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PLANNING FOR THE FUTURE – INVESTING AND PHILANTHROPY

Unit Overview

In this unit, the student will learn about the various types of investments and their role in financial planning. The benefits of using one's wealth to help others will also be discussed.

Investing

What is Investing? Check the situations below that you think represent investing.

_____ 1. Janet keeps her money in a safety deposit box at the bank.

_____ 2. Jeremiah just opened a money market checking account.

_____ 3. Eugene contributes to a 401K through work.

_____ 4. Linda Suzanne cashes her pay check and puts the money in different envelopes.

_____ 5. Judy puts her money in mutual funds.

_____ 6. Daniel collects baseball cards hoping to sell them in the future for a profit.

According to the Federal Reserve, an ***investment*** is anything you acquire for future income or benefit. When you ***invest***, you pay out money with the goal of making a profit. Whenever there is the potential of making money, you are investing. Numbers 2, 3, 5 and, believe it or not, number 6 are all examples of investing. In situations 2 and 4, there is no potential for growth; therefore, they are not examples of investing.

Investing your money is a good idea for several reasons. When you invest, your money makes money for you. It is a way to earn money without '*working*' for it. Also, you are less likely to spend money that is invested. As a result, you accumulate money to help meet your financial goals. It is also a way to plan for your future, to have money available for important purchases (i.e. a home, college education, etc.) and to secure your retirement.

Money Making Money

Compound interest (interest paid on previously earned interest and principal) is one of the factors responsible for the growth potential of investing. Let's say you decide to ***save $100 a month***. At the end of 10 years, you would have saved $12,000. However, if you put that same $100 a month in an account paying 5% compound interest, you will have $15,592.93 at the end of ten years. That is an increase of $3,592.93. The longer your money remains in an account paying compound interest, the faster your earnings accelerate.

Study the table below. At the end of ten years, the account paying compound interest has earned approximately 23% more money than the account bearing no interest. This increases to 42% after twenty years; if you leave your funds in place for thirty years, your account will yield a growth of 57%. Forty years results in a return of 69% while fifty years nets 78% over a non-interest account.

	Savings	Savings	Additional Earnings	% Additional Earnings
	no interest account	compound interest account (5%)	(Column 3 - Column 2)	
10 yrs	$12,000	$ 15,592.93	$ 3,592.93	23% more
20 yrs	$24,000	$ 41,274.63	$ 17,274.63	42%
30 yrs	$36,000	$ 83,572.64	$ 47,572.64	57%
40 yrs	$48,000	$153,237.86	$105,237.86	69%
50 yrs	$60,000	$267,977.14	$207,977.14	78%

Earnings calculated using the ITT Tech Compound interest calculator -
http://www.moneychimp.com/calculator/compound_interest_calculator.htm

Types of Investments

Investing does not guarantee that you will make money; in fact, you may lose money. Different investments involve various levels of ***risk*** or chances of losing money, but they also involve a range of ***potential*** to earn money (growth). Generally, an investment involving greater risk has larger potential for growth. On the other hand, investments that require a smaller risk usually have less potential for growth. Studying the different types of investments can help you decide what type of investment is best for you and your situation.

Income Investments - In these types of investments you are actually lending your money to a bank, business or government. In exchange for the use of your money, you are paid interest. Most income investments are low risk.

Savings Accounts are insured by the Federal Deposit Insurance Corporation (FDIC), which means you are guaranteed your money is safe. Unfortunately, the interest rates are also low so your potential to make money isn't that good. Since you can access your money at any time, savings accounts are referred to as ***liquid***.

U.S. Savings Bonds lend your money to the federal government for a set period of time; in return, you receive interest for the use of those funds. If you cash a bond in early, you pay a *penalty* by losing interest. U.S. Savings bonds pay higher interest rates than savings accounts, and because they are backed by the government, they are considered low risk.

Certificates of Deposit (CDs) are a bank's version of a savings bond. You loan the bank money for a set period of time (3 months to several years), but if you cash a CD early, you lose money. CDs pay higher interest than U.S. Savings bonds.

Other types of bonds include ***Corporate, Municipal and U.S. Treasury***. Like U.S. Savings bonds, these are sold by corporations as well as state, local and federal governments. You need at least $1,000 to buy one of these bonds, and you are usually required to buy more than one at a time. They pay a specified amount of interest on a regular basis and are considered a low to moderate risk.

Money Market Accounts work like checking accounts in that you can take your money out when you want. However, you might be limited in the number of checks you can write each month. These accounts offer a higher interest rate than savings accounts but pay a lower rate than CDs. Unlike savings accounts, money markets require a high minimum balance. They are also insured by the FDIC.

Growth Investments - Investments of this type invite you to buy ***shares*** in a company with the hope that they will increase in value. If they do, you can make a considerable amount of money. If your shares decrease in value, however, you may lose a significant amount of money. These types of investments are generally considered higher risk. Nonetheless, if you compare money invested in income accounts to money invested in growth accounts over long periods of time, growth investments usually do better than income investments.

Stocks are the most common type of growth investments. When you buy stock in a company, you own part of the company. The idea is to buy stock when it is cheap and sell it when it increases in value, making you a great deal of money. Then again, the company may decrease in value, and your investment may be worth less or even worthless. As a result, stocks are considered a riskier method of increasing your financial wealth. They are generally liquid in that you can access your money at any time. You can buy stocks directly from the company or through a ***broker*****,** a person trained to buy and sell investments.

