FINANCIAL LITERACY
FOR YOUTHS

Guide 101: Budgeting for a Trip

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Every country announces a budget plan annually. This shows that budget planning plays an important role to maintain financial soundness. If a country puts effort in planning for a budget, individuals should have a budget plan for everything involving monetary terms. By doing so, they can keep track of the inflow and outflow of money. To contextualize the idea of budgeting, it is more practical to exemplify it with a case study of budget planning for a trip.

Case Study:

Eddy is dying to go on a short trip to Boracay Island for a short getaway and in the meantime, to find peace within himself.

Problem

You see, Eddy is a typical college student. By typical, it means that he is technically broke. To be precise, he has yet to earn a stable income other than receiving monthly allowance from his parents. Apart from that, he works as a part-timer in a retail outlet which does not fulfill his desire for shopping. Hence, he feels that he does not have enough money to do whatever he wants.

Figuring out how much Eddy needs:

The key to any trip is being smart with your money and that starts even before you hit the road. It is important to know how to save and plan your trip so you don't find yourself running out of money along the way.

The tip here is to start allocating your budget with the major expenses first – usually this will be the cost of your flight tickets, but accommodation also adds up too! We should not forget the minor expenses needed to taste local delicacies of the foreign land as well. It is wise if we can even get sample prices as a rough idea of how much it costs for a room, a street snack or a restaurant meal!

For this case, a quick search on google showed that Eddy needs roughly RM1200 for his short getaway.

CAN EDDY AFFORD THE TRIP?

The financial affordability of Eddy for this trip comes into question. If Eddy has extra savings kept aside, he might be able to fund his travel expenses. Or else, he might need to figure out other ways to acquire the amount of money needed. The next question comes into picture now. By how much is Eddy short of for this trip? To identify this problem, he needs to look into his monthly expenditure, monthly allowance and savings account. It will be much simpler for Eddy to tabulate it and find out with a monthly budget. Let us look into Eddy's financial condition with the following steps.

STEP 1: Get yourself a big piece of paper

And obviously a pen.

STEP 2: List down all your monthly income

The first step to taking control of your finances is by planning out your budget. It will take some effort, but it is a great way to get a quick snapshot of the money you have coming in and going out.

Eddy starts by adding up his monthly income:

Income	RM
Allowance from parents	1600
Part-time job	800
Total income	**2400**

According to this information, Eddy has RM 2,400 to spend every month.

A good tip right here is that you always guess (estimate) low for income, and guess (estimate) high for expenses. This prevents you from overstating your income and understating your expenses. In general, this approach is prudent as it gives you extra capacity to manage your funds on hand.

STEP 3: Identifying Outflow

This part is a little tricky. The best way someone can accurately measure this is to look back at his or her spending history.

Expenses	RM	%
Rent	1000	41.67%
Food (RM10 * 60 meals)	600	25%
Shopping	300	12.5%
Sundry expenses	200	8.33%
Gym membership	180	7.5%
Telephone	80	3.33%
Transport cost (occasional Grab car)	50	2.08%
TOTAL ESTIMATED MONTHLY EXPENSES	**2410**	**100.41%**

Red flag is up. Eddy is making a loss every month. In other words, he has zero disposable income and zero savings. How is he going to fund his trip? How is he going to save then? What are the alternatives?

STEP 4: Identifying needs and wants

Eddy needs to classify his expenditure into two major classes. They will be (1) necessary expenditure and (2) optional expenditure. In layman's terms, the things Eddy spent on could be categorized into his "needs" and his "wants". To do that, let us take a look at his monthly expenses.

Items	Type of Expenditure
Rent	NEED
Food	NEED
Shopping	WANT
Sundry expenses	WANT
Gym membership	NEED
Telephone	NEED
Transport cost (occasional Grab rides or Uber)	NEED

STEP 5: Planning a Budget

Generally, personal financial constraints refers to the lack of funds to purchase things a person desires. In other words, Eddy is facing personal financial constraints by not having enough budget for this trip. However, there are a few alternatives which Eddy can consider to save up $1200 for this trip.

