HOW, & WHY, TO BUILD AN EMERGENCY FUND

Created by the IFW in collaboration with Kim Uzzell of The Financial Wellbeing Academy.

One thing we know is that life can be unpredictable.

Even when we think we've got everything in place, something seems to crop up and catch us out.

And that can be expensive – especially if we don't have the money put aside to cover it.

If you've ever needed to pay out unexpectedly for a problem with your car or your home, you'll understand how crucial an emergency fund is, if you don't want to end up taking out a potentially high-interest loan, asking family members for help or choosing between fun and necessity.

Happily, creating, building and maintaining an emergency fund is simple with this six-step guide.

1. ***Work out how much money to keep in your emergency fund***

How much is enough?

There is no 'perfect' amount to have in your emergency fund. Everyone has different income and expenditure levels, different priorities and different sets of circumstances.

For example, does your household have one income or two to cover the bills, do you have children or pets, or do you have expensive commuting costs?

It's important to create a plan that's right for YOU, even if the amount you're working with is very different to other people you know.

Take a look at your monthly bank statements. Whatever you have left over at the end of the month after these essential costs is your disposable income. Work out how much of it you're willing to save each month into an emergency fund.

Essential outgoings include:

- Mortgage or rent
- Utilities
- Food
- Leisure

Ideally, in total you should save the equivalent of three to six months' essential outgoings set aside. This amount will vary according to whether it's intended solely to keep yourself afloat or yourself, a partner and/or dependents. Everyone will have different needs, and it's important to take these into consideration so you're not caught out later.

If you tend to be tempted to spend money as soon as you save it, open a new savings account that you don't see on your phone every time you log into your online banking. The money is still there, and growing for when you need it but "out of sight, out of mind" can help reduce the temptation of spending it without thinking.

Keep this money in an account you can access easily and immediately. This should be a separate savings account rather than your current account or, for instance, the kids' university fund. Rather than calling it an 'Emergency Fund' or 'Rainy Day Fund', why not go for something positive like 'Freedom Fund' or 'Sunshine Savings'?

If you can, you might want to factor in some personal funds for less essential items, such as holidays and other wellbeing activities.

2. Start paying into your emergency fund regularly

We often have good intentions to save any money that's left over at the end of the month, but we also know that by the end of the month there's a good chance we'll already have spent our money on other things.

Instead of waiting to see if there's anything spare on the day before payday, you could treat your savings just like any of your other essential bills.

You wouldn't dream of waiting until the end of the month and then choosing whether or not to pay your mobile phone bill – it probably comes out automatically every month so you don't have to think too much about it.

Why not do the same with your savings? Make it a non-negotiable and automatic payment, along with your other regular bills.

Once you have an idea of the amount you need to save and you've set up the easy-access account you want to channel it into, set up a monthly standing order or direct debit to make paying into it as simple as possible.

You can still add money into it at the end of the month if you've got any spare, so keep an eye on what you're spending during the month, and see if you can put a bit more into the 'pot' just before payday.

This will enable you to reach your target amount, and peace of mind, sooner. It's motivating to see your savings add up – the more you see your money build, the more you'll want to add to it.

3. Round up on your spending

We might not use cash much now, so the jar might take a longer time to fill, but the good news is that technology allows our banking and savings apps to do the exact same thing for us – just into a digital jar instead.

Check your current account, or look for “round up apps.” You’ll find that a lot of current accounts offer the option to round up pennies after each spend, automatically putting the “change” into your savings account.

For example, if you buy a coffee for £2.90, it will “round up” to the nearest £ and ten pence will go into your nominated savings account.

You probably won’t notice these small amounts going out of your current account, but you’ll also be pleasantly surprised by how they contribute to your emergency fund pot.

4. Keep your emergency fund up to date

We know life is unpredictable, so don’t let yourself get complacent and ignore your emergency fund.

With costs rising, it’s important to keep an eye on the value of your emergency fund compared with your essential outgoings and ensure they continue to match. You may find you need to adjust the monthly amount you pay in if your monthly costs increase.

It’s also worth noting that if you’ve taken advantage of a special offer or rate of interest from your bank, you may need to renew your savings account each year so you don’t suddenly find your money isn’t at the best rate available.

Add a reminder to your phone or calendar to have a chat with your savings account provider, or check on one of the savings rates comparison sites online about a month beforehand to make sure that account still offers the best interest rate on the most appropriate terms available to you.

It only takes a few minutes but it could make quite a bit of difference to the amount your savings can earn for you.

You could also set a regular “money date”, especially if you share the financial responsibilities with someone else in the household, to make sure you all know what’s needed to feel financially secure.

This doesn’t just avoid potential money problems in the future, but can also help avoid arguments about money or other stressful things, making your homelife easier too.

5. Use the money if you need to

As important as it is not to empty your emergency fund on a whim, don't forget that it's there for a reason. If something does happen that means you need money urgently, don't be afraid to spend the money you've saved.

It's there to save you stress, and should be used when you need it.

It can be useful to remind yourself that not everything we think we need justifies dipping into the emergency fund – a takeout on a day when you can't be bothered to cook might NOT be the best use of your emergency fund.

However, getting the boiler serviced just before winter arrives, or investing in new tyres for your car to keep it safely on the road could be a great use of your emergency savings.

6. Remember to restock your emergency fund

When you do spend a chunk of your emergency fund, don't forget to top up the account as soon as you can, so you're not caught out if, for instance, your car breaks down again or something else expensive happens.

Although you may not face another unplanned expense for a long time, just knowing the money is there removes that concern and leave you free to enjoy the rest of your disposable income.

And when your emergency fund reaches the target that you've set yourself, you can do this exercise again, but with a new goal in mind – perhaps adding to your pension, investing in your home or a trip of a lifetime!