



Tashkent State University of Economics

Household finance

Lecture 9: Trust and household financial choices.

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Managing Your Own Financial Affairs

You Have the Ability

- ▶ **America is still the land of opportunity even with a 42% average tax burden. You have the right to succeed or fail in business and investment.**

You Need a Roadmap

- ▶ **You must have a specific blueprint that outlines and details where you are and where you want to go.**

There are Six Fundamental Steps in the Managing Process



The Personal Financial Management Process

Steps:

- 1. Establish Your Financial Goals
- 2. Get Started Now--
- 3. Let Time and Compound Interest Work for You
- 4. Buy Right Life Insurance
- 5. Beat Uncle Sam With a Retirement Plan
- 6. Invest for the Future Using Common Stocks

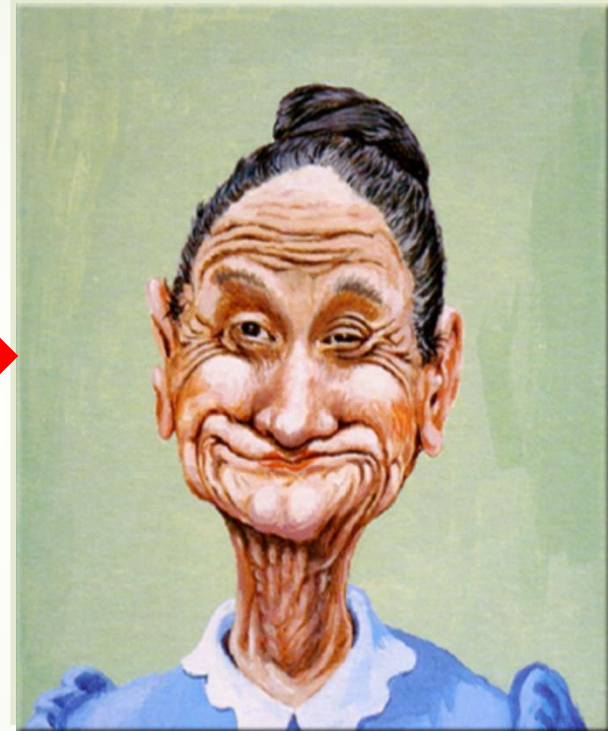


1. Establish Your Financial Goals

A. How Much Will You Make in Your Lifetime?

<u>Income</u>	<u>Earnings</u>
\$20,000	\$ 800,000
\$25,000	\$1,000,000
\$30,000	\$1,200,000
\$40,000	\$1,600,000
\$60,000	\$2,400,000
\$80,000	\$3,200,000

A Retirement Example



From This

to

This

(In forty years)

1. Establish Your Financial Goals (continued)

- *Assuming an average income of \$50,000 per year, how much do you need at retirement?*

We make the assumption that you will need approximately 80% of your disposable income upon retirement (\$40,000 per year for 20 years).



Establish Your Financial Goals (continued)

- **Assume you would like to retire in 40 years on the equivalent of \$40,000 in today's purchasing power.**
 - 1) **Assume CPI is equal to 7.04 in 40 years (equivalent to 5% inflation)**
 - 2) **Therefore your income must be $\$40,000 * 7.04 = \$281,600$**
 - 3) **Assume you want a 20 year annuity at age 65 that pays \$281,600 per year. You must have \$2,103,395.**
 - 4) **Therefore, over the next 40 years you must save \$2,742 per year assuming a return of 12% per year. The monthly equivalent is \$228.50 or 6.9% of disposable income.**



Establish Your Financial Goals (continued)

- **Sources of Additional Income**
 - 1) *Reassess your priorities through a budget*
 - *Disposable Income Less Expenses = Available Discretionary Income*
 - 2) *Adjust Your Lifestyle*
 - 3) *Earn Additional Income*
 - 4) *Realign Your Expenses*
 - 5) *Avoid CREDIT*





2. Get Started Now

A. Time Value of Money

\$1,000 invested Every Year Has a Value of:

