

Personal Finance

Investing



Begin by making

Lifetime Projections of:

- **Career choice**
- **Expected income throughout career**
- **Family plans**
 - ✓ Married or single
 - ✓ Number of children
 - ✓ College enrollment
 - ✓ Retirement age
- **Amount of planned savings**
- **Projected living expenses**

Create a Personal Income Statement

such as this one for the year ended ___/___/___

Income:

Summer Job	\$4,500.00
Help From Parents	<u>2,400.00</u>
Total Income	\$6,900.00

Expenses:

Giving	450.00
Saving	450.00
Automobile	1,500.00
Food	1,000.00
School Expenses	<u>1,000.00</u>
Total Expenses	<u>4,400.00</u>

Net Income: **\$2,500.00**

Beginning Income Statement

- **Complete a projected income statement for the current calendar year.**
- **List assumptions that are made:**
 - After tax income
 - Ignore inflation
 - Still in school

Investing

- **Becomes relevant only if saving occurs**
- **When a younger person learns to save – greater the potential benefit**
- **Reason - time value of money - the sooner you save, the sooner your \$\$ start to work for you**

One Out of Every 125 Americans Is Now a Millionaire



Homeowners vs Renters

- **Average renter in 2001 had net worth of \$4,800**
- **Average homeowner had net worth of \$171,700**



Suggested Allocation Of Disposable Income

- **10 percent to give**
- **10 percent to save**
- **70 percent to live on**
- **10 percent for discretionary spending**

Application Of Economics

- **Allocation of scarce resources among unlimited wants**
- **No person ever has enough money to afford everything that can be bought**
- **Choices must be made**

Factors Affecting Time Value Of Money (Growth of Savings)

- **Size of deposits**
- **Rate of return**
- **Length of time**

Effect of: Deposit Size

(25 year old - 8 percent account)

<u>Deposit Size</u>	<u>Total Deposit</u>	<u>Balance Age 65</u>
\$100	\$ 48,000	\$ 349,100
200	96,000	698,200
300	144,000	1,047,300
400	192,000	1,396,400
500	240,000	1,745,500

Effect of: Rate Of Return

(25 year old - \$150 monthly deposits)

<u>Rate of Return</u>	<u>Total Deposit</u>	<u>Balance at 65</u>
5.0%	\$72,000	\$ 228,903
7.5	72,000	453,573
10.0	72,000	948,612
12.5	72,000	2,068,186

Effect of: Time

(\$150 monthly deposit – 8% rate of return)

<u>Beginning Age</u>	<u>Total Deposit</u>	<u>Balance at 65</u>
55	\$18,000	\$ 27,441.90
45	36,000	88,353.06
35	54,000	223,553.91
25	72,000	523,651.17

Time Value of Money Illustration

- **Person One**
 - ✓ **Starts saving age 25**
 - ✓ **Deposits \$1,000 per year**
 - ✓ **10 years and stop**
 - ✓ **Total deposit \$10,000**
 - ✓ **Leave deposit until 65**
 - ✓ **8 percent**
 - ✓ **Balance @ 65 \$145,772.45**

- **Person Two**

- ✓ **Saves nothing until age 35**
- ✓ **Deposits \$1,000 per year**
- ✓ **30 years**
- ✓ **Total deposits \$30,000**
- ✓ **Leave deposit until 65**
- ✓ **8 percent**
- ✓ **Balance @ 65 \$113,283.21**
- ✓ **Never catches up with person one**

Factors Affecting Time Value of Money

- **Size of Deposits**
- **Rate of Return**
- **Length of Time**

**Never Invest In Anything
You Do Not Understand**

Portfolio – Group or listing of investments

Risk – Possibility that something other than intended outcome will occur

Diversification

- **Investing in variety of things**
- **Not likely adversely affected by same factors**
- **Best method of risk reduction**

Random Walk Theory

- **Short term securities prices move randomly**
- **Impossible to predict**
- **Active trading does not pay**

Dollar Cost Averaging

- **Invest equal amounts of money at regular time intervals**
- **Usually pay lower average price than those buying at “right time”**
- **Choose investments for long-term potential**

Types Of Securities

- **Debt**
- **Equity**

Debt Securities

- **Securities arising from a loan**
- **Examples: Bonds & Bank CDs**
- **Earnings - Interest**
- **Low level of risk if held to maturity**
- **Predictable results**
- **Moderate rate of return**

Equity Securities

- **Securities arising from ownership**
- **Example: Common stock - owning a part of a company**
- **Two ways to make money**
 - ✓ Increase in value
 - ✓ Distribution of earnings - Dividends
- **Higher level of risk**
- **Less predictable results**
- **Average higher long term rate of return**