

## Managing Personal Finances

### Chapter Objectives

After completing this chapter, you will be able to:

#### ▶ Section 28.1 Personal Financial Planning

- **Explain** the steps involved in the financial planning process.
- **Identify** sources of financial information.
- **Discuss** sources of risk.
- **Discuss** the consequences of choices.

#### ▶ Section 28.2 Money Management

- **Discuss** the importance of budgeting.
- **List** the steps for preparing a budget.

### Ask

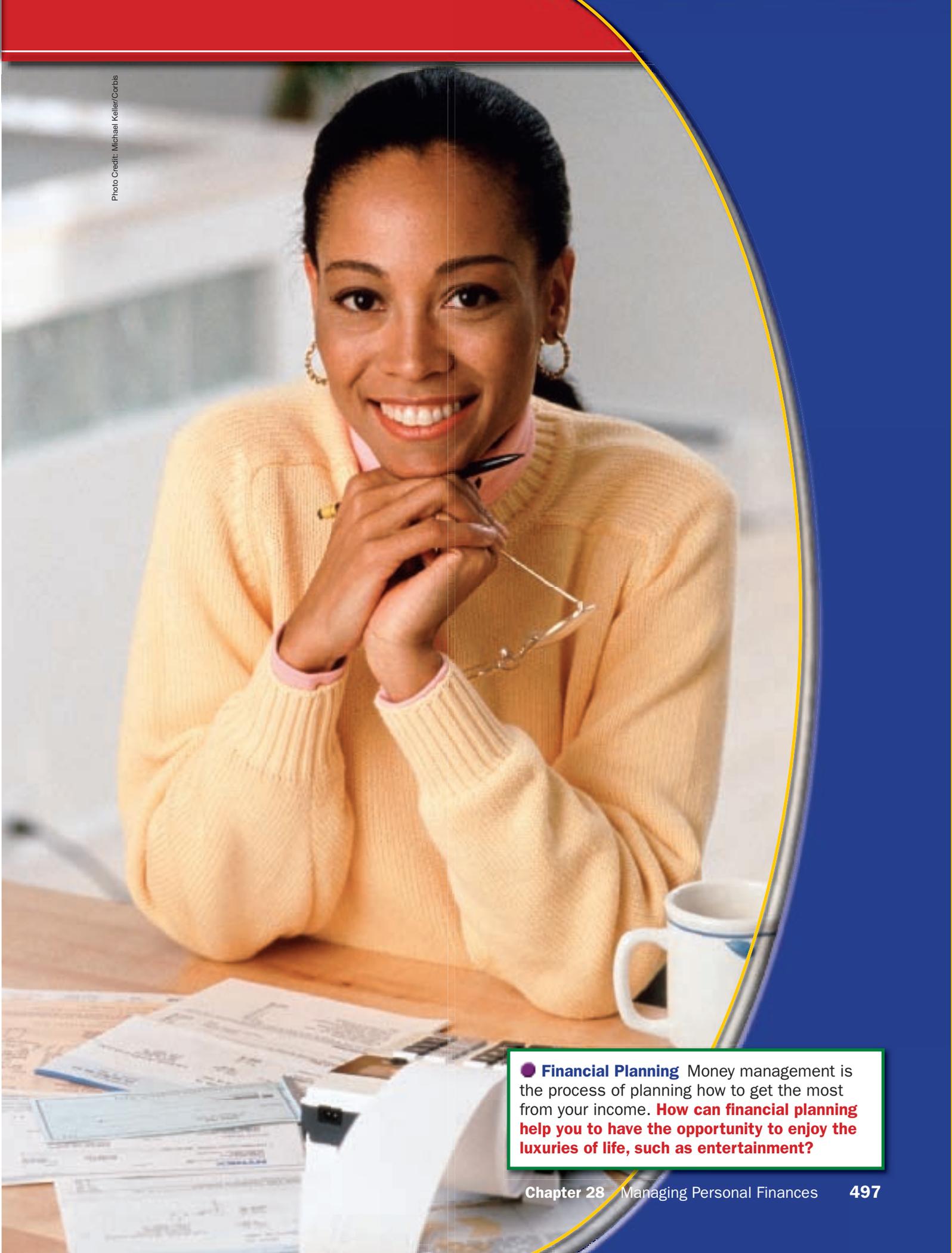
#### STANDARD Understanding Hedge Funds & POOR'S

**Q:** What are my options if I'm able to take a big risk?

**A:** Hedge funds are private investment funds for wealthy individuals and institutional investors. By law you must have an annual income exceeding \$250,000 and investable assets of around \$1 million to participate in the world of hedge funds. This is mainly because hedge funds are limited partnerships that operate like unregulated mutual funds, and therefore carry substantial risk. Hedge funds use a variety of investment strategies, some of which are more conservative, employing little or no leverage, while others carry more risk, using leverage and derivatives. The term *leverage* means that for a given amount of money, an investor can control an asset worth a larger amount.

