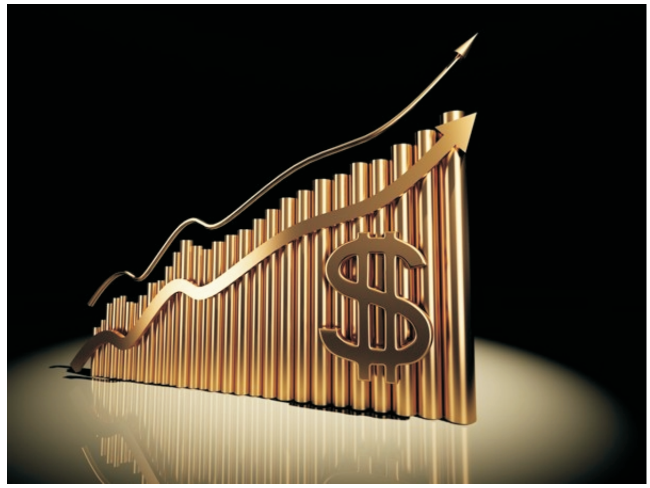
Identify Personal Financial Goals

EVERYONE has personal financial goals. Your financial goals may be to be wealthy, to have no debt, and to give generously. Whatever your goals may be, you will need to follow a plan to make your goals a reality. All plans begin with the present day snapshot or a reality check of ground zero. The financial ground zero is the monthly budget.



Objectives:

1. Define wealth as it pertains to an individual.
2. Create a budget.
3. Describe investment and savings strategies.

Key Terms:

assets	investment	net worth
budget	liabilities	personal wealth
certificate of deposit	money market account	savings account
compound interest	mutual funds	stocks

Understanding Personal Financial Goals

What does it mean to be rich? People have their own definitions of what "rich" means to them. Is being rich important to you? If it is, how do you plan to make it happen? If you don't have a plan for obtaining this goal, your chances of making it happen are slim.

PERSONAL WEALTH

Personal wealth is an abundance of valuable material possessions or resources. Examples of valued possessions or resources could be land, homes, businesses, jewels, natural resources, or many other things.

NET WORTH

Net worth is the difference between **assets** (what is owned) and **liabilities** (what is owed). Net worth is wealth. Assets are the entire property of a person, association, corporation, or estate. Assets are possessions that generally increase in value or provide a return.

Assets

Your personal belongings and possessions are assets.

- Your savings account (an account that accrues regular interest on money held in the account) is an asset.
- A retirement plan, such as an Individual Retirement Account (IRA), Simplified Employee Pension (SEP), or 401(k) is an asset.
- **Stocks** (capital raised by a corporation through the issuance of shares that entitle holders to an ownership interest) and bonds (interest-bearing certificate of public or private indebtedness) are assets.
- A dwelling, such as a house or a condominium, is an asset.

FIGURE 1. A building such as this would be considered an asset.

Liabilities

Your debts, or the accounts for which you are responsible, are liabilities. Examples of liabilities include:

- A home mortgage
- Credit card balances
- A car loan
- Medical bills
- Student loans

SETTING FINANCIAL GOALS

The first step to any achievement is to define and set a specific goal. Financial goals are no different. Define your financial goal and then begin to map out the steps to getting there. As you set your goals, remember to be realistic. Establish time frames for the steps you will take to achieve the overall goal as well as the main goal. Devise a detailed plan, but be flexible because goals can change.

Creating a Budget

All financial goals begin with an accurate budget. A budget offers a starting point from which goals or changes can be made. A **budget** is an estimate of anticipated income and expenses for a certain period of time. Income is financial gain (earned or unearned) accruing over a given time period. Expenses are financial burdens or outlays. They are a cost of goods and services.

ADVANTAGES

Although creating and following a budget takes some time and effort, the benefits of having one make the effort worthwhile. A budget helps you understand where your money goes. It can help you avoid spending more than you have. It can also help you invest expendable income to increase personal wealth.

BUDGET DEVELOPMENT

The first step to developing a budget is to calculate your monthly income. Then track your daily and/or monthly expenses. Sometimes this requires the recording of every expense for 30 days for an accurate picture. Then determine the amount you will need to pay your regular monthly expenses. Finally, divide your annual or semiannual costs into monthly costs. This will give you an estimated monthly budget.

FIGURE 2. An appropriate budget must be developed to achieve a desired financial goal.

Budget Surplus

If you are fortunate, you will have a budget surplus. You can figure your budget surplus or deficit by taking your monthly income and subtracting your total monthly costs. The amount remaining is available for investment or could be used to pay down other loans.

Investment and Savings Strategies

There are numerous ways to increase your wealth. One technique is to profit from your money management choices.

INVESTMENT

Investment is anything acquired for future income or benefit; it involves committing money to earn a financial return. This return comes from generating additional income or by an investment growing in value. Stocks are an obvious example, but they do not guarantee a return. In some cases, items of value can be resold (e.g., real estate or vehicles).

