# Financial Literacy

Understanding personal finance helps you

1. Make the right decisions on future investments
2. Prepare for critical life milestones and goals
3. Manage sudden, unexpected events - at least for the short term.
4. Control your expenses
5. Reduce your stress

# The 5 Basics of Financial Literacy

1. The Personal Budget
2. The Impact of Interest
3. Saving Money
4. Credit & Debt
5. Identity Theft & Safety Issues

# 1 – Creating a Personal Budget

**Step 1: Identify all sources of income**

Income: money received by a household on a regular basis. salaries, pensions, child allowance, tax refunds.

**Step 2: Identify all areas of expenses**

Include fixed and variable expenses, along with savings set aside for future goals.

**Step 3: Calculate the difference between income and expenses**

If the result is positive (+), you are spending less than you are earning. If your result is negative (-), you are not spending within your means and should reduce your variable expenses.

# 2- The Impact of Interest

- **Interest** is the cost (premium) paid for the use of money. It is usually calculated on a monthly or annual basis, and is quoted as a percentage (%) of the money that has changed hands.

- When you deposit money in a savings account, you are allowing a bank to use your money, therefore the bank will pay you an interest premium for this activity. If a bank or other lender has lent you money, then you will pay them an interest premium.

- **Simple interest** means that interest is calculated on the <u>original</u> amount of money for each period of time; therefore, the interest premium will be exactly the same in each period.

- **Compound interest** is calculated on the <u>current</u> amount of money in each period, which will include the interest gained from the previous period .

# Simple vs. Compound Interest

| | Simple interest earned | Compound interest earned |
|---|---|---|
| **Initial Deposit** | $10,000 | $10,000 |
| Year 1 | $1,000 | $1,000 |
| Year 2 | $1,000 | $1,100 |
| Year 3 | $1,000 | $1,210 |
| Year 4 | $1,000 | $1,331 |
| Year 5 | $1,000 | $1,464.10 |
| Year 6 | $1,000 | $1,610.15 |
| Year 7 | $1,000 | $1,771.56 |
| Year 8 | $1,000 | $1,948.72 |
| Year 9 | $1,000 | $2,143.59 |
| Year 10 | $1,000 | $2,357.95 |
| **Total Interest** | **$10,000** | **$15,937** |

Example of $10,000 invested for 10 years at 10% with simple interest, versus that same $10,000 invested with compound interest:

As you can see, the compound interest method results in an additional $5,937 in interest revenue earned.

# Compound Interest - High Interest Costs

- Using credit cards and retail store cards are a very expensive way to borrow money, being that they act as a short-term loan option.

- When you use a credit card or store card, there is a grace period (usually up to 45 days) during which no interest is charged. However if you do not pay the card off in full during this grace period, the interest rates can be quite high, often exceeding 20% of the value of the loan.

- Because this loan involves compound interest, it quickly rises and the sum can be significant.

- Short-term loans from a bank and personal lines of credit are also high interest and expensive loan options.

# Credit Card Interest Example – NOT CLEAR

- A purchase of $5,000 is made with a credit card at an 18% annual compound interest rate.

- The minimum monthly payment on this credit card balance would consist of the monthly interest plus 1% of the current principal amount (this minimum payment would equal $133.33 after the first month of interest is charged).

- If only minimum payments are made, it would take 277 months for the credit card balance to be paid off in full, at a total of $7,723.49 ($2,723.49 in interest charges)

- As you can see from this example, compound interest on credit card purchases can add up to significant amounts very quickly

# Compound Interest Example

Compound interest can also be viewed as “interest paid on interest” that causes a snowball affect (or compounding) that can rapidly grow your wealth.

To maximize compound interest, it’s important to start early and plan to save for a long period of time.

