What is finance for?

1. Functional POV: financial system
   - Overcome asymmetric info
   - Price info
   - Control risk/uncertainty
   - Transfer resources
   - Pooling of funds
   - Exchange of goods and services
2. Outcome-oriented POV

	Present	Future
Security	Day-to-day	$ shock
Freedom of choice	Everyday life choices	$ goals

Financially included: has insurance, active transaction acc, can raise $2k in 24 hours

What influences $ wellbeing:

Social economic environment → personality, knowledge, decision context, available opportunity → behavior

Note: financial wellbeing = how satisfied you are w/ your $ situation

WEEK 2

ASIC (Australian Securities and Investments Commission): police, educate

Credit issues

- Too high interest % (19-20%)
- Payday loans → higher than credit card. Why? Short-term. Unsecured.

Financial planning process:

1. Collect + assess $ data of client
   Stocks and flows: BS, cash flow
2. Determine objectives + goals
3. ID any $ problems: no insurance, massive negative cash flow, high credit card debt
4. Written plan w/ alts and recs
5. Recs + implementation
6. Review

Note: step 2+3 → analysis of clients' needs

Current cash flow → current net worth → $ value of future needs

Financial planning complication: unrealistic expectations

Balance Sheet:

- Financial position: assets (cash, superannuation, bonds, house). Liabilities. Net worth/equity.
  Note: net worth = amount of $ after selling all assets at fair value and pay off liabilities

- To track progress towards goals
- Set, monitor, revise $ plan

Cash flow statement:

- Measures net cash: tracks inflows/outflows
- Gain budgetary control over $ outflow
- If cash surplus, rec: ++ savings, investment, - - debt
- If cash deficit: cover by drawing, borrowing, selling assets

Difference between income statement and cash flow statement: in P/L, accrual accounting. In CF, cash accounting.

Household expenditures from most to least:

- Poorest: rent → food → transport
- Richest: transport → rent → food/recreation

High $ stress, due to: unemployment, illness, low income, unfair $ practice, addiction, divorce

Old age poverty → age pension averages around $22k/year

Monitoring financial progress

- Solvency ratio = $\frac{Net\ worth}{Assets}$
  "How much buffer" NEVER NEGATIVE or close to 0!!
- Liquidity ratio = $\frac{Liquid\ assets}{Current\ liabilities}$
  "How long we can pay current expenditure w/ liquid assets"
- Savings ratio = $\frac{Cash\ surplus}{Inflow\ after\ tax}$
  "How much is available to put for savings"
- Debt service ratio = $\frac{Total\ monthly\ loan\ payments}{Monthly\ gross\ inflow\ before\ tax}$
  "Ability to repay debt"

Why household debt is higher in Australia then the rest? House prices in a 'bubble' → high mortgage repayments

Setting financial goals

Note: financial goals are set in $ value

- Short-term: < 12 months
  Cash budgeting → consistent w/ long-term
- Medium-term: < 2 years
- Long-term: < 5 years
  To be set first, eg retirement, inheritance, emergency $

Budgeting: cash projection based on forecasted cash flows

- Short-term financial planning report to help achieve $ goals
- Cash basis
- Stages: estimate $ inflows → estimate $ outflows → finalise budget

The need to fit in influences financial decisions