Mutual Funds

Mutual funds are a professionally managed form of collective investments. Money is pooled from many individuals and is invested in stocks, bonds, short-term money market instruments, and/or other securities. The fund manager (portfolio manager) trades the fund's underlying securities—realizing capital gains or losses—and collects the dividend or interest income. The investment proceeds in the form of dividends or interest income are then passed along to individual investors.

Compound Interest

Compound interest is the concept of adding accumulated interest to the principal so interest is earned on accrued interest. This investment strategy helps build wealth faster. The act of making the accrued interest part of the principal amount is called compounding. Compounded interest is always favorable to simple when looking to invest.

SAVINGS STRATEGIES

There are several types of savings accounts, but the type you select should be suitable to your individual needs.

Savings Account

A personal **savings account** is an account often provided through a local bank, savings and loan, credit union, etc. The interest earned is typically very low, but you have immediate access to your money without any fees for withdrawals.

Money Market Account

A **money market account** is a savings account offered by banks and credit unions and is similar to a regular savings account. However, these accounts usually pay higher interest, have

UNDER INVESTIGATION...

LAB CONNECTION: Budgeting for an IRA

How would you like to earn approximately a million dollars for your retirement? All you need is the initial $2,500 deposit and $100 every month. If it is invested at 9.5 percent, in 45 years, you will have earned $1,056,873!

But how can you save $2,500 in order to invest it? Start with a budget. Use the spreadsheet below to get started. Fill in the dollar amounts. Calculate the totals for each category, and determine if your budget has a deficit or a surplus. Any expendable income may be used for investment or savings. Write a short action plan to invest your surplus or a plan to recover the deficit.

TABLE 1. Budget Spreadsheet

****MONTHLY FIXED EXPENSES****	
Rent/Mortgage Payments	
Car Payment	
Other Installments	
Appliances	
Furniture	
Regular Savings	
Emergency Fund	
TOTAL	
*****ANNUAL EXPENSES*****	
Life Insurance	
Home Insurance	
Car Insurance	
Real Estate Taxes	
Car Registration	
Pledges/Contributions	
TOTAL	
DIVIDE MONTHLY SHARE TOTAL BY 12	
*****MONTHLY BALANCE SHEET*****	
Net Income	$
(Total Budget)	$
Living Expenses	$
Fixed Expenses	$
Annual Expenses	$
TOTAL MONTHLY EXPENSES	$
BALANCE	$

higher minimum balance requirements (e.g., $1000 to $2500), and allow only three to six withdrawals per month. Money market accounts often limit check writing to three checks each month.

Federal Deposit Insurance Corporation

The money market account is insured by the Federal Deposit Insurance Corporation (FDIC), so even if the bank or credit union goes out of business, the money in the account is protected. The FDIC is an independent agency of the federal government that was created in 1933 because thousands of banks failed in the 1920s and early 1930s. Not a single person has lost money in a bank that was insured by the FDIC since it began. If the money market account is obtained from a credit union, it is insured by the National Credit Union Administration (NCUA), which is a federal agency.

Certificate of Deposit

A **certificate of deposit** or CD is a deposit held for a certain period of time and is a financial product commonly offered to consumers by banks, thrift institutions, and credit unions. CDs are similar to savings accounts in that they are insured and thus are virtually risk-free. CDs from a bank are insured by the FDIC. CDs purchased from a credit union are insured by the NCUA. CDs differ from savings accounts in that the CD has a specific fixed term of three months, six months, or one to five years with a fixed interest rate. It is intended that the CD be held until maturity, at which time the money may be withdrawn with the accrued interest.

Summary:

You have heard the terms “wealth” and “net worth.” Personal wealth is an abundance of valuable material possessions or resources. Examples of valued possessions or resources could be land, homes, businesses, jewels, natural resources, and more. Net worth is the difference between assets (what is owned) and liabilities (what is owed).

The first step to any achievement is to define and set a specific goal. Financial goals are no different. Define your financial goal and then begin to map out the steps to getting there. All financial goals begin with an accurate budget. A budget offers a starting point from which goals or changes can be made. A budget is an estimate of anticipated income and expenses for a certain period of time. Once your budget has been established, you can begin to set some real financial goals. One technique for increasing your wealth is to profit from your money management choices. Choices may revolve around investments, compound interest, and savings accounts.

Checking Your Knowledge:

1. List three advantages of creating a personal budget.
2. Explain the difference between an asset and a liability.
3. Define the term “compound interest.”
4. Define the term “budget,” and explain why it is important.
5. Define the term “net worth.”

Expanding Your Knowledge:

Ask your friends and family if they know any financial planners. Record their names and phone numbers, and contact one or more of those people to schedule an interview. Ask about the situations they see with their customers. What are some common pitfalls? What can they share with you that specifically pertain to being a student?

Web Links:

Building Wealth: A Beginning Guide to Securing Your Financial Future
http://www.dallasfed.org/ca/wealth/pdfs/wealth.pdf

Savings Calculator
http://www.planningtips.com/cgi-bin/savings.pl

Fortune: 10 Rules for Building Wealth
http://money.cnn.com/popups/2006/fortune/buildwealth/