<u>%</u>	<u>20yrs</u>	<u>30yrs</u>	<u>40yrs</u>
5%	\$ 33,066	\$ 66,439	\$ 120,800
10%	\$ 57,275	\$ 164,494	\$ 442,593
12%	\$ 72,052	\$ 241,333	\$ 767,090
15%	\$102,444	\$ 434,745	\$1,779,090
20%	\$186,688	\$1,181,882	\$7,343,858



2. Get Started Now (continued)

- ▶ **B. Begin Your Savings With a Lump-Sum**

Assume you started with a \$5,000 lump-sum plus \$1,000 per year. At 10% after 40 years you would have \$668,890.

- ▶ **C. Pay Yourself First**

- ▶ *Take 10% of Your Disposable Income and Start a Savings Plan.*



2. Get Started Now (continued)

- ▶ ***D. Start an Emergency Fund***
 - ▶ ***Should eventually be the equivalent of 6 months income in a liquid account such as a Money Market Mutual Fund or Capital Growth Fund***

- ▶ ***E. Savings Priorities***
 - ▶ ***1) Emergency Fund***
 - ▶ ***2) Retirement Program***
 - ▶ ***3) Investment Fund***



4. Buy the Right Life Insurance

- ▶ *A. Purpose of Life Insurance*
- ▶ *B. What are You Paying For?*
- ▶ *C. What Should You Buy?*
- ▶ ***Therefore never buy whole life insurance***
- ▶ ***Never buy life insurance as an investment***
- ▶ ***Buy term insurance***