**Mathematics** Ten years ago Mateo made a valuable long-term investment. He spent \$2,000 on 100 shares of XYZ stock. His 100 shares are now worth \$5,500. What is the percent increase on his investment?

**CONCEPT** **Percents Greater Than 100** Percents greater than 100 represent values greater than 1. For example, if the cost of an object is 250 percent of another, it is 2.5 or  $2\frac{1}{2}$  times the cost.



● **Financial Planning** Money management is the process of planning how to get the most from your income. **How can financial planning help you to have the opportunity to enjoy the luxuries of life, such as entertainment?**

# Personal Financial Planning

## Reading Guide

### Before You Read



Think about some ways you manage your money now and your plans to manage money in the future.

### Read to Learn

- Explain the steps involved in the financial planning process.
- Identify sources of financial information.
- Discuss sources of risk.
- Discuss the consequences of choices.

### The Main Idea

Financial planning provides a solid foundation for making financial decisions. It involves looking at your financial position and setting goals.

### Key Concepts

- Making Financial Decisions
- Sources of Financial Information
- Understanding Risk
- Consequences of Choices

### Vocabulary

#### Key Terms

personal financial planning  
goals  
opportunity cost



Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) for a printable graphic organizer.

### Academic Vocabulary

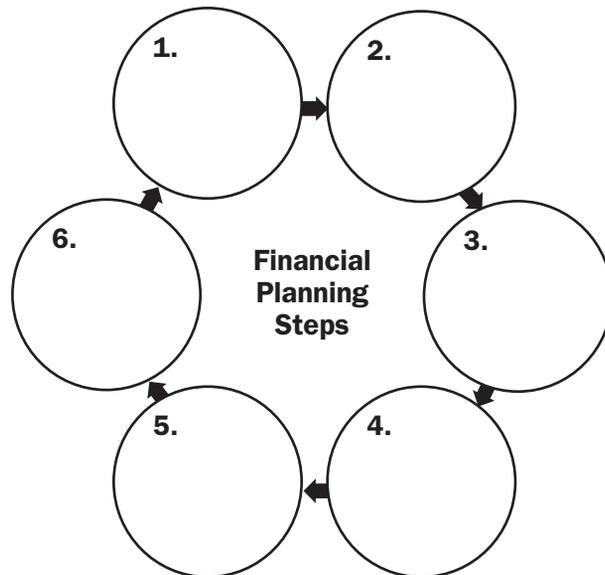
You will find these words in your reading and on your tests. Make sure you know their meanings.

sources  
achieve

revise  
resources

### Graphic Organizer

In a figure like the one below, list the six financial planning steps.



### Academic Standards

#### English Language Arts

**NCTE 1** Read texts to acquire new information

**NCTE 9** Develop an understanding of diversity in language use across cultures

#### Mathematics

**Number and Operations** Understand meanings of operations and how they relate to one another

# Making Financial Decisions

Personal finance refers to all the things in your life that involve money. **Personal financial planning** means spending, saving, and investing your money so you can enjoy the kind of life you want, along with financial security. Everyone has different financial goals. **Goals** are the things you want to accomplish. Getting a college education, buying a car, and starting a business are some examples of goals. Planning your personal finances is important because it will help you reach your goals. The financial planning process has six steps.



**Define** What is personal financial planning?

## Step 1: Determine Your Financial Situation

Once you have determined your financial situation, you will be able to start planning. First, make a list of your savings, monthly income (money you receive, such as job earnings, an allowance, tips, gifts, and interest on bank accounts), monthly expenses (money you spend), and debts (money you owe to others). A good way to estimate your expenses is to keep a careful record of every amount you spend for one month.

### As You Read

Think about how your wants and needs affect your financial goals.

## Step 2: Develop Your Financial Goals

To develop clear financial goals, you will need to think about your attitude toward money. Is it more important to you to spend your money now or to save for the future? What are your wants and needs? Would you rather get a job right after high school or continue your education?



