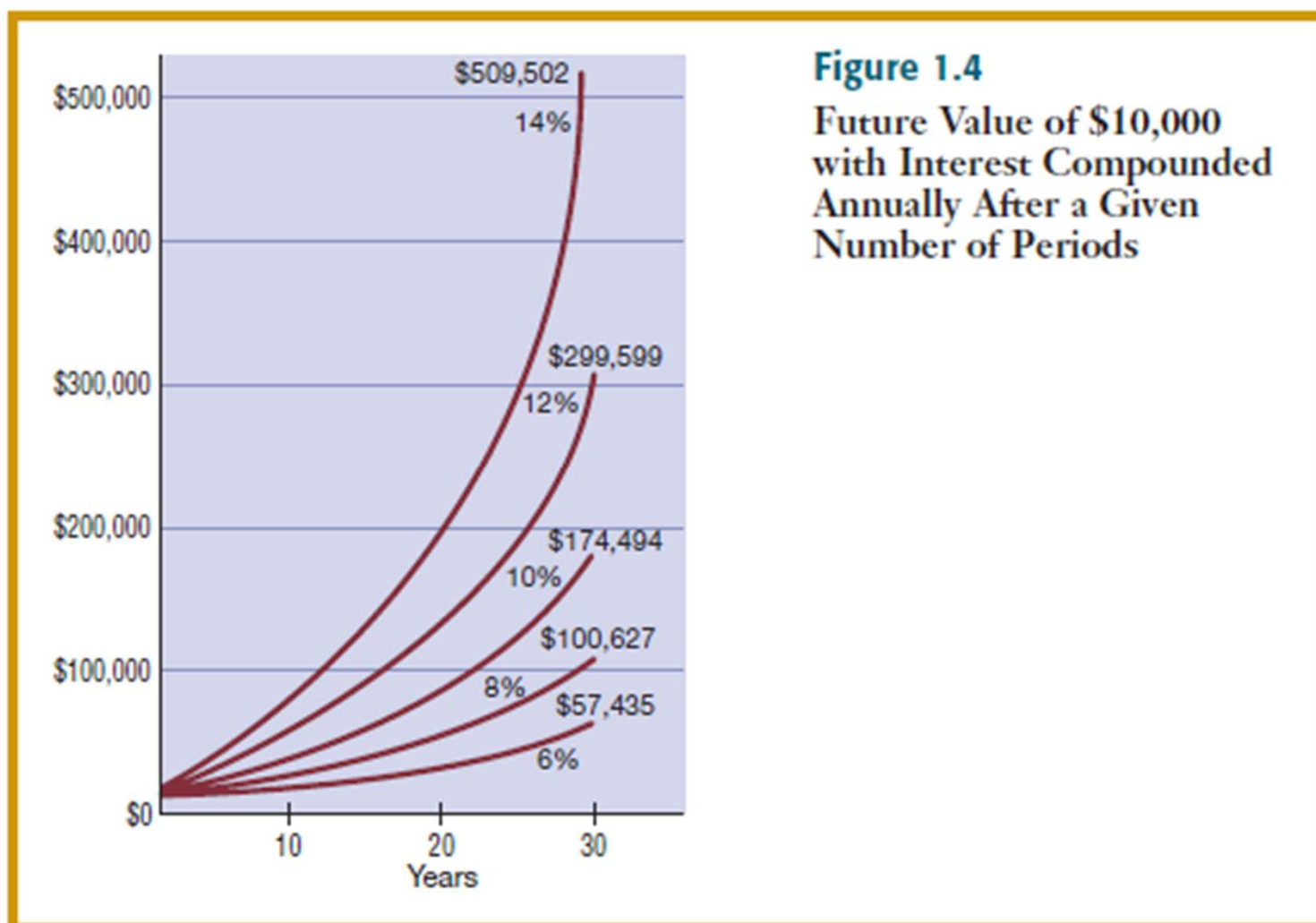
Marginal analysis in decision making

- *Utility* – the ability of a good or service to satisfy a human want
- *Marginal Utility* – Extra satisfaction from one more incremental unit of a good or service
- *Marginal cost* – Additional cost of one more unit of some item

Income taxes in decision making

- *Marginal tax rate* – Tax rate at which your last dollar earned is taxed
- *Tax-Exempt income* – Income that is totally and permanently free for taxes
- *Tax-Sheltered income* – Income exempt from income taxes in the current year