Plan A: Saving $110 per month

Items	RM	Adjusted RM	Notes
Rent	1000	1000	NEED
Food (RM10 * 60 meals)	600	600	NEED (can reduced by cooking/cheaper alternative, but sad thing is eddy's place doesn't have a kitchen nor he knows how to cook nor he can get cheaper food somewhere)
Shopping	300	150	WANT (can cut by 50%)
Sundry expenses	200	100	WANT (can cut by 50%)
Gym membership	180	100	CHEAPER ALTERNATIVES (100 pm)
Telephone	80	50	CHEAPER ALTERNATIVES (40 pm)
Transport cost	50	50	NEED
TOTAL ESTIMATED MONTHLY EXPENSES	**-**	**2050**	**-**
EXTRA	-	350	-
Less: 10% of total income for "just-in-case" funds Emergency, better choice of word?	-	(240)	Also known as rainy day funds, for unplanned events, e.g. needing a new phone urgently after unexpected damage. *more will be highlighted at the end
Available for saving		**110**	

Referring to the table computed above, Eddy can opt to cut down on the unnecessary expenses, including shopping and sundry expenses. The idea of this part is if it's a "want", we will cut the expenses by 50%. On top of it, Eddy could save up quite a bit if he were to switch to a cheaper monthly gym membership plan and monthly telephone plan. Let us assume Eddy had managed to scout around and found a store that offers lower price rates for his sundries. He then walks to the sundry store to purchase what he needs. Just by doing that, he is able to cut down RM 130 worth of expenses as well as break into a sweat by walking. As the saying goes, Eddy could kill two birds with one stone.

Do the math now. Hit the buttons on the calculator! (RM 1200 / RM 110 per month)

It will take Eddy approximately 11 months to save up to RM 1200 for the trip.

This means Eddy gets to plan this trip 11 months in advance.

Plan B: Cheaper meals and cut all want(s)

Instead of having to wait for a period of 11 months, are there any ways to save RM 1200 faster? Eddy is a gym freak who is not willing to give up on the gym plan he had signed up for. Plus, he does not find the need to switch his phone plan. However, Eddy is willing to cut down his expenses on non-necessities and opt for cheaper meals.

Since Eddy is a fitness enthusiast, he needs to consume a large amount of carbohydrate and protein in his meals to rebuild his muscles. To kickstart his day, he can prepare bread slices with peanut butter spread. As for lunch, he can enjoy a plate of chicken rice with friends at the budget of RM6. Speaking of dinner options, the local delicacy Ramly Burger which can make a run with the conventional fast food chain burgers at a cheaper selling price can be an affordable yet filling meal. Eddy could also enjoy an egg cracked on or wrapped around his burger patty for dinner.

Here is the breakdown for every meal in a month:

Breakfast	A loaf of Jumbo Bread = RM 3.55 A Jar of Peanut Butter = RM 7.85 (Let's assume Eddy needs two loaves of bread and one jar of peanut butter per week)	RM 60 / month {(RM 3.55 X 2) + RM 7.85 } X 4
Lunch	Food Court or University Cafeteria (RM 6 budget)	RM 180 / month (RM 6 X 30)
Dinner	Ramly Burger (RM 5 averagely per burger)	RM 150 / month (RM 5 X 30)
		Total Meal Expense: RM 390/ month

Items	Old Figure	New Figure	Difference
Rent	1000	1000	
Food	~~600~~	390	210
~~Shopping~~	~~300~~	0	300
~~Sundry expenses~~	~~200~~	0	200
Gym membership	180	180	
Telephone	80	80	
Transport cost (occasionally Grab car)	50	50	
TOTAL ESTIMATED MONTHLY EXPENSES	**2410**	**1700**	**710**

With this budget planning, the total estimated monthly expense has gone down by RM 710 as compared to the initial estimation. With this method, Eddy can save up RM 1200 in less than 2 months. This plan could also save up to nearly 80% of Eddy's time as compared to plan A.

