What If I Am Forced Off My Savings Strategy?

By: Joe the Investor

Many people have a strategy for their budget that divides up their cash flow into fixed expenses (things I cannot control that easily), discretionary expenses (things I can control more easily) and savings for future goals. Much of the finance literature talks about ideas like paying yourself first, allocating a fixed percentage of your income to savings, using the RRSP for savings, or forced savings through home ownership. What if your long term savings system gets taken off the rails? Let’s say that you lost your job and your income becomes very uncertain. Can you still allocate 10% of your income to savings? What if you have no income and have to live off of your savings - a reversal of what your system is designed to do? Other examples are where your expenses are growing very quickly each year and certain parts of your budget get squeezed out. This is happening with the twin demons or higher interest rates and higher inflation.

The savings strategy is analogous to steering a boat or flying a plane. You have this long term target which is a patch of land straight ahead. Your navigation is on target at the moment. Suddenly a storm comes up and knocks your boat miles off course. You can still find that patch of land, but you have to change your direction and work longer and / or harder to reach it. For the plane analogy, you may be flying at a certain speed and at a certain heading, but turbulence appears and takes your plane far off course. You would have to adjust your heading and make your way back to the destination. If there are multiple storms that occur in the journey which is like life itself, you would have to keep making adjustments to your direction and speed to get toward the target. If the storms damage your boat, you may have to stop and make repairs before setting sail again. The financial parallel to this is suspending RRSP contributions, selling assets, stopping savings allocations, changing your environment or in extreme cases going bankrupt and rebooting the financial plan.

How do you make these adjustments when these events occur? It will come down to your priorities and what sort of disturbance you are dealing with.

Making Adjustments or Changing the Long Term Goal

The key to remember is that financial plans are not always automatic and linear. There are situations when you have to make exceptions and recalibrate the big picture, while keeping your financial goals or target in mind. Many of the setbacks that are experienced are temporary in nature and can be adjusted to fairly quickly.

The first step is to have a goal in mind or your destination. You draw an initial map – or a financial plan to reach this goal. You develop a process or a trip plan. If you save $20,000 per year until age 60, I will have enough money to make work optional.

The next thing to keep in mind is that you can still reach your goal, but it may take a different path than the original map. Another variation of this theme is that the speed at which your goal is reached can be altered at any time – either made faster or slower. This is like the wind holding back your plane and then changing directions and pushing you ahead faster. The financial plan is your benchmark which you will keep on revisiting to see if you are on target relative to where you are today.

The last thing to remember is that just because you set up a destination, it does not mean that you can't change it. The key question is: For what reason am I changing the destination? Is it because I genuinely have a change of heart and don't need or want it any longer? Is it because I believe that I needed to do very specific things and since I was not able to do them, is the plan toast? This type of questioning is changing what I actually want to achieve as opposed to "How do I achieve it?" This is an adjustment for a different reason. You can recycle aspects of your old plan to build a new plan as well.

Example of the Process

You set out on this course to reach your retirement goal. After 2 years, you get laid off for 3 months. Your income is lower so you are not able to save the $20,000 in that particular year. You can extend your plan by one year if you believe you can get back on course. If your income is permanently altered, how much can you save per year afterwards? Let's say it is $15,000 per year instead of $20,000. You resume your course with this number in mind, but your original target is still $20,000 per year. You are reaching your goal, but at a slower pace. Is it acceptable to retire 5 years later? How about 10 years later? This is one of the recalibrations that may occur. You may decide that you will have to find some income from a second job to fill in the shortfall. If you can do it, you can make up for lost ground. The extra income may cause you to spend more time working which may cost you in other ways like family time, hobbies or health deterioration. After a year of a second job routine, you may decide to find a job that pays a higher salary. This could mean retraining which may suspend income while you take extra courses. This may mean a career shift which would mean a lower salary at first but bigger income potential after a short time. Each of these decisions is a calibration to your journey that changes the speed and timing of achieving your goals. However, you can still have the long term heading in mind as a target to have your site on. People may get discouraged that the goal is not being met in a linear and predictable fashion. Oftentimes, financial goals are not achieved in the way that you set out in the beginning, but may be reached through means you did not expect. If you have the long term goal in mind, you may get future opportunities to short circuit the path or accelerate your journey. Examples of this are a boost from an inheritance, a windfall, a promotion or a new business.

The Key Message

The takeaway is that savings methods can and will change from time to time. As long as the long term goal is kept in mind, adjustments can be made to keep you on your path. Don't be discouraged by these events as they happen from time to time. The time to change your long term plan is because you have a different goal that you want to accomplish.