Essential Standard 4.00
Understand the role of finance in business.

Objective 4.03
Understand saving and investing options for clients.

Topics
• Saving and investing basics
• Saving and investing options
• Evaluation factors for savings and investing options

Saving and Investing Basics

• Reasons money is borrowed by the following:
  – Individuals: People usually borrow money to purchase large ticket items such as homes and cars.
  – Businesses: Businesses usually borrow money to operate or expand their business, which may include purchasing a building, replacing old equipment, or offering new products.
  – Government: The Government may borrow money to improve or expand transportation, schools, or other public services.

Saving and Investing Basics

• What is saving?
  – Saving is putting away money for future use.

Saving and Investing Basics

• What is investing?
  – Investing is using savings to earn more money for future financial security.

Saving and Investing Basics

• Saving influences on economic activity
  – Saving influences the economy by making more money available to be used by individuals, businesses, and the government. When the borrowed money is spent, the demand for goods and services is increased, which creates more jobs and spending for workers.

Saving and Investing Basics

• Main goals of savers and investors include making available immediate income and long-term growth.

Saving and Investing Basics

• Growth of savings is interest earned when others borrow your money.
  – Simple interest is the amount of money paid to saver on amount deposited for a period of time.
  – Compound interest is the amount of money paid to saver on money deposited and interest previously earned for a period of time.

Saving and Investing Basics

• Impact of compound frequency on savings growth rate - The more times that interest is compounded the more growth of savings.

Saving and Investing Basics

• How is simple interest calculated?
  – Simple interest is calculated by using the formula (P=Principal, R=Rate, T=Time and I=Interest Rate)

Saving and Investing Basics

• How is compound interest calculated?
  – Compound interest is calculated by using the formula (A=Amount, P=Principal amount/the initial amount you borrow or deposit, r=Annual rate of interest and n=Number of times interest is compounded)

Savings Growth

Simple interest

$1,000 at 10%

Year 1: $1,000 * .10 = $100

Year 2: $1,000 + $100 = $1,100

What would the value be at the end of year 3?

Compound interest

$1,000 at 10%

Year 1: $1,000 * .10 = $100

Year 2: $1,100 * .10 = $110

What would the value be at the end of year 3?

Saving Options

Savings Plans

– A savings account usually allows low or zero balance, deposit or withdrawals anytime and interest to be earned. Usually withdrawals are allowed without penalties.

– Certificates of deposits (CDs) requires a minimum deposit, money to remain deposited for a period of time without penalties. Penalties may be assessed if money is withdrawn before specified time.

– Money market account requires a minimum deposit and interest is earned based on government and corporate securities. Usually withdrawals are allowed without penalties.

Main Categories of Investing Options

• Stocks
• Bonds
• Mutual Funds and Exchange-traded Funds
• Real Estate
• Commodities
• Collectibles

Stock Investments

• Two main categories of stock:
  – Preferred stock pays dividends at a set rate.
  – Common stock represents general ownership in company and sharing of profits.

• What are stockbrokers?
  – Stockbrokers buy and sell stock and bonds at a set price for a commission for stockholders.

• Stock exchange
  – The stock exchange is where the trading of securities take place.

• What is market value of stock?
  – The market value of stock is the price for which a share of stock can be purchased.

Stock Investments

• What are the major similarities and differences between preferred and common stocks?
  – Major similarities between preferred and common stock are:
    • Both have investment risks and pay dividends
  – Major differences between preferred and common stock are:
    • Preferred stock pays dividends before common stock is paid.
    • Preferred stockholders do not have voting powers; but common stockholders are invited to annual corporate meetings and permitted to one vote per share of stock owned.
    • Preferred stock is less risky than common stock.

Stock Table

Year 1 $1,000 at 10%

Year 2: $1,000 + $100 = $1,100

Year 3: $1,100 + $110 = $1,210

What would the value be at the end of year 3?
Selecting Stock

Factors that could influence investors in selecting stock:

- **Economic**
  - Inflation
  - Interest rates
  - Consumer spending
  - Employment

- **Company**
  - Dividend yield is the amount paid per share for stock.
  - Price-earnings ratio is the relationship between a stock's selling price and its yield.

**Yield Calculations**

Yield is usually calculated in the following way:

\[
\text{yield} = \frac{\text{current value} - \text{original value}}{\text{original value}} \times 100\%
\]

For example:

- A stock is bought at $40 and valued at $43:
  \[
  \frac{43 - 40}{40} = \frac{3}{40} = 0.075 \text{ or } 7.5\%
  \]

**Yield Calculations**

Dividends also may be added to the calculation.

For example:

- A stock is bought at $40 and sold at $43, but also earned a $2 dividend during that time:
  \[
  \frac{43 + 2 - 40}{40} = \frac{5}{40} = 0.125 \text{ or } 12.5\%
  \]

**Bond Investments**

- What is a bond?
  - A bond is a promissory note to pay back a specified amount of money at a stated rate on a specific date.
  - Bonds are issued to lend funds to the organization selling the bond.

**Main Categories of Bonds**

- **Government bonds**
  - Municipal bonds are issued by local and state governments for public service projects.
  - U.S. savings bonds
  - The federal government issues Series EE bonds, HH bonds, and I bonds. Also the federal government issues Treasury bills and notes.
  - The EE bond interest is paid once the bond is cashed. The HH bond interest is paid twice a year, which may be considered income.
  - Treasury bills and notes
  - The treasury bills and notes differ by their maturity time frame. Treasury bills may reach maturity between 91 days to a year; whereas treasury notes take one to ten years.

- **Corporate bonds**
  - Purchasing corporate bonds is a means of loaning money to a company.

**Lenders versus owners as it relates to investing in a company's stocks and bonds**

- How does stated interest rate impact the value of a bond?
  - The stated interest rate usually determines the price investors want to pay for a bond. If a bond's stated interest rate is lower than similar ones, investors will most likely want to pay less for the bond. If the stated interest rate is higher than similar ones, the seller will most likely want to be paid more than its face value.

**Mutual Funds**

- Companies assist investors of mutual funds by studying companies' stocks and bonds, and then buying a variety of stocks and bonds to sell.

Some examples of mutual fund categories:

- Aggressive-growth stock funds look for quick growth but also have a higher risk than other stock.
- Income funds concentrate on stocks that pay regular dividends.
- International funds invest in a variety of company stock around the world.
- Sector funds purchase stocks of companies in the same industry.
- Bond funds concentrate in corporate bonds.
- Balanced funds invest in both stocks and bonds.

**Exchange-traded Fund (ETF)**

- An exchange-traded fund (ETF) is a portfolio of stocks, bonds, or other investments that trade on a stock exchange like regular stock.

**Other Investments**

- Real Estate includes land and anything attached to it.

Some advantages of investing in real estate are:
- Tax benefits
- Increased equity
- Pride of ownership

Some disadvantages of investing in real estate are:
- Property taxes
- Interest payments
- Property insurance
- Maintenance

Some real estate examples may include:
- A house
- A condominium
- A mobile home park

- Commodities and futures

- Commodities include grain, livestock, and precious metals.

- Commodity investors usually agree to buy and sell for an amount at a specified price in the future.

Some examples may include:
- Rice
- Cattle
- Gold

- Collectibles

- Collectibles are items collected over time that may increase in value.

Some examples may include:
- Artwork
- Antique furniture
- Autographed items

**Evaluation factors for savings and investing options**

- Safety and risk
- Potential yield
- Liquidity
- Taxes