### A Beginning Step

Planning your personal finances will help you reach your goals. **What is the first step in personal financial planning?**



**Making Money** The most common way for teens to earn money is through an allowance. However, many teens do not get an allowance. Some other ways to get money may be by doing work around the house, or as a reward for receiving good grades. *Do you think you should be paid for doing chores or getting good grades?*

### Step 3: Identify Possible Courses of Action

It is important to consider your options before making a decision. Generally, you will have several possible courses of action.

### Step 4: Evaluate Your Alternatives

When you evaluate your alternatives, use the **sources** of financial information that are available. Look at where you are in your life, your present financial situation, and your personal values. Consider the consequences and risks of each decision you make. Your financial goals will help you determine the best option.

### Step 5: Implement a Financial Plan of Action

A plan of action is a list of ways to **achieve** your financial goals. If your goal is to increase your savings, a plan of action could be to cut back on spending. If you want to increase your income, you could get a part-time job or work more hours at your present job.

### Step 6: Review and Revise Your Plan

As you get older, your finances and needs will change. That means your financial plan will have to change, too. You should reevaluate and **revise** it every year.

## BusinessWeek Reader and Case Study

### Follow My Money

**A host of young bloggers have opened their finances for all to see—and learn from.**

Jonathan Ping is not a financial guru. He's not a certified financial planner. And he's not a millionaire (yet). He's simply a 27-year-old engineer living with his wife and dog in a rented house in Portland, Oregon. Within the next 18 months he hopes to scrape up \$100,000 for a down payment on a home, and he wants to build a net worth of \$1 million by age 45. So far he's at \$88,953.

How do I know this? It's in bold type in the top right-hand corner of his Web log, MyMoneyBlog.com, where Ping keeps a daily tally of his progress. He's one of more than 150 bloggers, mostly 22 to 35, who have adopted an open-source approach to personal finance. Most keep their names secret, but that's about all they hide. In stark contrast to

their parents' generation, for whom comparing incomes can be awkward, if not downright taboo, bloggers list financial information down to the dollar in retirement, brokerage, and savings accounts.



**CASE STUDY** Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) for the *BusinessWeek* Reader Case Study.

#### Active Learning

Use a spreadsheet to develop a budget of your daily expenses. Examine your budget carefully to determine which costs meet your values and goals and which ones you could eliminate to save money. Write a journal entry about your findings.

## International Business

### The Euro

In 1957, the Treaty of Rome initiated the objective of a common European market to increase economic prosperity among the people of Europe. The Single European Act of 1986 built on this objective by organizing the Economic and Monetary Union (EMU), which laid out the foundation for a single European currency. Euro banknotes and coins were put into circulation on Jan. 1, 2002. Currently the euro is the currency of several countries in the European Union.

### Examples of Languages Across Cultures

**Q:** In Mandarin Chinese, how do you say “Please” and “Thank you”?

**A:** 請 (traditional) or 请 (simplified) (pronounced: Chēng)

謝謝 (traditional) or 谢谢 (simplified) (pronounced: Shǐ-ě shǐ-ě)

What are some of the benefits of having a common currency throughout Europe? Why have only 12 countries adopted the euro?

## Sources of Financial Information

When making financial decisions, the Internet is a good place to get information on social and economic conditions. Most corporations put facts about their company and financial situation on their Web site. They will also mail information that is requested. Magazines such as *BusinessWeek*, *Time*, and *U.S. News & World Report* and newspapers such as *The Wall Street Journal*, *The New York Times*, and *Financial Times* can also help.

## Understanding Risk

When you make a financial decision, you also accept certain risk. Some types of financial risk include:

- **Inflation Risk** Inflation is a general increase in the cost of goods and services. If you wait to buy an item you want, you risk the possibility that the price will increase.
- **Interest Rate Risk** Interest rates rise and fall, which may affect the cost of borrowing or the profits you earn when you save or invest.
- **Income Risk** Your income may rise or fall. You could lose your job due to unexpected health problems, family issues or other reasons. You could also find a better job or get a raise.
- **Personal Risk** Some choices increase risk. Driving for eight hours on icy mountain roads instead of traveling by airplane may not be worth the money you would save.
- **Liquidity Risk** You may have to withdraw your savings or investments. Liquidity is the ability to convert your financial **resources** into cash easily without a loss in value.

An important part of financial planning is understanding which risks you can afford to take and which ones you cannot. If you decide a course of action is too risky, you might decide to choose an alternative. In some cases, insurance is available to limit your exposure to risk. Diversification of your assets is another way to minimize risk.