Plan C: Alternative by borrowing from parents **

Meanwhile, Eddy thinks of getting funded by his parents. This might be the fastest way to go for a trip. Is that so? Thinking of which, perhaps he need not cut down on his daily expenses for this instance. If his parents lend RM 1200 to him, Eddy is willing to pay back RM 100 per month after his trip. However, we need to take note of initial living expenses. It has exceeded the amount of money he has on hand. How is he going to pay back his owings to his parents of RM 100 per month? In other words, he needs to reduce some of his unnecessary expenditure after the trip to fork out RM 100 per month. At the end of the day, Eddy still needs to fork out RM 100 per month until he completely repays his debts.

To pay down this 'loan', let us first calculate the net present value by using the simple present value of annuity formula.

$$P\left[\frac{1-(1+r)^{-n}}{r}\right]$$

$$P = Periodic\ Payment$$
$$r = rate\ per\ period$$
$$n = number\ of\ periods$$

Assuming the monthly growth rate equals to 1.3% ; 12 months of payments ; RM 100 per payment, Eddy needs to pay a total net present value of RM 1100. Theoretically, Eddy has an extra RM 100 to spend, whereas his parents are making a loss of approximately RM 100. This could be explained through the fundamental financial theory, Time Value of Money. The current value of money is worth more than the future. Since Eddy agrees to pay back RM100 monthly, Eddy does not need to take into account interest rate or any other relevant factors. In simple terms, Eddy does not need to pay for any extra costs (interest expense) on top of his initial amount of borrowing. Therefore, the amount of RM 1200 is worth more for this instance as compared to the total amount of repayment for Eddy in the future given the discount rate of 1.3% monthly.

Isn't it reasonable and rational for Eddy to borrow some cash from his parents? In comparison to all three suggested alternatives, this method seems to be the most cost-effective and the most efficient choice of funding for the trip. It requires nearly zero cost and has the least time consumption to reach the RM 1200 target of budget for the trip. However, we need to take into account the saving pattern Eddy should have. It is always good to save for rainy days.

Comparison for 3 plans

Among the three plans suggested above, Eddy has to weigh the costs and benefits of each one of them. Every plan presents different values of money. Plan A and Plan C are considered to be very different from Plan B. From the detailed budget planning in Plan B, it is evident that Eddy has to make slight drastic changes in his budgeting plan to save up RM 1200 effectively in 2 months. This will require Eddy to cut down a lot on his spendings for sundries and on shopping. Let us not forget, Eddy would need to have an affordable meal such as Ramly Burger for dinner daily as well as prepare his own breakfast every morning. If Eddy is determined to stand on his own feet, this plan is moderately and reasonably sound. Or else, he might need to consider the two other plans which seem to be easier to carry out.

For Plan A, Eddy gets to save up to RM 1200 in 11 months by contributing RM110 per month into his budget. However in this plan, it was not taken into account the risks involved such as inflation, interest rate and foreign exchange risk. On the other hand, these risks have a smaller impact on Plan C. Upon implementation of Plan C, Eddy might need to forgo part of the opportunity cost by reducing certain optional expenditures in his monthly financial budget after his trip. As agreed, he is obliged to pay back his parents RM 100 per month. Coming into the subject of potential earnings, the time value of money seems to be higher in Plan C. Eddy needs to pay back an amount totalling RM1100 of the present value of the future cash flow. In other words, when we discount a monthly amount of RM100 as fixed payment to the current period, Eddy makes a profit of RM 100 each month.

In comparing these two similar plans (Plan A and Plan C), Eddy does not need to make that much changes or adjustments with his monthly expenditure. However, he needs to take into consideration the opportunity cost he is willing to forgo now or in the future. Somehow, every choice made comes with its own consequences. Nevertheless, Eddy gets to understand the ‘price’ he needs to pay for every decision made.

Plan	Time Consumed	Opportunity Cost
A	Approximately 11 months before trip	RM 110 savings per month Higher risk involved
B	Approximately 2 months before trip	RM 710 savings per month Drastic changes in lifestyle
C	12 months after trip	RM 100 payment per month Lower risk involved

Budgeting techniques and risks for overseas spending

Now that Eddy has carried out an analysis of the budgeting plans available for himself, it is now time to plan and prepare for the future by finding out the right budgeting techniques and risks during the trip.

