

Getting to the Heart of Your Financial Health

The Envelope System Helps You Take Control of Your Monthly Cash Flow

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Understanding and controlling your monthly cash-flow situation is at the very heart of your financial health. The first step is to determine the cash flow (budget) that is required to cover your fixed and discretionary monthly expenses. Having an effective cash-flow system is similar to living a heart-healthy lifestyle—by addressing both effectively—you reap the enormous benefits associated with quality of life, and worry a lot less!

For those who need a straightforward way to get a handle on their monthly finances, the envelope system is for you. The main premise of this system is very simple: don't buy what you can't afford. As reasonable as this sounds, not many people follow this principle.

We are bombarded by ads trumpeting: “Buy Now, Pay Later”; “Don't Pay a Cent Event”; or “Refinance Your House For Next to Nothing!” It is not uncommon for people to borrow to buy big-screen TVs, computers or even cameras. The envelope system is a simple, proven method that allows people to live within their means while still doing the things they want to do and enjoying life now!

The envelope system works like this: First, you list your household's monthly **net income** (after tax and deductions). For example, if the amount you receive in your bank account from your employer every two weeks is \$1,400.00, then your net monthly income is simply \$2,800.00. Don't worry about the extra two pays per year not being accounted for. Second, list all your monthly expenses, (visit www.noregretsbook.com for a free sample cash flow analysis worksheet).

You will find that many of your monthly expenses are relatively consistent and fixed, such as mortgage/rent, property taxes, utilities, retirement savings, goal savings, car loan/lease, etc. These fixed expenses should be automatically debited from your bank account. This puts most of your monthly cash flow on automatic pilot.

Make Discretionary Expenses Fixed

Many of your more discretionary expenses, such as clothing, gifts, groceries, home maintenance, and entertainment are somewhat optional and vary every month; for example, gift expenses are usually much higher around the holidays.

Start putting a fixed dollar amount to these discretionary expenses—make them fixed. Try and use a number that is realistic and that you would feel comfortable spending each month. For example, if you feel \$300 per month is a reasonable amount to spend on

entertainment, put that figure in the entertainment column. Do this with each category. When you get to the bottom of the list, add up all your expenses and deduct them from your net income. You should be running either a surplus (extra \$\$) or a shortfall (negative \$\$). If you are running a negative balance you should review and reduce where you can until you run a balanced budget. Remember, if you don't run a balanced budget each month, you will only continue to borrow to sustain a lifestyle you are not able to afford, and it will eventually catch up with you.

Implementing the System

Groceries are the one exception that cannot be radically reduced. They are not really optional, as we all need to eat on a regular basis. So, for groceries, if your monthly budget is \$600, then I suggest that with each pay (assuming you are paid bi-weekly) you take \$300 cash (yes cash!) and place it in an envelope labeled "Groceries." Use this cash to pay for your groceries.

Next up, set up envelopes for the other usual expenses. Label your envelopes as follows (you fill in the dollar amounts, these are just examples): Gifts (\$200 per month), Clothing (\$200 per month), Entertainment (\$300 per month), Home Maintenance (\$100 per month). You now know you have discretionary expenses of \$800 per month, or \$400 per pay.

When you receive your pay, place \$100 in the gift envelope, \$100 in the clothing envelope, \$150 in the entertainment envelope, and \$50 in the home maintenance envelope. Yes, it is a little cumbersome, but it works. And yes, you should physically put cash into the envelopes. Now what do you do? Anytime you want to do something under the Entertainment heading, such as order a pizza on Friday night, use the cash in that envelope. If there is no cash in the Entertainment envelope that night, unfortunately, that means no pizza tonight—so get cooking! Conversely, if you haven't used any Entertainment money in four months, you would have \$1,200 saved up. Reward yourself—perhaps go away for a golf weekend!

The Gift envelope will build, as this is a seasonal expense. Most of your spending will occur at certain times of the year, i.e., at Christmastime or on birthdays, so don't spend it on something else if you notice it's bulging with cash!

Clothing is similar to Gifts. We don't usually buy clothing on a regular basis. Again, only use cash from your Clothing envelope to buy clothes. If there is not enough money in the envelope to buy your outfit, then you'll just have to wait! If you really want that outfit, you could take some money from your entertainment budget, but that would mean a sacrifice on the entertainment front. It's up to you. If you are uncomfortable with the idea of having cash on hand in the home, then you could set up a separate account and have the bi-weekly amount automatically go to this account. But then you would have to track

how much of the balance in the account was for each expense, and this could prove quite time-consuming. Our clients have tried many methods, but the cash method (envelope system) works best.

Creating a Debt-free Universe

The envelope system makes money real again. By using credit cards, direct payment, cheques, “buy now and pay later plans,” money has become virtual, and it’s very easy to lose track of something that was never physically in your hand to begin with. Our society is far too focused on having everything we need or want *now*, which is why we are the most indebted civilization in history. If you don’t have the cash to buy it, the evident thing to do is to wait until you do. This was patently obvious to previous generations, but seems to be a new concept to people in their high-spending years today. And of course, there are whole industries that have a vested (and very profitable) interest in keeping you in debt.

As the worlds of marketing, industry, and banking have become more sophisticated, they have managed to convince us that debt is the norm and not the exception. Debt is the most influential factor that is stopping people from creating wealth and achieving their goals. If it is used without care, it will eventually catch up with you and cause your finances and possibly other areas of your life to collapse—I have seen several marriages end due to unwise borrowing.

The envelope system is the most effective method that allows people to live within their means while still saving towards their goals. Remember, this isn’t a punishment. By controlling and maximizing your monthly cash flow, you are succeeding at getting to the heart of your financial health. Whether you earn \$25,000 or \$200,000 per year, you can apply the envelope system, or a modified version of it, to your lifestyle.

No Regrets is available at Chapters Indigo and McNally Robinson bookstores across Canada.

For more information and for free resources visit www.noregretsbook.com

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