Choose to Save

Advanced Level

Saving money is an essential part your financial plan. When you save you accumulate funds by intentionally spending less than you earn. **Savings** is the portion of income not spent on **consumption** (the purchase of goods and services).

An important reason to have savings is for emergency expenses. Without savings, paying cash for an unexpected expense may be difficult. **Emergency savings** (cash set aside to cover the cost of unexpected events) creates a sense of financial security. The lack of an emergency fund not only creates financial stress, but also drives the consumer into debt.

Savings contributes to your net worth (wealth) and is recorded as a financial asset on your ***Statement of Financial Position***. Be sure this financial asset (your emergency fund) is in an "easily-accessible" account (usually a savings account) that can be accessed in a day or two without penalty. Financial assets easily converted into cash are called *liquid*. **Liquidity** is defined as how quickly and easily you can access your assets and convert them into cash.

What are examples of emergency expenses a household may encounter?

How much money to save

Most experts recommend having between 3-6 months of expenses put aside in emergency savings. Let's say your goal is to save six months of expenses. If you normally have $2,000 in expenses each month then you should try to build up a total of $12,000 in emergency savings. Be careful not to confuse the funds you've saved for emergencies with funds you'd like to spend on vacations with friends and family or on big expenses like a new flat screen TV or newer furniture. Emergency funds are just that; funds set aside only to be used in an emergency!

How to save money

Saving is an important part of setting and reaching financial goals. Your goal may be to build your emergency savings fund or to buy a car, new furniture or the down payment on your first home. You begin by setting your financial goal and working backwards to determine a realistic amount you can save during a specific time period. Saving money for future consumption always requires not purchasing something today. You must ensure the trade-offs are realistic and the opportunity cost of what you are giving up won't negatively impact your well-being.

What savings goal do you have in place?

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How to save money continued…

Your spending plan helps you determine how much you can save based on your income and expenses. A frequent assessment of what you spend your money on is a good habit to develop.

Here are a few money-saving suggestions:

- Examine current spending – Examine expenses in your ***Income and Expense Statement*** and your ***Spending Plan*** to determine changes that can be made to decrease your spending. Start with small expenses (your daily coffee shop drink, new clothes) and then review your larger expenditures (cable and cell phone plans and sometimes grocery bills) to see if there are opportunities to decrease your spending.

  The following are tips to decrease spending:

  1. Communication - Could you cancel your cable/satellite television or reduce the cost of your current package? Could you reduce the cost of your cell phone package? Could you drop your home Internet and use public Internet at places such as a library?
  2. Food - Could you eat at restaurants less? Could you purchase items in bulk instead of at a vending machine or gas station?
  3. Transportation - Could you use public transportation instead of owning a vehicle?
  4. Housing - Would you consider moving to a smaller or less expensive home or apartment in order to reduce your mortgage/rent payment and/or utilities?

> It may be difficult to decrease or remove contractual expenses from your spending plan. With a contractual expense, you have signed a contract that requires you to pay that expense for a specific amount of time. Make sure to consider the consequences of a contract before signing.

After reviewing your monthly expenditures, if you still can't reach your saving goal you might consider:

1. **Increasing your income** by lobbying for a raise, switching to a job that pays more or taking on a part time job if even only for a short period of time to increase your savings.
2. **DIY** – You've seen the "do it yourselfers" on TV, so why not try a couple of personal tasks on your own. Not only can this save you money (if you do it right the first time!) it but it can also give you a sense of accomplishment! However, the cost to you of doing something on your own is your investment of time (and materials) in place of the money you otherwise would spend. Make sure you are willing to give up the time and have the proper skills needed to complete do it yourself tasks.

   The following examples are Do It Yourself (DIY) activities:

   - Food - Pack your lunch and prepare food/beverages from scratch instead of purchasing ready-to-eat items such as coffee and frozen meals.
   - Transportation – Develop skills that allow you to take care of very basic vehicle maintenance and repairs.
   - Housing - Maintain the inside and outside of your home; visit your local home improvement center to learn about home DIY projects.

What are three ways you could start saving today?

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Income and Expense Statement for:	
Expenses	
Deductions Often Taken from Paychecks	
Contributions to retirement programs (401k, 403b, pension, IRA)	
Federal income tax and state income tax	
Social Security and Medicare	
Saving and Investing (Pay Yourself First)	
Contribution to savings and investments	
Insurance Premiums	
Health, automobile, home or renters, life	
Housing Costs	
Transportation Costs	
Food Costs	
Family Member Care	
Communication and Computers	
Telephone landline, cell phone, Internet, cable/satellite television	
Medical Costs Not Covered by Insurance	
Clothing and Personal Care	
Educational Expenses	
Pet Care	
Entertainment	
Gifts and Charitable Contributions	
Credit Costs	
Student loan, credit card, other loan payments	
Total Expenses	$
Net Gain or Net Loss (Income less Expenses)	$

Having solid savings habits helps you reach your financial goals. A successful saving strategy for many is to "**pay yourself first**." Paying yourself first means saving for the future by putting money aside ***before*** paying your regular monthly bills or using your income for discretionary purchases.

