

Personal Finance

In this article, we will explore the concept of personal finance, delve into its five fundamental areas, and provide valuable tips for effectively managing one's financial well-being.

Personal finance refers to the management of an individual's financial resources and decisions. It encompasses all aspects of an individual's financial life, such as budgeting, banking, insurance, mortgages, investments, and retirement, tax, and estate planning. The primary goals of personal finance are achieving financial security, meeting current and future financial needs and desires and ultimately reaching financial freedom.

Personal Finance is about meeting your personal financial goals. These goals could be anything – strategic decisions on buying or renting a house, planning for retirement or even saving enough money for a new car. It depends on your income, spending, saving, investing, and personal protection.

5 Core Areas of Managing Personal Finance

Income

Spending

Saving

Investing

Protection

Income

Income is all the money you bring in. This includes salaries, wages and other sources of cash inflow. Income is the starting point of personal finance. It is the cash flow that enables you to spend, save and invest.

Spending

Spending is the outflow of cash. Spending is everything an individual spends their income on. This includes rent, groceries, hobbies, eating out, travels, entertainments and whatever needs money to be acquired.

(Spending < Income !!!)

Saving

Saving is the amount that is left after you spend and you put it aside for future spending. But you should bear in mind that keeping money for a long time is very useless because it loses purchasing power (depreciates), particularly in time with high inflation, which is why, depending on your capabilities, investing it could be a better idea.

Investing

Investing is the act of buying financial assets such as stocks and bonds, and other resources with the expectation of generating a profit over time. Investing does come with risks, as not all assets appreciate and can lead to losses.

Protection

Financial protection refers to the measures and strategies individuals put in place to safeguard their financial well-being and minimise the impact of unforeseen events or risks, such as illnesses or accidents. Protection includes health insurance, estate and retirement planning.

Even if it is easy to track your spendings and savings, investing and other personal financial strategies may require the help of a professional. But if you want to better manage your finances without the services of a third party, here are some advice you could use:

1) Budgeting

Having a budget is crucial for staying within your financial limits and setting aside sufficient funds to achieve your future objectives. The 50/30/20 budgeting method is a great way of separating your income and it breaks down like this:

- 50% of your net income (after taxes) should be allocated to living essentials, such as rent, groceries, and transport.
- 30% should be spent on having fun and going out. For example, shopping, eating out and entertainment.
- 20% should be saved for the future- paying debt and for emergencies- or investing.

2) Limit and reduce debt

A very important rule "Don't spend more than you earn" is crucial in order to keep debt from getting out of hand. Nevertheless, debt can be an advantage when you use it carefully in order to benefit from it, for example acquiring an asset through a mortgage.

Another key rule would be "Only borrow what you can repay". Not being able to pay debt in time can lead to losing assets, bad credit scores, frozen bank accounts and other drawbacks keeping you away from financial well-being.

3) Maximise tax avoidance

Be careful, don't confuse tax avoidance/tax optimization with tax evasion. Tax evasion means concealing income or information from tax authorities to reduce tax, and it's illegal whereas tax avoidance means legally reducing your taxable income through tax code loopholes and other legal means.

A simple example of tax avoidance is if you (as parent) rent an apartment. You can have your child as the owner of the apartment so in papers it is your child that collects the rent and not you, "reducing" your income and therefore your income taxes.

To sum up:

Personal finance involves the effective management of your money to cover your current expenses and save for the future. It encompasses a wide range of areas, including handling expenses and debts, saving and investing wisely, and planning for retirement. Additionally, it encompasses strategies for protecting yourself through insurance and building wealth.

Comprehending how to oversee your finances is a crucial life-planning skill that can position you for a debt-free life. It empowers you to take control of financial pressures and provides a means to handle unexpected and costly surprises that life may present.

Sources:

<https://www.investopedia.com/terms/p/personalfinance>