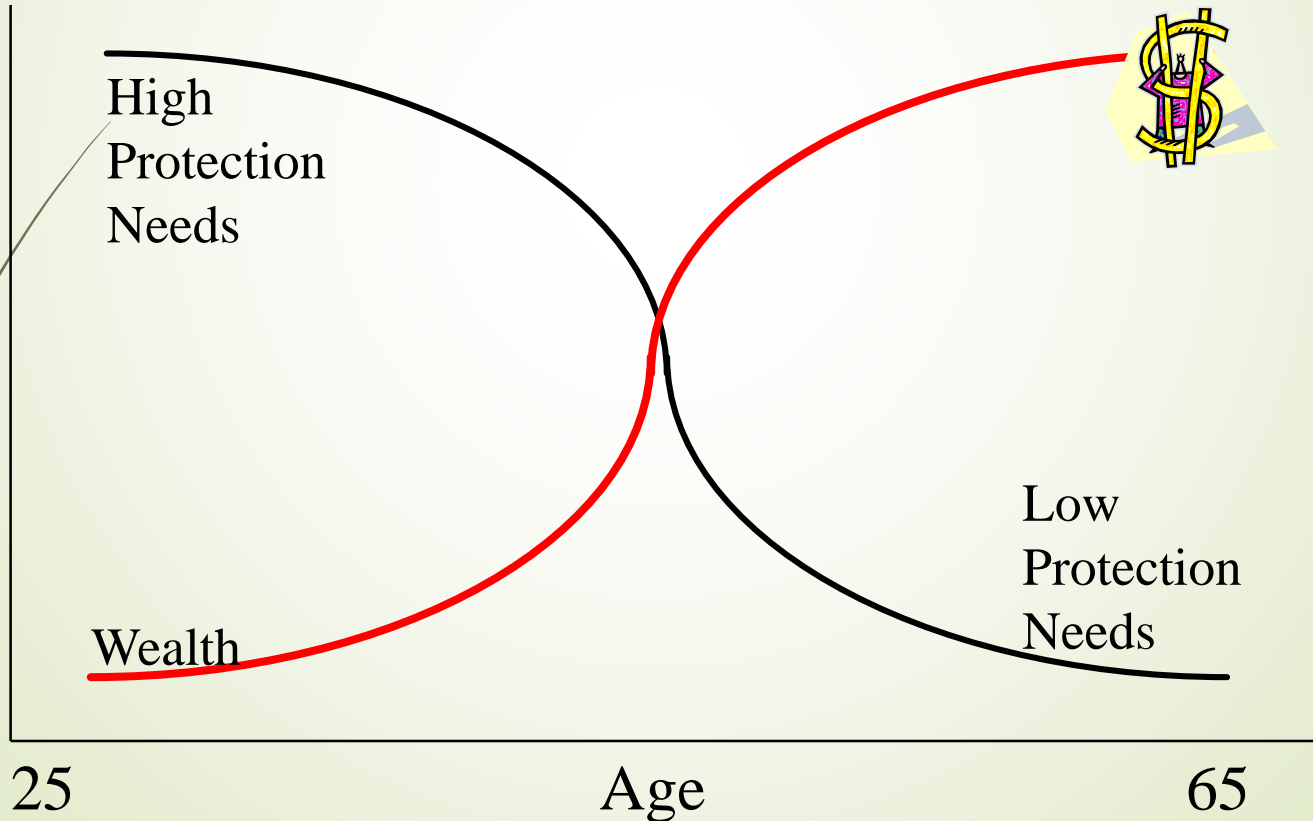


4. Buy the Right Life Insurance

- ***D. Responsibility***
 - ***1. High Responsibility:***
 - ***a. Dependents***
 - ***b. Debt/Credit***
 - ***c. Mortgage***
 - ***d. Age***
 - ***2. Low Responsibility:***
 - ***a. Few Dependents***
 - ***b. Little Debt***
 - ***c. Mortgage Paid***
 - ***d. "Golden" Years***

4. Buy the Right Life Insurance (continued)

Life Insurance Coverage



4. Buy the Right Life Insurance **(continued)**

- ▶ *E. Never Buy Any Kind of Cash Value Insurance*
- ▶ *F. Never Buy Life Insurance as an Investment/Income*
- ▶ *G. Solution -- Buy Term and Save
the Difference in an IRA*



Types of Insurance

- **1. Term Insurance -- Buy Protection Only**
 - **Level Premium, decreasing protection**
 - **Rising Premium, level protection**
 - **Rising Premium, decreasing protection**
 - **Features:**
 - **1) Renewable every 5 or (best) 10 years**
 - **2) Convertible into a cash value policy**