The gains from compound interest matter more towards the end of your saving years.

| | **Interest rate 2%** | | |
|---|---|---|---|
| | Compound Interest | | |
| Year | Investment | Interest | Total |
| 1 | 10,000 | 200 | 10,200 |
| 2 | 10,200 | 204 | 10,404 |
| 3 | 10,404 | 208 | 10,612 |
| 4 | 10,612 | 212 | 10,824 |
| 5 | 10,824 | 216 | 11,041 |
| 10 | 11,951 | 239 | 12,190 |
| 20 | 14,568 | 291 | 14,859 |
| 30 | 17,758 | 355 | 18,114 |

# 3 – Saving Money – some tips

Saving is an important aspect of maintaining a healthy financial household. Learning to save early on can help you gain essential knowledge, practices and skills that will be useful throughout life.

***Save Salary Increases*** and maintain your living expenses based on your prior salary amount.

***Automate Your Savings*** - Most banks will provide the option for you to send part of your paycheck to a savings account. (the percentage is up to you).

***Write Down Your Savings Goals*** and keep them visible. Although this method is simple, it has proven to be highly effective.

***Saving Later in Life*** - If you are starting to save in your 40's or 50's, it is important to save as much money as possible.

# 4- Understanding Credit & Debt

| Understanding Credit |
|---|
| The most common use of credit for most people is with a credit card |
| It is critical not to miss payments, even if you are only making the minimum monthly payment. If no payment is made within 30 days of the due date, credit card companies will report the incident to national credit bureaus |
| It is important to know your Credit Score – This is a number calculated based on your credit history. It helps lenders identify how much risk they may be taking in lending you money and your odds of successful repayment. |

| Understanding Debt |
|---|
| Good Debt - Debt that creates value and increases future wealth. Education loans, home mortgages and business loans are all examples of good debt. Typically, good debt options have lower annual compound interest rates. |
| Bad Debt - Debt used to purchase disposable items that quickly decrease in value.  For example, clothing bought with a credit card or retail store card. |

# 5 - Identity Theft & Safety Issues

- ***Identity Theft -*** refers to the act of acquiring and collecting someone else's personal information for criminal use or purposes.
- Identity theft techniques can be unsophisticated, such as sorting through physical trash or stealing mail.
- Technology (mainly the Internet) is used for more complex schemes such as email phishing and hacking, as criminals gather profiles of potential victims. Computer spywares and viruses which are designed to help thieves acquire personal information are an emerging trend.
- Victims of identity theft or fraud can experience financial loss and difficulty obtaining credit or restoring their "good name"

# Understanding Identity Theft

Identity thieves are looking for the following information:

- Full legal name
- Date of birth
- Social Insurance Numbers
- Full address
- Mother's maiden name
- Username and password for online services
- Driver's license number
- Personal identification numbers (PIN)
- Credit card numbers, expiry dates and the last 3 digits on the signature panel
- Bank account numbers
- Signature
- Passport number

# Types of Identity Fraud

Identity thieves may use the stolen information to gain access to financial accounts, hack into online accounts, and/or defraud others.

Another form of identity theft is when someone sets up accounts on social media websites using your name and/or other information. While this may not cause you financial harm, it can damage your reputation.

Once they access your personal information, identity thieves can also:

- Spend money from your online accounts
- Open new bank accounts
- Change passwords and contact information for your online accounts
- Apply for loans, credit cards and benefits in your name
- Rent an apartment or car in your name
- Commit other crimes using your credentials

# Ten Tips to Help Protect Against Identity Theft

- Store ID cards and documents in a secure place
- Shred any documents and items with personal information once you no longer need them
- Check balances on your statements from banks, credit cards and companies regularly to look for fraud
- Avoid giving out any personal information over the telephone unless you know the company
- Change your online passwords often and make sure they’re strong
- Avoid posting personal information online such as your date of birth and mailing address
- Before giving your credit card number or financial information to an online company, make sure its website is secure
- Make sure your computer’s anti-virus and other security features to detect malware are up-to-date
- Be aware that government organizations, financial institutions and police will **never** email or text to ask for your financial information
- Never click on a link from a spam message, especially when it promises rewards, prizes or any exclusive information

Thank You!

Questions ? Comments?

*(contact information)*