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Give your finances a fresh start

The first few weeks of a new year can feel like a clean slate: Past imperfections are relegated to history and you can redefine what you want to achieve in the year ahead. This is a great time to spring clean your financial closet and take action in pursuit of your goals.

A cognitive phenomenon known as the 'fresh start effect' explains that temporal landmarks, such as a new year or the start of a new week, can motivate aspirational behaviour. Temporal landmarks are days that stand out as being more meaningful than others, either because they mark the start of a new time period or represent a new beginning. They are also effective because they increase the distance between our current (and future) self and our past failures, which explains why we feel more motivated and driven.

However, when it comes to our finances, this motivation can be short-lived. This is because, well, life happens: Unexpected expenses creep in or we struggle to scale back on our spending, which affects our ability to save. Before we know it, we're committing to the same goal, one year later.

There are many different methods for setting and achieving different life goals, but not all of them will work for every goal. Because we are all different, what works for others may not work for you. It's important to find a method that resonates with you and is fit for purpose. A good, independent financial adviser can also help you figure out what will work best for your financial goals – and be the voice of reason when you are tempted to deviate.

Here are some ideas to help you set goals that you can stick to.

SMART goals

A popular formula for achieving your goals is to make them SMART: specific, measurable, achievable, results-focused and time-bound, to hold you accountable to what you set out to achieve. Research has found that while SMART goals for weight loss, wellness or fitness can bring you much glory, the strategy is not always successful with financial goals. This is because our finances are sensitive to life's unexpected events that are out of your control. For example, you may be saving up to upgrade your car but then you end up having to take financial responsibility for a family member. Or, you may have planned to buy a bigger home, but your company asks you to relocate to a new city and provides you with accommodation. The key for financial goals is to keep them flexible enough to account for changes in income and unexpected life events.

Rigid vs fuzzy goals

On the other hand, being rigid with your goals is effective for people who like the idea of creating different 'pots' for different purposes (or goals), and being disciplined about how much is allocated to each pot. But, what happens when one 'pot' runs out and another overflows? If you are too rigid, it can be difficult to tap into the 'wrong' pot for the 'wrong' purpose when something unexpected happens. Greg Davies, an expert in behavioural finance and decision science with Oxford Risk*, suggests that it may be better to put your money into one pot and work towards achieving the best possible investment outcomes – still a goal, but less rigid.

Of course, allowing for flexibility is not the same as giving yourself permission to fall off the savings wagon and simply spend. We all have non-negotiable priorities, like saving for retirement or settling all debt before you retire, which we should not compromise on. These should be separated from contingent goals, which can, and very often will, change over time, depending on what life throws our way. Because we don't know what our priorities will be in five or more years' time, we should avoid over planning for contingent goals.

Davies says we need to be comfortable with 'fuzziness' as it makes us adaptable when thinking about our financial future. Rather than trying to be overly precise with our financial goals, we should rather work towards building up capital so that when the next financial need arises, we will have enough saved up to meet the need. It can be hard to save without a precisely defined goal, as this takes discipline and commitment, but a shift in mindset can reveal just how attractive (and motivating) freedom of choice can be.

Improve your financial behaviour one habit at a time

Achieving your financial goals starts with making good financial decisions – but how do you ensure that you make the right financial decisions, at least, most of the time? Nobel Prize-winning behavioural psychologist Daniel Kahneman has done much work on how we, as humans, are hardwired to make decisions that don't always serve us well. We often act impulsively, automatically or intuitively, sometimes blissfully unaware of the decisions we're making in the moment. To control this, Davies suggests that we create 'decision prosthetics' – triggers that can influence our decisions in the moment, or help us make better decisions when we're likely to be acting impulsively, automatically or intuitively. They help us to be more thoughtful and deliberate when we most need support, which can positively influence the choices we make and, ultimately, our financial behaviour. But for this approach to work, we first have to be able to identify where and when these moments are likely to arise.

For example, if you struggle with overspending, then setting a low daily card limit is a good decision prosthetic that restricts how much you can spend on any given day. Similarly, leaving your credit card at home when running errands, avoiding large shopping centres with tempting luxury goods stores, unsubscribing from sale updates, or simply practicing gratitude for the things you already have, are all decision prosthetics (and good habits) that can help you spend less, and thus stay committed to your goals.

The compounding effect of developing good financial habits is just as magical as the compounding effect of time on the value of our investments. We also need to accept that for most of us, saving means sacrificing what we would really like to have today. It isn't easy, but it will be worth it over the long term.

**Oxford Risk is a spin-out company of the University of Oxford, which focuses on applied behavioural science.*

Commentary contributed by Ciani Gower, business analyst, Allan Gray

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