 **Reading Check** **Identify** List some types of financial risks.

## Consequences of Choices

An **opportunity cost**, sometimes called a tradeoff, is what you give up when you make one choice instead of another. Suppose you want to become a full-time college student. You would like to work full time, but your work hours would conflict with your class schedule. If you choose to pursue your education, you will give up the opportunity to work full time, at least for a while. The opportunity cost of going to college is working at the full-time job. However, choosing between the alternatives involves more than just knowing what you forgo. It also involves knowing what you gain.

### Section 28.1

#### After You Read



#### Review Key Concepts

1. What are some examples of long-range financial goals that consumers may have?
2. List the steps of the financial planning process.
3. Name some types of financial risk.

#### Academic Skills

4. **Mathematics** The average U.S. family spends about 16% of its income on housing and 12% on household expenses. If a family's monthly income is \$3,125, how much does it spend on housing and household expenses?

**CONCEPT** **The Distributive Property** The Distributive Property states that  $a \times c + b \times c = (a + b)c$ . You can multiply each percent by the monthly income then add the products, or you can add the percents and multiply their sum by the monthly income.



For math help, go to the Math Appendix.



Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) to check your answers.

# Money Management

## Reading Guide

### Before You Read

Think about some steps you can take now in managing your money so that you can get the most from your income.

### Read to Learn

- Discuss the importance of budgeting.
- List the steps for preparing a budget.

### The Main Idea

Meeting your financial goals requires you to know your income and expenses. A budget can enable you to track your spending and make choices about your money.

### Key Concepts

- The Importance of Budgeting
- Preparing a Budget

### Vocabulary

#### Key Terms

money management	expense
budget	fixed expenses
income	variable expenses
gross pay	budget variance
deductions	surplus
net pay	deficit



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### Academic Vocabulary

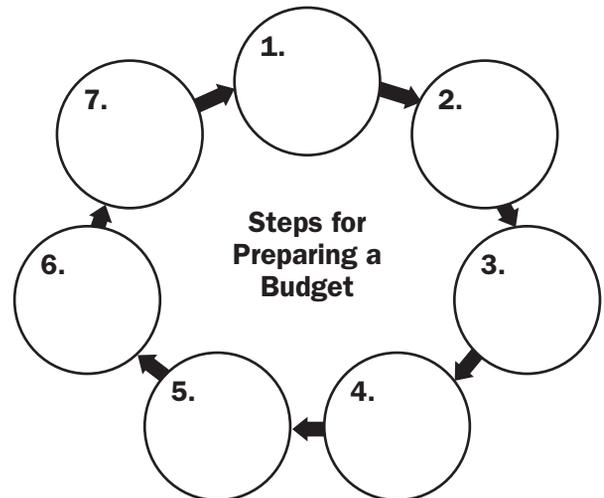
You will find these words in your reading and on your tests. Make sure you know their meanings.

utilize  
hence

intermediate  
major

### Graphic Organizer

In a figure like the one below, list the seven steps for preparing a budget.



### Academic Standards

#### English Language Arts

**NCTE 1** Read texts to acquire new information

**NCTE 7** Conduct research and gather, evaluate, and synthesize data to communicate discoveries

**NCTE 12** Use language to accomplish individual purposes

#### Science

**Content Standard F** Students should develop understanding of science and technology in local, national, and global challenges

**Everyone Budgets**

Families, corporations, and even governments set budgets. The budget of a government is similar to your budget, setting up the intended income and expenses for the year. Nearly all large businesses re-forecast their budgets on a quarterly basis. In the future, annual budgets may be replaced with monthly or rolling forecasts. *What does it mean if a company comes close to delivering its budgeted figures?*

## The Importance of Budgeting

Money management is necessary for consumers, businesses, and governments. **Money management** is a method of planning to get the most from one’s money. Like consumers, businesses and governments must figure out how to **utilize** their income to pay for things they want or need. Income is a limited resource for everyone. Most people want more goods and services than they have money to buy. A budget helps them to set financial priorities. **Figure 28.1** shows average U.S. household expenses.

A **budget** is a plan for using your income in a way that best meets your wants and needs. It includes a record of your expected income, your planned expenses, and your planned savings over a certain period of time. **Hence**, a good budget helps people set priorities for spending and saving and tracks their money.