Time value of money in decision making



Breakdown the financial planning processes

Create a plan based on the decision

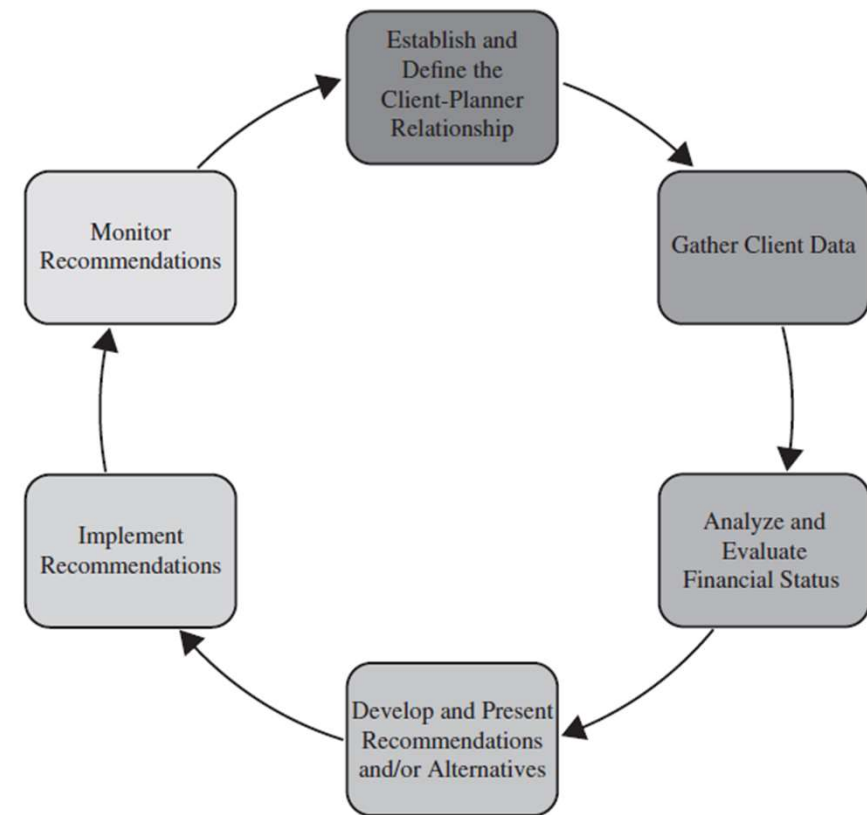
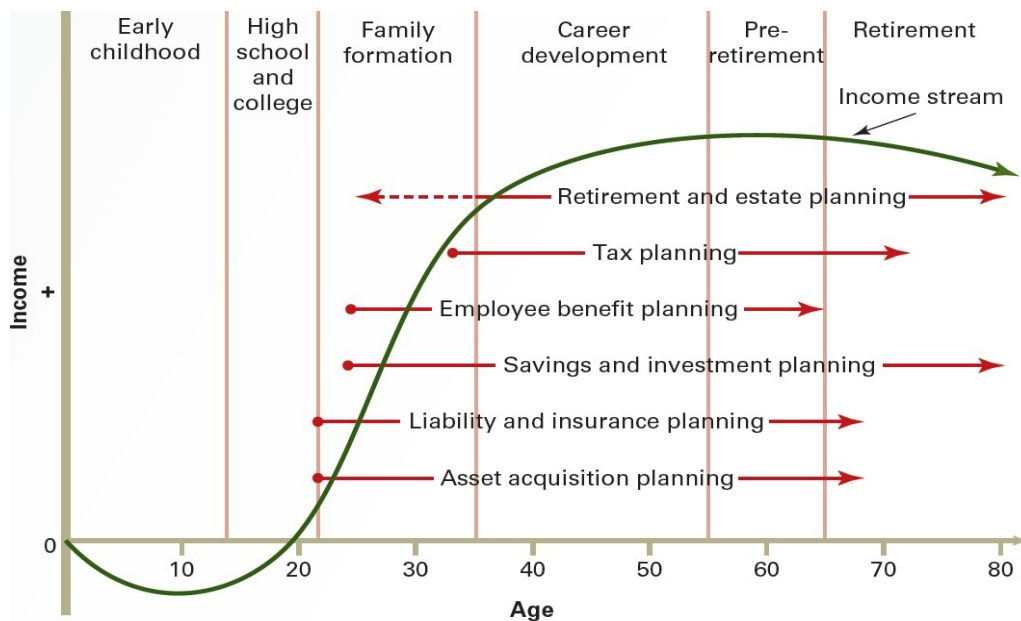
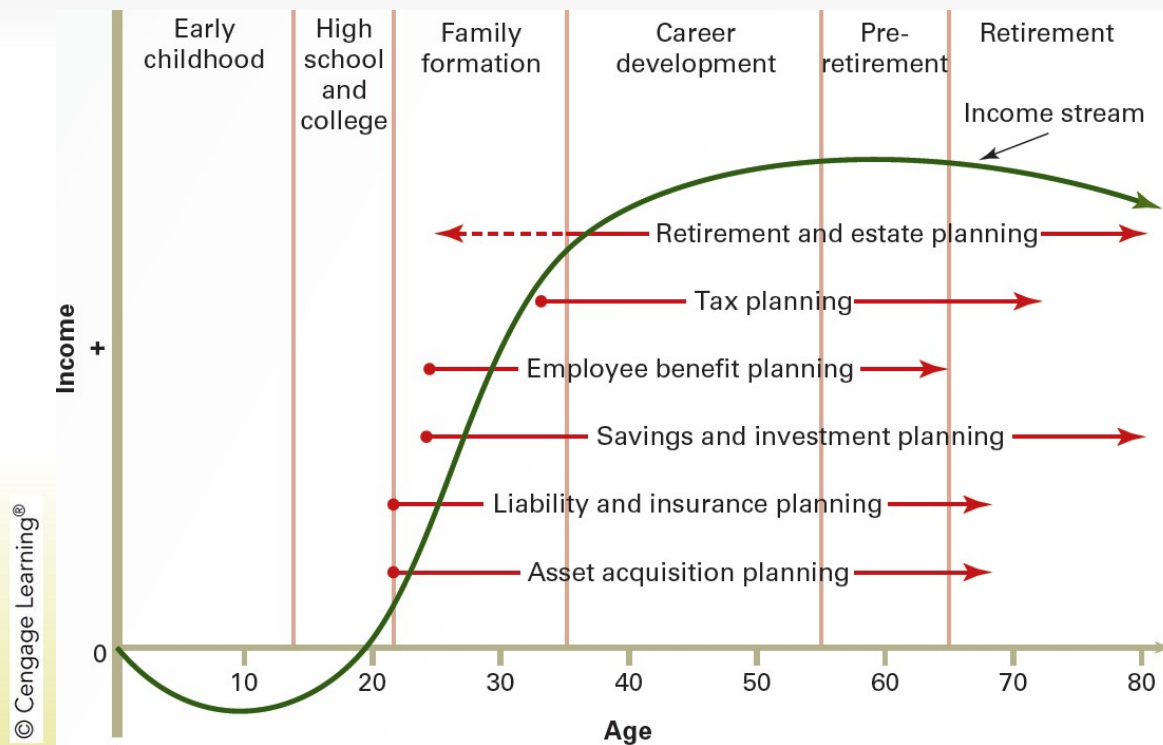


