

Financial Capability Episode 3 – The financial decisions I need to make



Arun:

Hello, my name is Arun Aggarwal and welcome to 'My Future Finances'. In this series of six episodes, we'll be drawing on your experiences of managing money and exploring the key issues that affect your money and your futures. Now, these episodes are all British Sign Language enabled and will have captions and transcripts.

Arun:

Your journey towards financial independence:
What steps to take to be financially secure both now and in the future

Arun:

Welcome to the podcast Iona. We've got some big financial decisions to discuss and ones that many of us, myself included, feel ill-prepared to make.

Well, you're definitely not alone Arun and that's why I'm here to help.

Brilliant. We know that first jobs can be exciting, but also a little bit challenging and one big financial decision that we need to make is about pensions. Why are these so important?

Iona:

So, I would describe a pension as your future fund. You built it up over your working life so that one day you can retire and live off your pension, so you don't have to keep working, it's as simple as that. And today we're living longer than ever before, which is fantastic, but it also means that we need to start planning for retirement today because I think we all want to have choices in the future about how we'll spend our later lives. So, we have to start shaping those choices now by building up our pension fund. You get various types of pension but the main one that people need to know about, if they are a full-time employee, is their workplace pension. At the moment, you are automatically enrolled into your workplace pension from the age of 22 if you're earning over £10,000. Now you can opt out of that pension at any time if you really need or want to. But overall, it's a really good idea to stay in that pension because firstly, you're getting tax relief from the government and secondly, your employer is putting money into the pension as well as you. So, you're getting free money from your boss towards your future fund. You can't get better than that.

Arun:

I have to say the idea of living off one pot, for the rest of my life is really scary but I was chatting to a mate of mine and they were saying that they started paying into their pension straight away. Is it really going to make much of a difference if I start now to slightly later?

Iona:

Well, I think your friend is really smart because they figured out that if they start their pension as soon as they start working, that will make a huge difference to their pension pot. So, the general consensus is that you'll need a pension pot worth about £260,000 in order to have a comfortable retirement. Now, Arun I know

that sounds like a lot of money, but it actually boils down to about £19,000 a year which includes the state pension. And the reason why that figure doesn't sound very.

high is because it's going to be lower than your working income, because you're not spending as much money when you're retired, so long as you own your own home rather than rent it. So, in order to achieve that income, the pensions company, PensionsBee, figured out that you'd need to pay in £190 a month into your pension, including the employee contributions and tax relief, in order to retire at 66. Now £190 sounds pretty doable for most people, but if you started making contributions at 35, you'd need to pay in £270 a month. If you waited until 45, you'd have to pay in £430 a month. So, the longer you leave it, the more you'll have to pay in. Now, the reason for that is your pension is invested in the stock markets and it needs to be in the stock markets for as long as possible to give you the best chance of hitting that target for your future fund. History suggests that money invested in the stock market will grow much more than it would do in an ordinary savings account, but it needs that time to grow to really ride out the ups and downs of the stock market that we see all the time. So, the sooner you start contributing to your pension fund, the easier it will be to build your future fund.

Arun:

Oh, okay. That makes a lot of sense then. So, I guess, how do we really get to grips with the more detailed financial aspects of it all? For example, why do I need to learn how to understand my pay slip? I work, I get paid, I spend, what's my payslip going to tell me?

Iona:

Well, payslips are really important because they tell us lots of things and not just our salary, but what we pay in tax, which can be quite complicated, but I'm going to break down. And other stuff like pensions, student loan contributions and so on. So, here are the important things to note on your payslip. Your tax code, which tells your employer how much tax-free pay you should get before deducting tax from the rest of your salary, but you need to check that this code is correct against your latest tax code letter. Then there's your national insurance number. Now, this is a number that you have for your whole life to make sure all your taxes are in order and help build your entitlements to things like your state pension. You'll need to then note your gross pay, which is your pay before any deductions versus your net pay, which is the take home pay you actually get when all the deductions have been made. These include tax and national insurance, your pension contribution, your student loan repayments if you're earning above the repayment threshold, any court orders and child maintenance and trade union messages. If you're on statutory sick pay or any maternity, paternity, and adoption pay, these payments will also show up on your payslip. Now, obviously, if you're self-employed you don't get payslips and you don't get tax deducted under the pay as you earn or PAYE system. So, you have to submit self-assessment tax returns every year, which will detail what you earn and all the work-related expenses that should be factored in. So, it's worth getting to grips with how those forms work and what kind of expenses you would be able to claim if you do go self-employed. And finally, it's really important to keep your payslips safe, even if you're receiving them digitally, which is increasingly the norm these days. You need to file them away in a safe, secure place, because payslips have a lot of information on them which could be used for identity fraud and also you just want to keep track of your earnings and tax payments in case you need to query anything with your employer or the tax office in the future and you may need to provide proof of earnings i.e. your last three payslips to qualify for financial products like mortgages in the future.

Arun:

I guess circling back to working then. What kind of money issues or hidden costs might we need to consider at the start of a job?