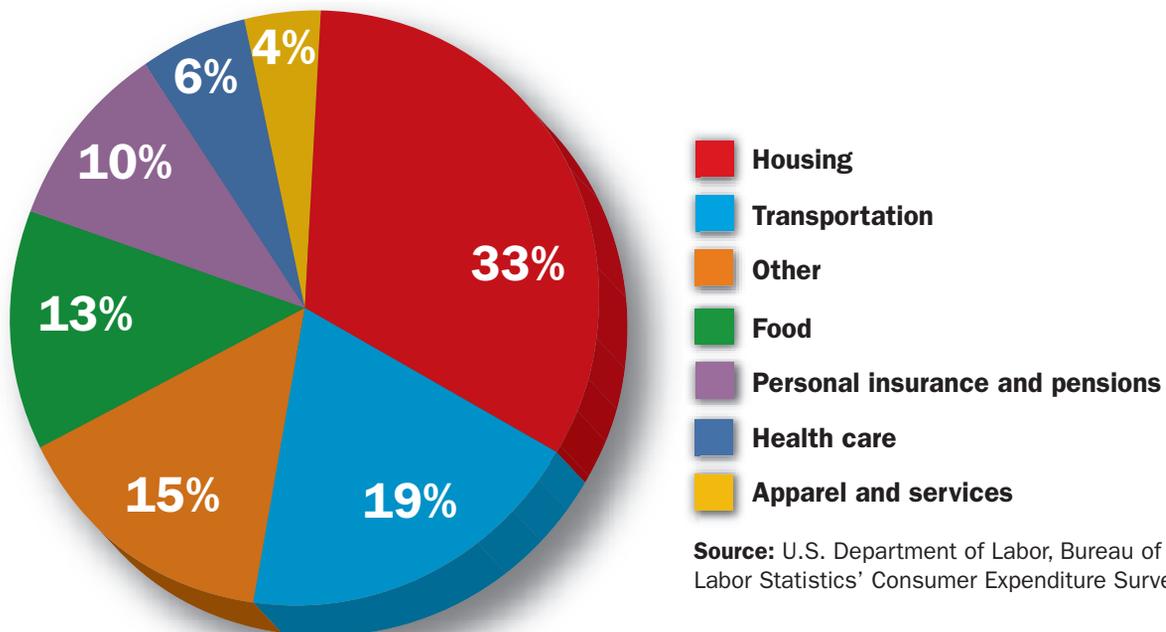
**Reading Check**

**Analyze** Why is income a limited resource for everyone?

## Preparing a Budget

Planning a budget is a seven-step process: Set your goals; estimate your income; budget for unexpected expenses and savings; budget for fixed expenses; budget for variable expenses; record what you spend; and review spending and saving patterns.

**Figure 28.1** – Average Household Expenses



**Source:** U.S. Department of Labor, Bureau of Labor Statistics’ Consumer Expenditure Survey

**The Cost of Living** This graph shows how an average household in the United States spends its money. **If a family earns \$3,000 a month, how much money (on average) would that family spend on housing?**

### Budgeting for IT Productivity

In today's world, most business leaders believe that an organization that does not invest in information technology (IT) cannot survive. Just imagine an office without computers. IT increases productivity. However, while investments in IT are necessary, part of the role of IT professionals is to match productivity gains to technology costs. Productivity is the primary measure of technology's economic impact. It is frequently difficult to measure technology's impact, but as with every other budgetary line item, expenditures must match organizational goals to technology expenditures. When the costs for IT software and hardware are added up, decisions need to be made that narrow the difference between investments in IT and the performance it generates.

### Web Quest

Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) for links to Web sites where you can research ways IT costs influence businesses' investments. Write a few paragraphs describing how IT affects productivity.

## Step 1: Set Your Financial Goals

As you prepare to set your financial goals, you should consider several questions: What do I want to accomplish in the next month? The next year? The next five years? What is important to me? Are my goals practical? A budget should help you decide which goals you can meet with the amount of money you have. You might find it helpful to separate them into short-term, **intermediate**, and long-term goals.

