



PERSONAL FINANCE

Saving is disposable income minus consumption spending. “Paying yourself first” means saving money before spending money on consumer goods. Reasons to save vary from person to person; they might include a promise that money saved will be matched by an adult (a parent or uncle, perhaps), the satisfaction of buying a special gift for someone in the future, or the desire to buy something for one’s own use in the future.

Simple interest is the annual interest paid on the initial amount saved (the principal). To find the amount of simple interest earned annually on an account, multiple the amount by the interest rate. Example: $\$500 \times 3\% (.03) = \15.00 simple interest earned annually

Compound interest is interest paid on both the principal and the interest added to the principal. The Rule of 72 illustrates how compound interest works. In using the Rule of 72, divide 72 by the interest rate paid to determine how many years it will take for a saved amount to double when the interest is compounded. Example: $72 / 8\% = 9$ years for a saved amount to double.

The three rules for building wealth are: start early, buy and hold, and diversify.

Individual stocks would be considered the savings alternative with the highest risk and highest potential reward, when compared to bonds, certificates of deposit, and stock mutual funds. Certificates of deposit would be considered the savings alternative with the lowest risk and lowest potential reward, when compared to bonds, stock mutual funds, and individual stocks.

When you diversify, you take on many small risks, rather than one large risk. Asset diversification refers to investing in a variety of assets such as stocks, bonds, and mutual funds.

Investments with a higher potential for return have greater risk.

The disadvantage of a revolving credit account is that balances can rise quickly if only the minimum payment is made each month.



PERSONAL FINANCE

Making purchases on credit can sometimes be a good idea if the situation is an emergency, such as having to get your car towed in for repairs; you want to make a major purchase such as a car or home; or buying something on sale will save you money, even considering finance charges. Credit increases the cost of purchases.

Short-term goals are those that can be achieved in one year or less. Saving \$50 a month to buy a guitar that costs \$500 is an example of a short-term goal. A medium-term goal is one that can be achieved in one to five years, such as saving to buy a new car. A long-term goal is one that can be achieved in longer than five years.