Make paying yourself first automatic. Ways to accomplish this include:

- Automatic transfers - Most depository institutions allow you to set up automatic transfers among accounts within their depository institution or to accounts at other institutions. Once the initial setup is complete, the money is automatically moved from one account to another on dates designated by you.
- Payroll Deduction - Many employers offer payroll deduction to employees. With this type of payroll deduction, you designate a certain percentage or specific amount of your paycheck to be deposited into an account of your choice.

Many resources are out there to help you reach saving goals. Websites like https://secure.piggymojo.com and http://www.stickk.com, help you develop goals and stick to them with peer support. Internet-based spending plan programs such as https://www.mint.com, and programs offered by depository institutions offer goal tracking through online/mobile banking.

Increasing the value of money

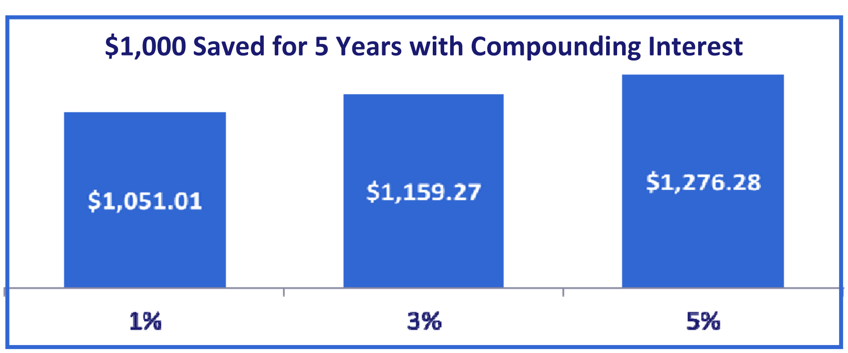
Saved money can increase in value while providing for your future. ***Time value of money*** is the idea that money available at the present time (today) is worth more than the same amount if received in the future. That's because if you have it today, it can grow over time. Understanding this core principle of personal finance will help motivate you to save early and often. The factors that affect the size of your savings balance in the future are time, the interest rate, and the amount you save each period.

Interest rate

Interest is the price paid for using someone else's money. The **interest rate** is the percentage rate used to calculate interest. Interest is earned (if you are the lender) or paid (if you are the borrower). When you save money in an interest earning account you earn interest. Savings tools are products offered by depository institutions that, in most cases, allow your deposits to earn interest.

If you don't withdraw the interest earned from an account, the interest has an opportunity to earn additional interest. Earning interest on interest is known as **compound interest.**

Graph 1 is an illustration of how higher interest rates and compound interest increase the value of savings.



To maximize your return:

- Save at the highest interest rate possible!
- Save for as long as possible!
- Save as much as possible, as often as possible!

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Time

Time is necessary for money to increase in value. The longer you save, the more time your money has to grow. Take Felix and Savannah for example:

Felix's parents began saving $50.00 per month for Felix's college education when he was born, and saved until he was 18. Savannah's parents waited until she was a freshman in high school and only had 4 years to save until she turned 18. Both accounts earned the same interest rate (6%) and had the same balance when the students turned 18 (about $19,500). However, Savannah's parents had to save significantly more ($350/month) to reach the same savings goal, because they started later.

Felix

Saved for: 18 years

Contributed: $50/month

Total Contribution: $10,800

Interest Earned: $8,856

Total Balance: $19,656

Savannah

Saved for: 4 years

Contributed: $350/month

Total Contribution: $16,800

Interest Earned: $2,676

Total Balance: $19,426

Amount of Money

The more you save, the larger the value of your savings will be. The **principal** is the original amount of money saved or invested. Table 3 illustrates the difference in value for different amounts of principal if left to grow at 3% interest for 5 years.

3% interest for 5 years	
Principal	Value of Savings
$100	$115.93
$1,000	$1,159.27
$10,000	$11,592.74

***Your present self impacts your future self.* By saving money today you will have financial security in the future**

What are you willing to give up today to start saving for your future?

Saving is an essential component of your financial plan. Having savings reduces future financial uncertainty and negative emotions such as stress by helping to ensure you will be able to immediately pay for unexpected expenses with cash. An added bonus of saving money is the opportunity for savings to increase in value if saved in an interest-earning account... Saving money will require that trade-offs be made. Saving money for future consumption will always means that you give up the purchase of something in the present. Once a commitment to saving money has been made, saving is best accomplished if you automatically pay yourself first.