## Step 2: Estimate Your Income

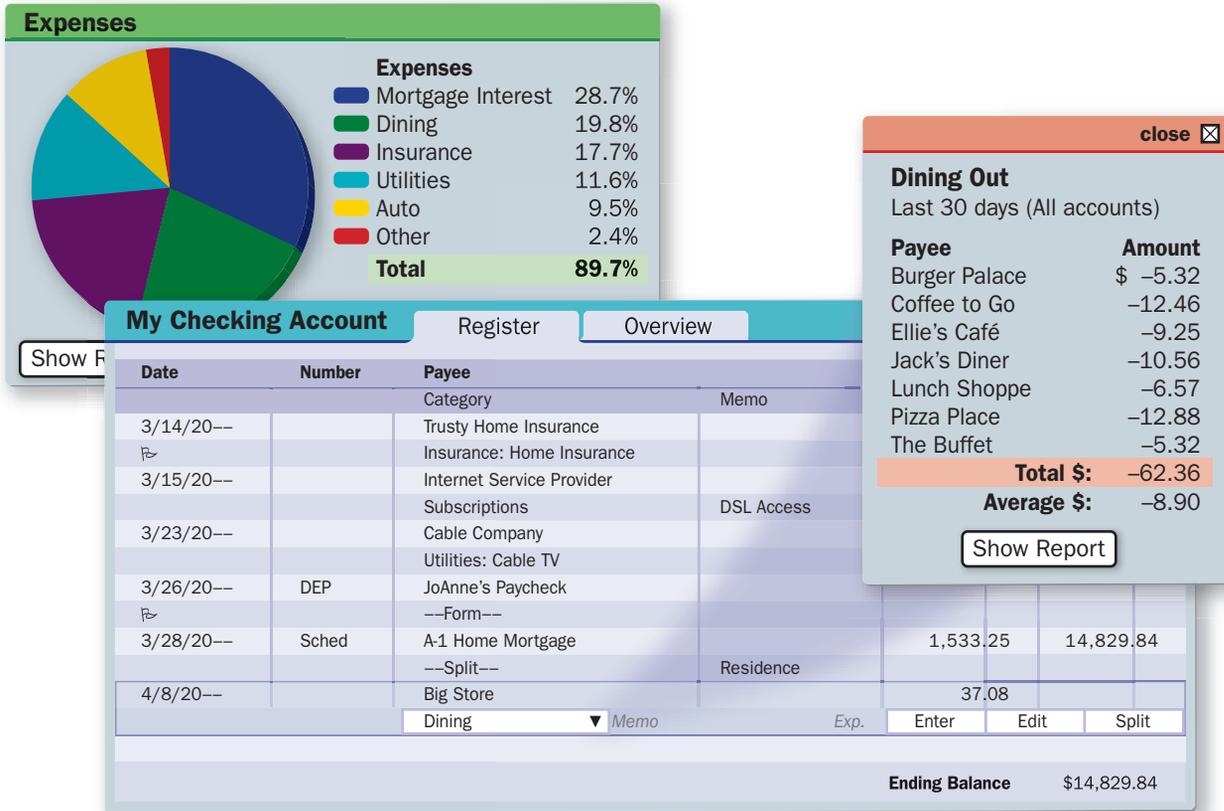
Once you have set your goals, you can begin working on a budget. Start by recording your estimated income for the next month. Your **income** is the actual amount of money you earn or receive during a given period. Include all sources of income that you know you will receive, such as take-home pay and income on investments.

**Pay and Deductions** Your **gross pay** is the total amount of money you earned for a specific time. Your gross pay is reduced by various **deductions**, or amounts that are taken out of your pay before you receive your paycheck. Deductions include items such as taxes, insurance premiums, retirement contributions, and union dues. Your take-home pay, or **net pay**, is your gross pay minus deductions.



**Withholding** Full-time workers pay several kinds of taxes. *Withholding* is income tax withheld from an employee's wages and paid directly to the government by the employer. It is a form of deduction from pay. The funds are applied to the worker's federal, state, and local income taxes as well as his or her contribution to Social Security and Medicare. Self-employed people pay their taxes directly to the government. *Why do you think taxes are withheld from workers' paychecks?*

**Figure 28.2** – *Managing Your Money*



**Budgeting Software** You can use budgeting software to create reports, charts, and graphs that quickly show you when you paid a bill, how much you paid, and to whom. **How might budgeting software make preparing your taxes easier?**

### Step 3: Budget for Unexpected Expenses and Savings

You have to plan for expenses such as food, rent, and clothing to satisfy your basic needs. An **expense** is an amount of money used to buy or do something. You must also plan for unexpected expenses, such as medical visits or accidents. Unexpected expenses could include rises in costs for items such as gasoline. **Figure 28.2** provides a glimpse of budgeting software.

**As You Read**

Think about some unexpected expenses you have had and how they affected your budget.

A budget must also include a plan for savings. Savings make it possible for you to meet future wants and needs. They also protect you against expenses that you did not budget for, that are higher than you expected, or that are completely unexpected. You need a savings plan if your long-term goal is to make a **major** purchase, such as a new computer or a vacation.

When you develop your budget, make sure that the total income figure is the same as the total for planned expenses and savings. If your planned expenses and savings are more than your income, you will have to cut some expenses or find some other source of income.

## Step 4: Budget for Fixed Expenses

**Fixed expenses** are expenses that occur regularly and are regularly paid. They include payments for rent, insurance, and a car loan. The amount of a fixed expense might sometimes change, but it is usually about the same over long periods.