FIGURE 6.1 The Systematic Financial Planning Process

Exhibit 1.4 The Personal Financial Planning Life Cycle



Breakdown the financial planning processes

Implement – review and revise the plan

As you get older, your finance and needs will change

Your financial plan will have to change as well

Could consider re-evaluating and revising your financial plan (if necessary) every year

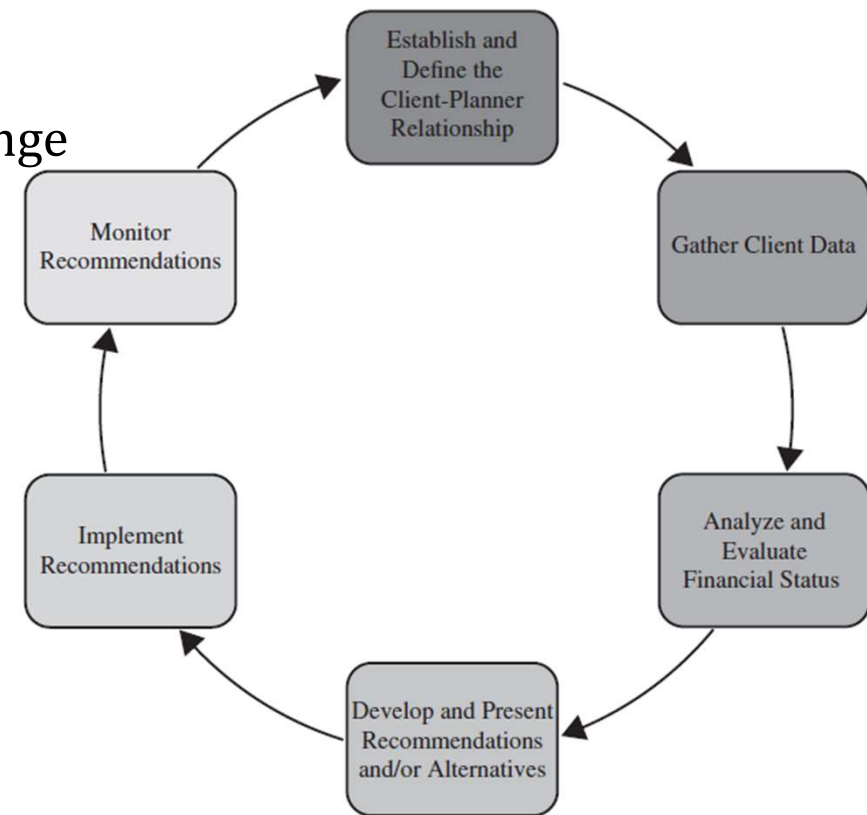


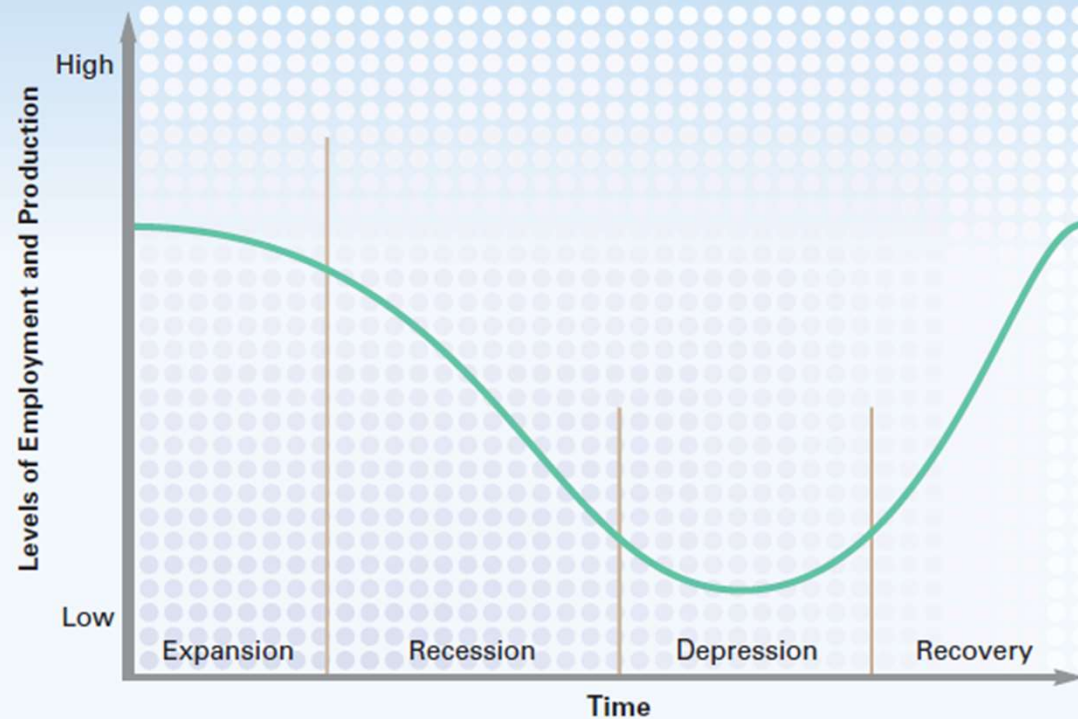
FIGURE 6.1 The Systematic Financial Planning Process

How the Economic Environment Will Affect Personal Finance

Exhibit 1.11

The Economic Cycle

The economy goes through various stages over time, although real depressions are extremely rare. These stages tend to be cyclical and directly affect the levels of employment and production.



Phases of Economic Cycles

Expansion

- Real GDP increases until it hits a peak

Peak

- Expansion ends and a contraction begins

Contraction

- Real GDP falls

Trough

- Contraction ends and an expansion begins

Exhibit 1.7 The Business Cycle



Source: Adapted from William Boyes and Michael Melvin, *Economics*, 8th ed. (Cengage, 2011), p. 135.

Economy

Inflation

- General price level is increasing

Consumer price index (CPI)

- Measure of inflation based on changes in the cost of consumer goods and services

Purchasing power

- Amount of goods and services that each dollar buys at a given time

How the Economic Environment Will Affect Personal Finance

It is important to

- predict the future directions for the Economy
 - GDP
 - Index of leading economic indicators ([LEI](#))
- predict the future directions of prices and inflation
 - Consumer price index
 - Personal inflation rate – the rate of increase in prices of items purchased by a particular person

Essential Information of personal financial plans *

1. A summary of the goals
2. Significant assumptions and justification
3. Estimates
4. Recommendations
5. A description of limitations on the work performed
6. The recommendations in the engagement should contain qualifications to the recommendations if the effects of certain planning areas on the client's overall financial picture were not considered.

** Adapted from Paragraph .35, Statement on Standards in Personal Financial Planning Services No. 1*