Protection Profile

\$100,000


PROTECTION



25

Age

65



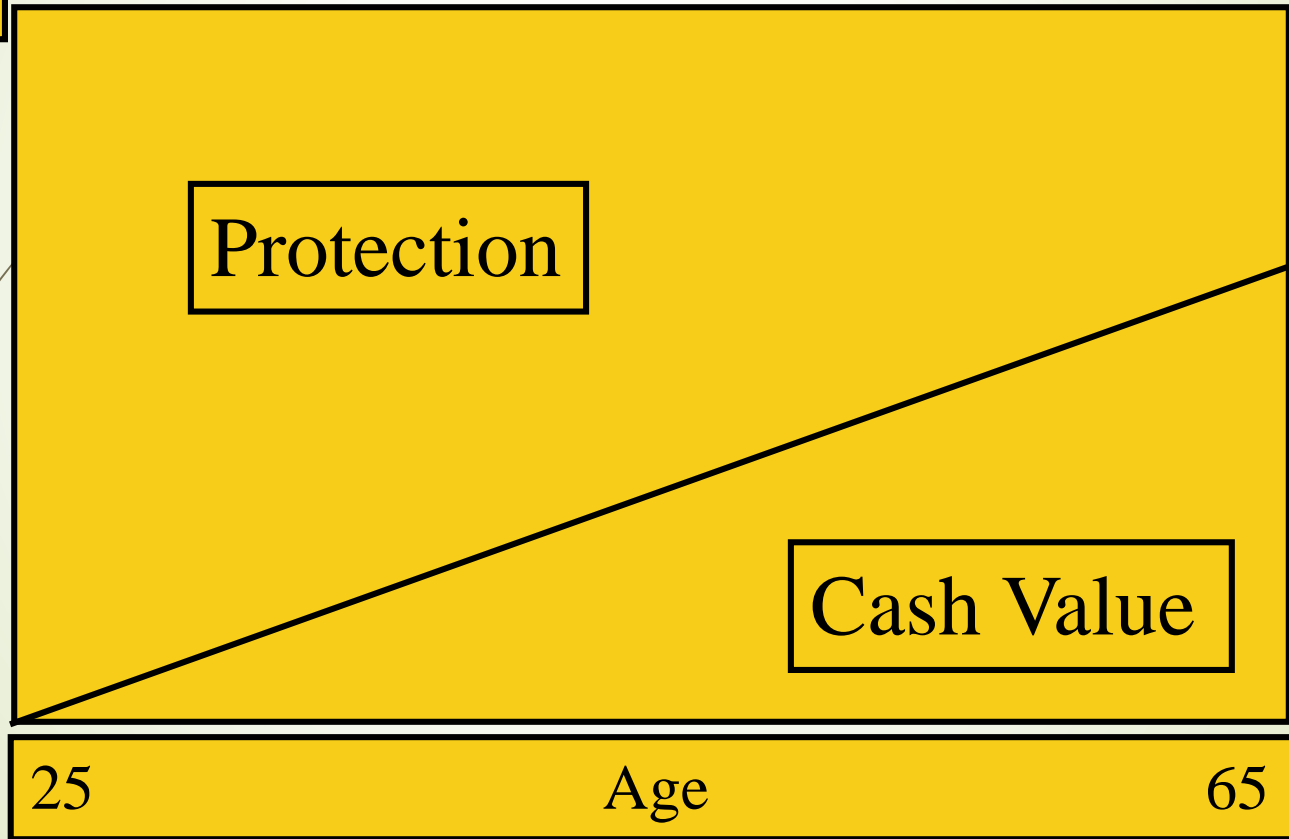
Types of Insurance **(continued)**

➤ 2. Whole Life

- a. Premiums payable to death**
- b. Combines protection and savings plan**
- c. Provides living (borrowing) and death benefits**
- d. Alternatives at retirement:**
 - Continue protection**
 - Take cash settlement**
 - Convert to an annuity**

Protection Profile

\$100,000



Protection

60%
of
F.V.

Cash Value

25

Age

65

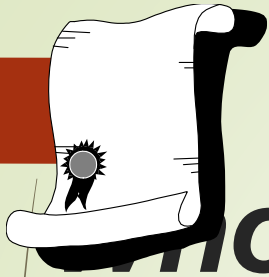


Whole Life Policy vs. Term plus IRA

- ***1. \$100,000 whole-life policy costs \$1200/yr.***
- ***2. Buy 5/10 year renewable, decreasing term***
- ***3. Save difference in a Mutual Fund at 6% per year***

Whole Life Policy vs. Term plus IRA (continued)

Age Term	Face Amt.	Annual Prem.	Difference \$1200-Premium	Estate
25-29	\$100,00	\$390	\$ 810	\$104,565
30-34	94,000	362	838	104,832
35-39	88,000	416	784	106,914
40-44	80,000	496	704	109,274
45-49	68,000	600	600	110,550
50-54	52,000	660	540	111,975
55-59	32,000	610	590	115,572
60	-0-	-0-	1200	113,020
61-64	-0-	-0-	1200	157,984
At age 65:			\$157,984	
			All Cash	



Whole Life Policy has:

Cash Value	=	\$57,300
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Protection	=	\$42,700
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Total	=	\$100,000
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Review Questions:

- *What are the key factors in establishing investment goals and plans?*
- *Assume you are currently earning \$80,000 per year and will retire in 20 years. If you feel you can live on 80% of your salary during retirement and you further assume you will live for 25 years after you retire, how much of a lump sum must you have in 20 years when you retire to meet these goals?*
- *What is the difference between whole life insurance and term insurance?*
- *It is always better to begin a savings plan with a lump-sum and then a consistent periodic investment, why?*
- *Term insurance can be purchased at least three different ways, what are they?*
- *What is the greatest achievement of human civilization?*
- *Explain what the meaning of the parables: 1) The Grain of Wheat and 2) The Master and the Slave.*