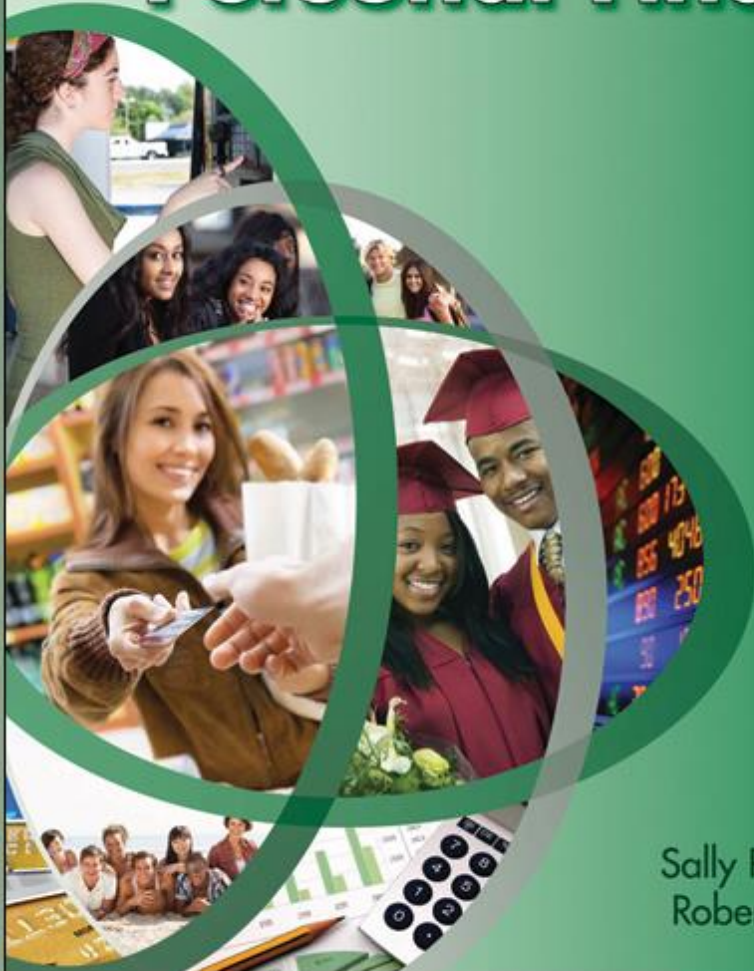


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# Foundations of Personal Finance

Ninth Edition



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*PowerPoint Presentations for*

# Foundations of Personal Finance

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# Chapter 5

## Savings

Section 5.1

# **SAVINGS PLANS**

# Objectives

- Define personal savings goals.
- List and describe various types of savings instruments that are available from financial institutions.
- Compare and contrast the different types of savings products.

# Terms

- savings plan
- emergency fund
- SMART goal
- savings account
- annual percentage yield (APY)
- interest-bearing savings account
- high-yield savings account
- money market account
- certificate of deposit (CD)

# Creating a Savings Plan

- **Saving** is setting money aside for future use
- A **savings plan** is a strategy for using money to reach important goals

# Budget for Saving

- Pay yourself first
- Budget for savings
- Use direct deposit
- Let your savings grow
- Reduce spending, increase saving

# Create an Emergency Fund

- Create an **emergency fund** – an amount of money you can access in case of an emergency
- Set **SMART goals** for saving



# Create an Emergency Fund (Continued)

## SMART Goals

**S**

Are my short- and long-term goals **specific**?  
Exactly what do I want to achieve?

**M**

Are my goals **measurable**?  
How will I know when a goal is achieved?

**A**

Are my goals **attainable**?  
Am I setting goals that can be achieved?

**R**

Are my goals **realistic**?  
Have I set goals that are practical?

**T**

Are my goals **timely**?  
Are the dates for achieving my goals appropriate?

# Savings Products

- A **savings account** is used to accumulate money for future use
- The *Truth in Savings Act* requires advertising to include:
  - Minimum amount required to open the account
  - Interest rate
  - Annual percentage yield (APY) and the time period
  - Minimum deposit, time requirements to earn APY
  - Description of fees, conditions, and penalties

# Savings Products (Continued)

- **Annual percentage yield (APY)** is the rate of yearly earnings from an account, including compound interest
- **Interest-bearing savings account** is a type of demand deposit that allows for regular deposits and withdrawals with no set maturity date

# Discussion

What is the name of the act that helps consumers compare savings products and make informed decisions?

