

Topic 7: Create a medium-term budget

After completing this topic, you will be able to:

- explain why a budget is important;
- explain how a budget might help you to avoid paying bank charges or interest;
- work out a budget for several months; and
- explain how direct debits and standing orders will help when budgeting.

What is a budget?

A budget is a financial plan for the future – whether that is the immediate, short-term, medium-term or long-term future.

Planning your finances means that you can afford to do the things that you want to do, while at the same time making sure that you cover all of your essential expenditure. People who do not budget properly can often end up in a mess, with their bills unpaid, unable to afford essential things such as food and transport, and often missing out on good fun with their friends because they have run out of money.

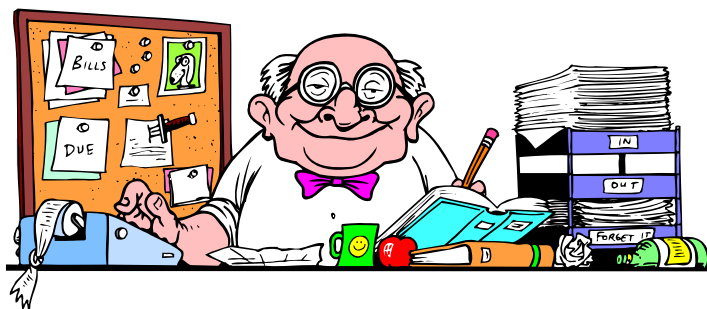
Working out a budget

In order to work out your budget, you need to make a list of all of your essential expenditure. These items are not the same for everyone. If you own a house, then you have to include household bills in your list of expenses, and rent or mortgage payments. If you live with your parents, the list of essential expenses will be shorter, because your parents will pay for most of the things that you need.

Once you have made a list of the things for which you *need* to pay – that is, your essential expenditure – then you can see what is left for the things that you *want* – that is, non-essential expenditure.

Essential expenditure includes such things as:

- rent;
- electricity;
- gas;
- telephone;
- any loan repayments;
- insurance;
- fuel or bus fares;
- food;



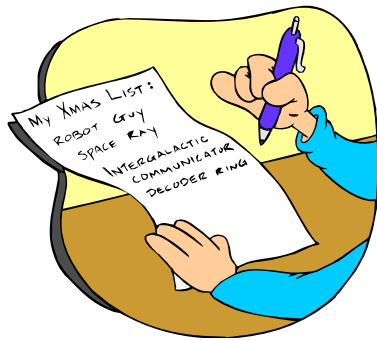
- books and study items; and
- some clothes.

Non-essential expenditure includes such things as:

- trips to the cinema;
- holidays;
- fashion accessories;
- coffee in town with friends;
- a day out shopping; and
- meals in restaurants.



Can you think of some more essential and non-essential items of expenditure?



Activity 7a

If you do not have financial plan, think about the problems that you might have as a consequence.

How might the lack of a plan result in extra expenses?



Case study

Giorgio has worked out a monthly budget for his first week at work. He has a job paying £300 a month.

It is broken down into weeks, starting with his weekly income and then listing his expenses. Then there is a total for his expenses.

‘Net cash’ is income *less* expenditure for the week.

In this example, Giorgio’s opening balance starts off as zero. He then adds his net cash to his opening balance. His closing balance is carried forward to the next week.

Follow the entries carefully.

	Week 1	Week 2	Week 3	Week 4
Income	300	300	300	300
Expenditure				
Rent	75	75	75	75
Bus fares	25	25	25	25
Lunches	30	30	30	30
Weekends	45	45	45	45
Phone	10	10	10	10
Guitar lesson	15	15	15	15
Driving lesson	25		25	
Laptop repair		120		
Clothes			110	
<i>Total expenditure</i>	225	320	335	200
Net cash	75	−20	−35	100
Opening balance	0	75	55	20
Net cash	75	−20	−35	100
Closing balance	75	55	20	120



Activity 7b

Now you are going to work out a budget for yourself.

Imagine that you have just left school and started your first job. You earn £250 a week and out of this you have some regular expenses, as follows.

Weekly expenditure	£
Rent to mum	50
Train fares	45
Lunches	25
Weekends	60
Phone	15
Total	195

- *In your first week, you receive your wages. To celebrate, you decide to go to the cinema and out to eat afterwards, which costs you £25. You also have to pay a dry cleaning bill for £10 – because you spill ketchup all over yourself.*
- *In your second week, you know that you will have to pay the deposit on a holiday to Majorca with friends, which will set you back £90.*
- *In your third week, you would like to buy some new clothes and you set aside £150.*

There are four weeks in January.

Draw up a budget that shows your expenditure from week to week, to show how you can afford your new hectic lifestyle.

One important line to work out is the ‘net cash’ each week – that is, how much you plan to have left at the end of the week, which is calculated as:

$$\text{Income} - \text{Expenditure} = \text{Net cash}$$

After this, you have to work out how much money will be left in your bank account. This is called the ‘closing bank balance’ and is calculated as:

$$\text{Opening bank balance} + \text{Net cash} = \text{Closing bank balance}$$

- f) *If this were your budget, how would you deal with the financial problem that it is suggesting?*

NOTE: *This budget is for a person who is living at home and paying rent to their family. If you want more practice at working out a budget, your teacher will have some more examples.*

When you move away from home, some of your expenses increase and you will have more of them, such as bills for electricity, gas and water. You may also have to budget for a longer period of time.