## Step 5: Budget for Variable Expenses

**Variable expenses** are expenses that change and can be controlled more easily than fixed expenses. They include expenses such as food, phone charges, entertainment, and gifts. The amounts for these expenses usually vary from month to month.

## Step 6: Record What You Spend

To find out how practical your budget is, you will need to keep track of your expenses during one month and revise your budget if necessary. The difference between the budgeted amount and the actual amount that you spend is the **budget variance**. This figure can be either a surplus or a deficit. A **surplus** is extra money that can be spent or saved, depending on a person's goals and values. A **deficit** occurs when more money is spent than is earned or received.

## Step 7: Review Spending and Saving Patterns

Budgeting is a continual process. You need to review your budget each month and consider making changes.

### Section 28.2

#### ● After You Read

#### Review Key Concepts

1. What are the seven steps to preparing a budget?
2. What is the difference between gross pay and net pay?
3. How are fixed expenses and variable expenses different?

#### Academic Skills

4. **English Language Arts** Interview someone who is responsible for a budget for a club, business, or other organization. How do goals drive the budget? How often is it revised? How is it monitored? Write a story about your interview for the organization's newsletter.
5. **English Language Arts** What are your goals for the future? Write a description of where you see yourself living and what you see yourself doing in 10 years. Then write a short plan describing the money management techniques you will use in order to meet your goals.



Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) to check your answers.

# Chapter 28 Review and Activities

## Section 28.1 Summary

**Personal Financial Planning** Everyone must make financial decisions. Identifying your financial goals and planning how to get the most from your money are part of personal financial planning. If you plan well and carry out those plans, you can reach your financial goals. To create a financial plan, you need to determine your financial situation; develop your financial goals; identify possible courses of action; evaluate your alternatives; implement a financial plan of action; and review and revise your plan. Often financial planning means you must research options so that you can evaluate risk and make wise choices.

## Section 28.2 Summary

**Money Management** A budget is a tool for getting the most from your income. With a budget, you can estimate your income and expenses and track your financial progress over time. Income and expenses often vary over time, so a part of budgeting is reviewing your goals, revising them, and adjusting your budget as needed. To create a budget, you need to set your financial goals; estimate your income; budget for unexpected expenses and savings; budget for fixed expenses; budget for variable expenses; record what you spend; and review your spending and saving patterns. Budgeting is an ongoing process.

## Vocabulary Review

1. On a sheet of paper, use each of these key terms and academic vocabulary terms in a sentence.

### Key Terms

personal financial planning goals	deductions
opportunity cost	net pay
money management	expense
budget	fixed expenses
income	variable expenses
gross pay	budget variance
	surplus
	deficit

### Academic Vocabulary

sources	utilize
achieve	hence
revise	intermediate
resources	major

## Review Key Concepts

2. Explain the steps involved in the financial planning process.
3. Identify sources of financial information.
4. Discuss sources of risk.
5. Discuss the consequences of choices.
6. Discuss the importance of budgeting.
7. List the steps for preparing a budget.

## Critical Thinking

8. Why is it important to plan for spending, saving, and investing your money?
9. "People always have a choice: to use their money on a good or service, or to invest or save the money." Do you think this statement is true? Why or why not?
10. Sometimes people are willing to delay making a purchase so they can buy something better later. This concept is known as delaying gratification. What effect do you think delaying gratification can have on budgeting?
11. Some people think of their income as the total amount that they earn, not the amount that they actually receive in their paycheck. What effect will that thinking have on their ability to live within a budget?
12. What do you think is the most difficult part of budgeting? Why?
13. How do your spending habits affect your standard of living? What are some unexpected expenses that you may have that will affect your budget?
14. What suggestions would you give to someone who thinks that savings are not an important part of budgeting and money management?

## Write About It

15. Estimate how much money you need for an item you would like to buy in the future. Write a brief essay about items that you could forgo buying now to have that item. When do you think you can achieve your goal?
16. Some people think money is something that they can always get. Others think that money must be conserved and used wisely or it will not be available when needed. Write two or more paragraphs about your thoughts on each statement.
17. What are your goals? In two or more pages, describe where you see yourself living and what you see yourself doing in 10 years. What personal financial planning methods will you use to meet your goals?
18. Why is opportunity cost an important concept for people to consider in their decisions about personal financial planning? Explain your answer in two or more paragraphs.
19. Check in the yellow pages of your local phone book, a local newspaper, library, or online to find information about personal financial planning assistance available in your community. Write a summary of information you find.