# Savings Products (Continued)

- *Regular savings accounts* pay interest, allow deposits and withdrawals, and generally offer low interest rates
- *Passbook savings accounts* use a booklet to records deposits, withdrawals, interest earned, and current balance
- *Statement savings accounts* use a statement that lists all deposits, withdrawals, and interest earned

# Savings Products (Continued)

- Online-only savings accounts are provided by *Internet banks*
- A **high yield savings account** pays higher interest rates than regular savings accounts and requires a higher initial deposit and higher minimum balance

# Savings Products (Continued)

- A **money market account (MMA)** is a type of savings account that pays a higher interest rate than regular accounts
  - Requires higher minimum balance (\$500–\$10,000)
  - Most are limited to a specified number of checks per month
- A **certificate of deposit (CD)** is a savings account that requires a deposit of a fixed amount of money for a fixed term
  - Interest rates may be fixed or variable
  - Higher interest rates than MMAs and other savings accounts

# US Savings Bonds

- **EE Bonds** issued before 2012 are in paper form and purchased at half their *face value*
  - Since January 1, 2012, these bonds are issued electronically at full face value *to the penny* in amounts of \$25 to \$10,000
  - EE bonds earn a fixed rate of interest based on market yields of treasury notes; new rates are announced every six months
- **I Bonds** are sold at face value in amounts from \$25 to \$10,000 in electronic form
  - I Bonds pay a fixed interest rate
  - I Bonds pay a semiannual inflation add-on rate based on the consumer price index (CPI)



# Did You Know?

When you “buy” a savings bond, you are actually lending money to the federal government.

# Review 5.1

- Are savings bonds insured by the FDIC?
  - No, they are backed by the full faith of the US government
- What type of bank is able to offer free or low-cost services due to lower operating costs, since they only have to support a single computer network rather than multiple branch locations?
  - Online-only banks

Section 5.2

# **MAXIMIZING SAVINGS**

# Objectives

- Explain how savings instruments earn interest.
- List and compare alternative places, rather than a bank, to save money.

# Terms

- simple interest
- compound interest
- Rule of 72
- tax exempt
- tax deferred
- online-only bank
- share account
- brokerage firm

# Earning More Interest

- **Simple interest** is calculated only on the principal or the amount of money originally deposited
- **Compound interest** is calculated on the money deposited, plus the interest it earns

# Rule of 72

- **Rule of 72** is the equation used to estimate how long it will take to double an investment with a fixed interest rate
- To determine the number of years in which your savings will double:
  - $72 \div \text{interest rate} = \text{number of years}$
  - $72 \div 4 = 18$  years to double your money at 4% interest
- To find the annual interest rate needed to double your savings:
  - $72 \div \text{number of years} = \text{interest rate}$
  - $72 \div 20 = 3.6\%$  interest to double the money in 20 years

# Inflation and Taxes

- Inflation causes a dollar to buy less than it did before inflation
- Taxes reduce the amount we are able to save
  - **Tax exempt** means that earnings are free of certain taxes, such as certain savings accounts for education
  - **Tax deferred** means that taxes on the principal or earnings are delayed until the funds are withdrawn
  - Some retirement savings accounts are an example



# Did You Know?

Did you know that interest earned on your savings accounts is taxable?

# Alternate Places to Save

- Online-only banks
  - Lower operating costs can mean low-cost services or higher interest rates
  - Be sure to verify FDIC membership
- Credit Unions
  - Savings accounts are called **share accounts**
  - Insured by NCUA
- Brokerage firms
  - Allow you to purchase a variety of investment products in addition to savings accounts
  - Accounts may not be insured by the FDIC

# Did You Know?

Did you know that credit unions are owned by the members they serve?

# Review 5.2

- What does “tax exempt” mean?
  - Earnings that are free of certain taxes
- What does “tax deferred” mean?
  - Taxes on principal and/or earnings are not due until the funds are withdrawn