ASK THE EXPERT

Finance

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4 Steps to Fix your 'Financial Leakage'

There are four variables (pillars to financial success) that will affect your long-term financial success, of which you can control or influence only three. Yet so many people think they are powerless to affect real change, which could not be further from the truth.

These four 'pillars' to long term financial success are:

Time	Time investing. Time in the market. Time that you spend working. Time you spend in retirement.
Spending	How much it costs you to live? Where are your dollars going?
Income	How much you earn from your business and/or wages.
Investment returns	The quality of your returns over time, including dividends, rental returns, growth in the investment value etc.

The element that we are going to focus on here is the spending category – which is where the concept of 'financial leakage' comes into play.

I want to take you back to when I was a mother of two teenagers, being the main breadwinner of our family, paying for private school education, a mortgage and running a business. There were many expense items that I could point to that were large as a proportion of our household expenditure (as you can imagine). For the most part, they were things that my husband and I (well let's face it me!) had made some very deliberate and conscious decisions about. However, there seemed to be a lot of money going out that did not fall into that category. This is called financial leakage. For me, this financial leakage was in untraceable spending with cash. It was the fact that if

I had $100 in my wallet at the beginning of the week, it would be gone at the end of the week. I could not quite pinpoint where it had gone, and it certainly was not adding to my quality of life in any significant way. It was things like buying lunch once or twice a week, buying a coffee whilst waiting to pick the kids up from basketball training, buying some snacks from the canteen in between games at basketball stadiums on the weekend, and the inevitable items that the children needed.

It seems to be an innate aspect of the human condition that families and individuals, regardless of their family dynamic, encounter these financial leakage issues.

Just to be clear, I do not mean to say that any expenses of this nature will always be financial leakage. For some, buying a cup of coffee a few times a week is important to them because they really enjoy it, and it may be an opportunity to catch up with friends and colleagues – buying a coffee in this context would not be financial leakage. The distinction being that it is actually very important to them and the ritual surrounding the coffee is adding to their quality of life in some way.

So, it is not the item itself, but rather your relationship to it, that will define it as financial leakage.

Therefore, the key to managing your personal expenditure is to get control of your financial leakage. This is not to say that we should eliminate financial leakage altogether (I think that this is too hard and would take too much energy), but to keep it in control. Doing this will make a significant difference over time to your financial success.

Where do you start?

> **It is not the item itself, but rather your relationship to it that will define it as financial leakage**

Step one: be more mindful about where your money is going

Start recording where you spend your money. Reducing how much you use cash will make it easier to track. Go back over the past three months of your bank and credit card transactions and categorise your expenditures. Some banks have reports that you can use that may help you here – but I think to be more mindful and see the patterns of expenditures, you are better doing this process yourself initially. I caution you to be careful with your emotions as you go through this process. It is very easy to have feelings of overwhelm, guilt, judgement, and blame, all of which are normal, but they will not serve you, so tell these emotions to ‘stand down’.

Step two: find one or two expenditure items where you think there may be some financial leakage and think about what you will do differently to try to manage this.

I have some examples below.

Cash expenditure	Limit yourself to only having $20 in your wallet at the beginning of the week (in my example this would save $80 per week). And then only top this up on a set day per week.
Dining out	Dining out may be the result of: • being time poor • disliking cooking, or • not planning Work out why you tend you dine out, then look for ways to resolve the underlying issue. Allow yourself to still have some dining out options but only once a week perhaps. You set the rules. Do not let dining out be the default setting.
Shopping	Grocery shopping can be a financial leakage point because it always seems to cost so much each time you go to the supermarket. Once again, think about why this is – then make some changes to see if this helps. For me it is planning my meals for the week ahead and then doing the shopping online, therefore avoiding the special aisles or the items at the checkout that jump into the trolley. I have also seen families whose leakage point is that they go to the supermarket each day. Not only does this create a financial leakage point but impacts on time as well.
Memberships and subscriptions	Always start with the easy things. Cancel those subscriptions that are not being used, or are only used occasionally. Do you really need to subscribe to Foxtel movie channel, Stan and Netflix all at once? The number of times that I have unsubscribed from something that my children 'needed', and they only complained about it not being available six months later!
Finance commitments	Credit card payments, personal loans, car loans, home loans. It may be helpful to consolidate your debts into the lower interest rate environment of your home loan where you can – but only if you can keep control of these items and not let them build up again over time. Shopping around for a lower interest rate on your home loan can also mean some good savings. If you have trouble controlling your credit card debt, refer to the blog link for some more ideas on this. www.tagfinancial.com.au/blog/credit-cards-friend-or-foe

Step three: create a new pattern of behaviour around the areas you have identified so that you can keep track of how you are going with this change until it becomes a new habit.

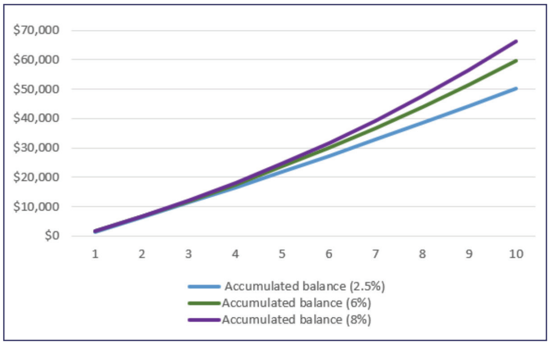
Remember only to tackle one or two elements at a time otherwise it will become too overwhelming. After some time, once the first ideas are starting to work, start working on the next element. I suggest having a monthly meeting with yourself (and your family if appropriate) to talk about these issues, commenting on the patterns of expenditure and brainstorming ideas of what to change next. If you have children, then this may also become a helpful learning opportunity, offering them tools about mindful spending, and preparing them for the future.

Step four: redirect the money that you target for your financial leakage repair project into something more meaningful.

This will make the results of your efforts more tangible. Set up a separate bank account to accumulate the additional money. Perhaps set an achievable and measurable goal to aim for. For example, my husband gave up smoking many years ago, and used this opportunity to save the money he would have spent on cigarettes to buy his first smart TV. He kept taking the cash out of the bank that he would normally have spent and put it all into a large money tin which allowed him to physically see his savings grow.

Think about how you might be able to apply this same concept to change your habits. Remember time is one of the other four pillars to financial success, so using these habit changes and continuing these patterns over a long period of time will be powerful. For example, the below graph shows the cumulative effect of saving just $100 per week over a ten year period.

Rate of return	Balance at Year 10
2.5%	$ 50,285
6.0%	$ 59,725
8.0%	$ 66,140



Reflect on what is important to you and start to take action that is true to your values. Action is the key to your success.

Resources that might be helpful for you

For some great articles and tools to assist with financial literacy, including a budget planner that will come in handy for these strategies, go to www.moneysmart.gov.au.

For a quick comparison on home loan interest rates that could save you thousands, go to tag.comparensave.com.au.

For more articles and videos about financial affairs for business owners, superannuation and investing, go to www.tagfinancial.com.au/blog and www.tagfinancial.com.au/videos.