Iona:

Well, when you start working, you need to understand what your starting salary will be. We've already talked about the importance of grasping the difference between gross pay and net pay and also understanding what your pension contributions will be and how much you will be paying back on your student loan. Also,

will your employer require anything from you? So, will you need to provide certain equipment or uniform or will your employer be providing that or reimbursing you for it? And if you are traveling to a job, say on the train, are there ways you could cut costs? So, for instance, could you get a season ticket if you're a train traveller? If you're going on the train off peak, would you perhaps consider getting a young persons or millennial rail card where you can save money on trains. And also, could you take advantage of any workplace benefits on offer? So, there are all sorts now being offered by employers like Cycle to Work loans, free financial advice, it's well worth finding out what's available because that stuff can really add value to your job.

Arun:

That's been really useful Iona. We know that getting your first job is an exciting event, you know, I was really gassed when I started mine. But there is a lot to understand around the money that you will eventually earn.

Arun:

Some of us have student debts to pay. What about clearing these? How do I know which ones to prioritise?

Iona:

Now, the student loan is different. It's a structured repayment process where the contributions are automatically deducted from your salary, but you need to be earning over £26,575 a year for that to kick in and even then you only pay a certain percentage of your earnings above that threshold. And what's more all outstanding debt is wiped at the age of 50 anyway. And the good news is that your student loan will not appear on any of your credit reports, which is something that we're going to cover in another one of our conversations. And it shouldn't affect your ability to borrow money. Though be aware that some mortgage lenders might look at your student loan as part of their affordability assessment. But of course, being in debt can be very stressful. It can get on top of us. So, it's important to tackle it head on and understand what your options are and if need be talk to your bank or your lenders and then if need be speak to a debt charity, if you're really struggling to make those repayments. And being open with your friends and family can help as well because sometimes being in debt is a real burden and just talking about it can really help us take that weight off our shoulders.

Arun:

From my own research, and people that I've spoken to, I understand that some companies offer quite a wide range of workplace benefits. Some of which enable you to stretch your money a little bit further or might be financially valuable in the coming years. Do you have any thoughts on these?

Iona:

So, on top of your workplace pension, your employer could also offer things like season ticket loans, car share, and Cycle To Work schemes and wellbeing options like discounted gym membership. They may also offer vocational options like volunteering and study days, or the option to take sabbaticals or go on courses to help you upskill. So, for instance, one of my former employers allowed me to go and take a course in news reporting and media law, which was really valuable to me. So, investigate whether your employer offers benefits that might add value to your life and help you skill up over time.

Arun:

Oh, brilliant. I know that a lot of the comments that we've received have been about around making the most of what I have, from your experiences then how easy is it to do that?

Iona:

Well, I think it's firstly about maximizing your income. So, it's well worth finding out what the benchmark salary in your industry or field is for someone with your experience and background. And you may discover

that you could be paid more and if so, that's a conversation that you could bring up with your employer and find out what you need to do to get that promotion. Maybe you could upskill in your spare time or do more around the office or pursue a passion that will make you more employable and valuable over time. So, for instance, I started my blog in 2011, but it wasn't just a passion of mine. It wasn't just something that I wanted to do because I wanted to learn. It actually became an asset as time went on and it made me more employable, because I was building up a lot of skills and knowledge through the blog. So eventually, I ended up basing my whole career around my blog. Now that might not happen for everyone, of course, but it's about looking for those opportunities to develop your own personal skills and brand and also, we've spoken about it before, but you know, it really bears repeating. Make time for budgeting so that you can assess what's going on with your finances.

Arun:

Now when I tell people that I work for a bank they inevitably ask me questions about different financial products, and they're actually really complicated. How can we make sure that people have all the information that they need to make a personalised decision, rather than asking me about it?

Iona:

I'm sure you know a lot more than you think, but yeah, I totally get where you're coming from. I think there is a perception that the world of finance these days is very complicated and unfortunately that means a lot of people shun financial decisions but actually it's about getting to know what your options are, weighing them up, finding out as much as you can, understanding the pros and cons and how those options would work for you and it's not as complicated as it sounds. I'd say avoid making decisions when you're tired or stressed out, don't rush into them. You know, you often don't have to make a decision straight away. You need time to go away, think about it, do your research. But also know that it's not the end of the world if you don't quite make the right decision. In the worse case scenario, you could probably reverse it in a lot of cases, for instance, with a lot of financial products there's a cooling off period of a week or 30 days. And that way you can change your mind if you're not sure and you can always find ways to improve and refine your decisions later on. But also, it's best not to overthink all your financial decisions, by all means do your homework and research and consult trusted organisations like Money Advice Service, or an independent financial advisor. If you're thinking about taking out a mortgage, speak to a mortgage broker. But ultimately, you've got to make your decisions good. So, if you decide, right, I'm going to open a savings account and then a week later you find another savings account that pays a better interest rate, then that's okay. Most important thing is that you've started saving because a lot of the time doing something is better than doing nothing. But also, don't be embarrassed about reporting fraud because it can and does happen to anyone. You can have your money or identity stolen through no fault of your own. And yes, it's very scary and upsetting, but it's better to deal with it right away so it can be resolved as soon as possible. But ultimately the best thing is to try to take those basic important precautions to reduce our chances of being defrauded. And being vigilant around our personal finances at all times.

Arun:

Thank you, Iona. That's been really informative, and you've given me quite a lot to think about, I will be changing my password now. Some final points of reflection from me then. Know that there actually are financial decisions to make as you start work. Planning how you make good financial decisions is not a waste of time. It can really help you make the most of what you have. Finally, being able to assess your own needs and making smarter financial decisions are going to keep you financially fit. Thanks again Iona and please join us again when Iona and I will be chatting about more money management.