Why, how and when you should figure out your net worth

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Do you have a full understanding of how much money you have? Only about 5% of people have an accurate idea of that they're worth, according to the non-profit Association for Financial Counseling and Planning Education. Financial planners say that's a problem.

"It's the starting point," says Kyle Ryan, head of advisor services for Personal Capital, a San Francisco financial technology company. "You can't set your goals for retirement without knowing what you have and your net worth is what you have."

Knowing your net worth tells you where you are financially at one point in time, says Michele Ferrara, a principal in the Private Wealth Services Group of Boca Raton, Fla., accounting firm MBAF. When checked at regular intervals over time, the series shows your progress toward goals like funding retirement. "It helps you gauge when you can retire and helps you see whether you are losing value or gaining value," Ferrara says.

A set of net-worth figures can alert you to problems in your financial approach before it's too late. "If you're losing value, it allows you to drill down into those areas and say, 'What do I need to focus on right now?'" Ferrara says.

Mortgage bankers and some other big-ticket lenders typically want to know your net worth before extending credit, adds Len Hayduchok, a financial planner in Hamilton, N.J. Net worth may also be evaluated by an insurance company if you are trying to purchase a policy with a large death benefit, Hayduchok says.

To calculate your net-worth, add up all your assets, including cash, savings accounts, investments, real estate and other valuables. Next, add up all your debts, including mortgages, credit cards and auto loans. Now, subtract debts from liabilities. The result is your net worth.

There are a number of online tools, including Personal Capital and Mint, that will do this work for you and show you a running total any time you care to check. Personal financial software such as Quicken will do the same. Whether done with a calculator and sheet of paper or online, there are a couple of things to keep in mind.

First, make sure you include all your assets and liabilities. A personal loan from a relative, for instance, should be included to give you an accurate liability figure. And don't neglect to include your art collection or garage full of classic cars on the asset side.

Also, take care to accurately value non-financial assets, especially collectibles. Be conservative when valuing personal-use assets, Ferrara says. "It has to be a value that someone would put on there in an arms-length transaction," she says.

You may also want to calculate your liquid net worth. This consists of all assets that you could convert to cash quickly, such as checking accounts and savings accounts, minus all bills that will have to be paid in the next 30 days or so. Your liquid net worth measures your ability to fund your lifestyle in the short term.

While net worth is a useful figure, it should probably only be consulted occasionally. Most experts suggest annually or perhaps quarterly. "Looking at net worth too often can get us too excited or too discouraged," Hayduchok cautions. Checking every morning, for instance, could lead to over-reaction to short-lived events such as market corrections, leading savers to sell off temporarily depressed assets at less than their long-term value.

At the same time, don't just figure your net worth a single time. Instead, do it regularly. "It's not something one and done," Ferrara says. "You need to evaluate and monitor it."

Sometimes your net worth may be negative, indicating you owe more than you own. While that's obviously not ideal, it may not indicate an emergency. For instance, Ferrara says, young people just starting out on their careers and trying to pay off student loans often show negative net worth.

Major market downturns also often may cause an investor's net worth to turn temporarily negative. When market cycles create negative net worth, Ferrara cautions that it's important not to over-react and sell while prices are depressed. Instead, she suggests meeting with your advisors and looking into spending cuts.

Finally, net worth is only one way to measure success. Not everyone derives identity from financial figures, Hayduchok says. Some, for instance, worry more about how much they contribute to other people's lives. "For some people, net worth is a totally irrelevant number because that's not how they measure their value," he says.

However, for anyone concerned about a secure retirement, calculating net worth is probably an unavoidable first step, similar to the weigh-in that begins many diet plans. "Net worth is the equivalent of getting on the scale," Ryan says. "It might not be pretty. But you have to do it."