## Technology Applications

### Spreadsheet Software

20. Early planning for college or postsecondary training is important. Use a spreadsheet to prepare a summary of the costs of a college education or training program. Visit Web sites for training and education institutions to find tuition and fees, estimated room and board costs, and costs for books and supplies.

## Business Ethics

### Family First or Strictly Business?

21. Suppose you work as a financial planner for a well-known novelist who is also very wealthy. Your duties include advising her on personal investments. You have a brother who owns a struggling online business. He asks you to advise your client to invest in his company, pitching it as a "hot new dot-com." What should you do?

# Chapter 28 Review and Activities

## Applying Academics to Business

### English Language Arts

22. Look for a paragraph in this chapter that describes a cause-and-effect relationship. Find another paragraph that has a topic sentence supported by details. Finally, find an example of a sequence of events.

### Mathematics

23. Find a picture of a big-ticket item you would like to own. Figure out the equivalent cost in movies (at \$7 per movie) and in dining out (at \$9 per meal) for the item. For example, if an MP3 player costs \$149, its cost-equivalent is 21 movies or 16 restaurant meals. Assuming that you see three movies per month and eat out seven times, make a plan for saving enough money to purchase your big-ticket item by eliminating one or more monthly movies and restaurant meals. Write a few sentences describing your plan.

**CONCEPT** **Problem Solving** You might start by computing how much you spend on movies and dining out each month. Then decide what you are willing to eliminate to save to buy the item you have chosen.

### English Language Arts

24. Based on the concepts you have read about in this chapter, write a word that means the opposite or almost the opposite of each of the following:

income  
gross pay  
variable  
unplanned

### Mathematics

25. Americans save less than 5% of their income. Other countries have a higher percentage of savings per capita, including Belgium (22%), Denmark (16.2%), and Japan (15.7%). Research the average per capita savings of at least 10 countries and display your findings in a bar graph.

**CONCEPT** **Bar Graphs** Bar graphs can be designed so that the bars are horizontal or vertical. Each bar represents the quantity associated with a different category, in this case, the per capita savings of a country.

## Active Learning

### Financial Planning Software

26. Interview two or more people who use budgeting or financial planning software to organize financial information. Ask them how technology has affected their records and financial planning. Do they believe they are better money managers because they use the software? Write a summary of the information you learned.

## Business in the Real World

### Investing in a Corporation

27. An annual report is a corporation's yearly review of activities, especially its financial dealings. Choose a corporation, and research its annual report, either online or by contacting the company. Read the report's overview and highlights. Did the company meet its goals? Why or why not? Would you consider investing in it? In a two-page paper, explain your answers.

## Real LIFE skills

### PREPARING A PERSONAL BUDGET

28. Select a college or technical school that you might like to attend after school. Obtain information on tuition and other fees. Add the cost of food, shelter, clothing, books, and any other items you think are part of the cost. Estimate the total cost of the education. Then estimate how you will pay for it. Prepare a budget for the time you will seek the education.

## COOL Business CAREERS

### FIND YOUR DREAM JOB

29. Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) for a link to the Occupational Outlook Handbook Web site. Click on the “OOH Search/A-Z Index” link and enter “budget analysts.” Write a one-page report about the job. Conclude your report with a list of things you could do now to prepare yourself to pursue the occupation.

## Role Play

### A BUDGET FOR YOUR MARCHING BAND

30. **Situation** Your school’s marching band has asked for your help in preparing the band’s budget for the upcoming year. You and three of your classmates are meeting to identify ways it can raise money and plan a budget.

**Activity** Hold a meeting to plan ways to raise money and to prepare a proposed budget. The band has \$435 in the treasury.

**Evaluation** You will be evaluated on how well you meet the following performance indicators:

- Identify three or more ways the marching band can raise money.
- Prepare a list of expected expenses for the marching band.
- Prepare a proposed budget.
- List steps that the band members can take to meet their goals.
- Communicate with others, and use correct grammar.

## Standardized Test Practice

**Directions** Choose the letter of the best answer. Write the letter for the answer on a separate piece of paper.

### 1. Which punctuation mark, if any, is needed in the sentence?

Samantha asked her accountant “Would it be better to cut my budget for housing, increase my income, or save less each month?”

- A , (comma)
- B . (period)
- C ; (semicolon)
- D The sentence is correct as it is.



**TEST-TAKING TIP** Keep your family members informed about your test schedule. They can help you with your studies and provide encouragement.



**READING** Go to the *Introduction to Business* Online Learning Center through [glencoe.com](http://glencoe.com) for a list of outside reading suggestions.