Activity 7d

Janine moves away from home in June and sets up her first flat. She is earning £1,100 per month. She is renting at £500 each month. She pays the following bills:

- *electricity at £80 each quarter (with the first bill due in September);*
- *gas, which she thinks will be £60 in the summer and which is also paid quarterly (with the first bill due in September, but the next bill due in December, which Janine thinks is more likely to be £120);*
- *water, which will be £30 each quarter;*
- *council tax, which will be £125 a month;*
- *a phone contract at £35 a month; and*
- *food, which will be £40 a week, so she thinks that she will plan for £170 a month, but also add a bit for going out, making the total food for each month £220.*



She has not planned for clothes, but thinks that if she puts £200 a month into a savings account, this will help her.

Using the sheet given to you by your teacher, try to work out Janine's budget.



Activity 7e

At the end of this topic, you will find the answer to Activity 7d. Look at the answer and discuss what the budget is telling us.

- a) Why is it a good idea to prepare this budget?**

- b) Look at the quarterly bills. Are these causing a problem?**

- c) Think about what will happen the next time the bills are due in March and then June. Can you think of something about which we thought in Topic 4 that would help Janine to solve this problem?**

- d) How might a standing order or direct debit help?**

Student budgets

Another group of people who have to budget carefully are students. This is because they get their money (that is, their grants) once a term and it has to last for ten weeks.



Activity 7f

Abbas is in his first term at university. He is living in halls of residence, so all accommodation costs and bills have already been paid. Below is a record of Abbas' spending during his first ten weeks.

Student expenditure for a term of ten weeks	Expense £	Balance £
Allowance		1,000
Week 1		
Freshers' Week (lots of money, but everyone spends loads that week)	200	
Food (including all of the stuff you forget to bring from home)	50	
At end of week		750
Week 2		
Books	60	
Food	35	
Going out	50	
At end of week		605
Week 3		
Food	35	
Going out with mates for someone's birthday	50	
Toiletries	20	
At end of week		500
Week 4		
Food	35	
Cleaning stuff (flat inspection)	10	

Mobile contract	30	
Last-minute gig	15	
At end of week		410

a) Can you work out how much Abbas has spent during his first four weeks at university?

b) How much does he have left to spend during the remaining six weeks of term?

c) Can you see what is going to happen here?

d) Discuss how Abbas might plan to get through the next six weeks. What would you do if you were Abbas? (You should include in your discussion the ideas about essential and non-essential expenditure that we met in the previous topic.)

e) Why should Abbas start off his first term at university with a budget?

f) What items of expenditure might Abbas have cut out if he had prepared a budget?

Tools that help with budgeting

Budgeting is much easier to do if your expenses (that is, your outgoings) occur with the same frequency as your income. For example, if you get paid once a month, it is much easier if your bills are paid monthly. This is why standing orders and direct debits are so useful.

If you were to get your electricity bill and phone bill every three months, you would have to remember to put some money aside to pay the bill in the third month. If you were to fail to do this, you would have to pay the whole amount in the third month and perhaps may not be able to go out or do any kind of leisure activity that month, because you would not be able to afford it.

Insurance premiums are due every year, but most people choose to divide this by 12 and pay a bit every month, rather than have one big bill once a year.

If you do not spread your payments in this way, and you are not very good at planning ahead and saving up for bills that come once a year, you might not have enough money to pay the bill when it arrives. In this case, you may end up with an unauthorised overdraft – and there will be charges for this, making the situation even worse.





Review questions

1. What is an 'outgoing'?
2. What is a possible source of income?
3. How do you work out net cash?
4. How do you work out the closing bank balance?
5. What does 'opening bank balance' mean?

Learning activities



Internet

- Visit <http://moneysense.natwest.com/schools/students/> and complete the examples for budgets.
- Visit www.moneyadvice.service.org.uk, choose 'Tools and resources', then 'Budget planner'. Look at the headings and put some amounts into the planner.
- Type 'Budget planner' into an Internet search engine, making sure to select only UK sites. See how many there are. Choose a few and see how practical they are. How many of these are offered on the websites of financial providers?
- If you are interested in student finance, look at the planner available online at www.ucas.ac.uk



Group

In two groups, make up lists of incomes and outgoings for a four-week period. You can choose to do this for a person at university living on an allowance, or someone at work with a regular income. Include some regular outgoings that occur each week and some irregular ones that occur periodically, such as shopping or going out. Swap your lists with each other and draw up a budget table showing income, total expenditure, net cash, opening balance and closing balance.



Individual

Ask your parents, or a family friend, to give you the details of their household expenses. Do not forget to ask which bills are paid monthly and which ones are less frequent (quarterly or half yearly, or even yearly). Draw up a basic budget plan for them, including bills, food shopping, fuel or transport costs, clothes, going out, holidays, regular fees (such as golf club subscriptions or football season tickets, etc), and do not forget things such as birthday presents and saving up for Christmas.



Key points for Topic 7

You should now understand:

- why a budget is important;
- how a budget might help you to avoid paying bank charges or interest;
- how to work out a budget, and how to use the terms 'net cash', 'opening bank balance' and 'closing bank balance';
- how direct debits and standing orders will help when budgeting.