It is near impossible to escape from F.E.A.R (Foreign Exchange Associated Risk) in the process of budgeting for overseas spending, even for Eddy himself. The underlying concept of risk arises from the possibilities of a loss in value from an unfavourable exchange rate fluctuation at the time of conversion of your home currency to another currency. For overseas investors, various financial models or trading strategies have been adopted in dealing with unavoidable risks associated with foreign investments. The most conventional method for investors in dealing with such risks is by carrying out hedging via forward contracts, future contracts and so on. However, coming back to our main discussion on this article, budgeting for an overseas trip by any means should not require Eddy to adopt such complex and complicated models. As it would be illogical for Eddy to carry out the trading strategies mentioned previously for an overseas trip spending budgeting plan, many other factors should be considered to minimize the risks associated with currency conversion and overseas transaction while travelling.

The first factor may be a common concept which tends to be overlooked or neglected by overseas spenders – methods of currency conversion or withdrawal. The interest rate charges or service charges imposed by financial institutions may not be a matter of concern for infrequent currency conversion or withdrawal, but the compounding effect or accumulation of such charges will be a shocking amount at the end of the day for a person unaware of the frequency of their withdrawals or conversion. As a general rule for currency conversion, using ATM machines supporting PLUS platform that charges a range of fixed amount for every foreign withdrawal (eg. Maybank charges RM 12 per foreign withdrawal) is the best and most reliable choice for currency conversion.

In addition, another common currency conversion method that is widely practiced in all countries is money exchange via the foreign exchange office, or commonly known as the money changers. Among the things that Eddy has to take note of when deciding to convert currency at money changers include the location of exchange offices, rates offered, and service charges imposed. Location at which these money changers are situated offers different rates or service fees for currency conversion, and money changers at airports and grand hotels tend to offer higher charges and lower rates compared to any other local money changers elsewhere. Moreover, certain money changers also tend to impose hidden or additional charges and it is important to enquire on these charges before using their services. Eddy should keep himself aware from time-to-time regarding the latest foreign exchange rates, by utilizing apps such as the XE Currency Converter app to ensure he gets the best deals from the right money conversion source.

With growing advancements in the market and financial field, various payment methods are made available to spenders internationally either via conventional methods (eg. debit card, credit card, cash etc), or via mobile and online payment methods (eg. Alipay or Zhifubao). However, this section will be focused on the conventional methods as opposed to the mobile and online payment methods which are yet to be widely practiced globally. It is always advisable to avoid debit card payments and to carry out transactions overseas by credit card or direct cash payments. It is undeniable that spenders utilizing card payments will tend to face higher possibilities of error in transaction which may cause them to be overcharged compared to cash payment users. Transactions carried out via debit card payments causes your home bank account to be directly debited (reduction in bank balance), while credit payment will only impose the spending charges on the user at the end of the month. The direct debit nature of debit card payments causes the reversion of such transactions to be more inconvenient to deal with, for which there is an error in the transaction. In normal cases, the debit card user would have to directly inform the home bank on such error within a period of one week for the transaction to be reverted. Telecommunication charges for overseas calls incurred may be costly, but there will be a small portion of the transaction fees involved if the error had gone unnoticed during the trip.

Lastly, setting a backup or emergency plan for a budgeting plan is always necessary for the unforeseen circumstances that might occur during the period of the overseas trip. Among the common events that Eddy may face include overspending, loss of cash due to theft and so on. Eddy should always have at least 2 bank cards usable internationally through ATM or have a foreign bank account set up for online money/fund transfer. The purpose of having multiple bank accounts is to create an emergency/backup fund on one of the bank accounts, which will ONLY be withdrawn on certain situations and not for casual daily spending. With all the features and functions of cards being mentioned previously, Eddy should also never forget to:

(i) Activate his bank cards or accounts for international usage (eg. Enabling Maybank overseas option)

(ii) Contact home bank in advance prior to traveling abroad to prevent bank cards being blocked or having service interruption due to the suspicion of fraud.

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