Mutual Funds permit you to become part of a large group of investors. A broker pools the money of many investors and buys bonds, stocks, real estate, etc. Mutual funds are considered less risky because the investment is ***diversified*** or spread among many different companies. One of the advantages of mutual funds is you can start with as little as $50

Real Estate involves the purchase of land and buildings with the idea that the resale values will increase over time. Although a considerable profit may be earned in this way, investors must be prepared to tie up their cash for a long period of time. Since property can also decline in value, it is a riskier way to make money.

Collectibles are items limited in number like works of art, baseball cards, antiques, etc. The buyer purchases the item with the expectation of selling at a higher price. This type of investment caters to a very small market, ties up the investor's money and is considered high risk.

QuickTime Types of Investment Opportunities (02:48)

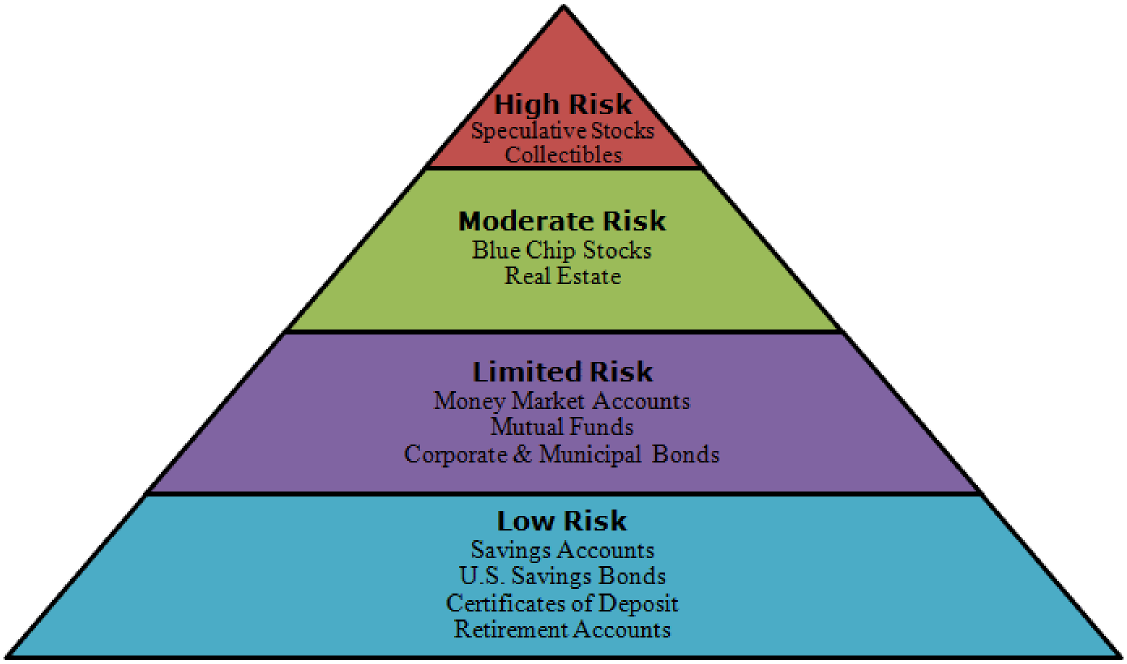
Retirement Investments - Accounts of this nature are designed to provide you with additional income when you retire. The money you save and grow through these investments gives you the flexibility to quit working altogether, to change careers, to pursue your hobbies or to do volunteer work. The sooner you begin to contribute to your retirement savings, the more likely your plans for the distant future are to become a reality.

Individual Retirement Accounts (IRA) are tax-deferred accounts designed to encourage retirement savings. You do not pay income tax on the money you invest until you cash in the IRA.

Roth Individual Retirement Accounts (Roth IRA) tax the money that you invest before you contribute to the fund. If you leave your money in a Roth for at least five years, you can access your money without paying any additional taxes.

401K Plans are employer-sponsored retirement programs and are named for the section of the tax code that regulates them. Employees can save a limited amount of their income in these tax-deferred accounts. Some employers also match a portion of their employees' contributions.

Investment Risk



Questions to Ask Yourself Regarding Risk

- What are my financial goals?
- How much money do I need to accumulate?
- How soon do I need money?
- How long can I afford to leave my money invested?
- What is my personal tolerance for taking risks?
- Can I afford to take risks?

QuickTime Choosing an Investment Strategy (02:08)

Managing Risk - Investment always involves risk. When you are investing for growth, you experience both good and bad periods; volatility and fluctuations result from political, economic and social changes. However, there are ways to minimize the risk and to avoid major losses. ***Growth Mutual Funds*** can recover from market downturns in a reasonable period of time and provide the following advantages:

- ***Diversification*** spreads your money among twenty-five to one hundred different investments within the mutual fund. If one stock does poorly, gains in other areas balance your loss.

- ***Dollar Cost Averaging*** is another benefit of investing in a mutual fund. This means the buyer is investing the same amount at regular intervals, such as monthly or quarterly. This reduces the risk associated with price swings, because it balances the highs and lows of stock prices.

The Facts and Figures of Investing

Although there are many variables when it comes to investing, one factor remains constant. The earlier you begin to invest, the more time your money has to grow and to work for you.

It is possible for an initial investment to grow simply because of time and compound interest. For example, at age twenty-five, a person would need to invest $4,419 at a rate of 10% compounded annually to reach a total of $200,000 by age sixty-five. However, an individual, who did not invest until age forty-five, would have to invest $29, 229 to reach a goal of $200,000 by age sixty-five.

The table below illustrates how much money you can accumulate with different investment amounts at ages.

Invest Today to Meet Retirement Goals at Age 65					
Age	**Amount Invested**				
20	$2,743	$5,487	$8,232	$10,976	$13,719
25	4,419	8,838	13,257	17,676	22,095
30	7,117	14,234	21,351	28,468	35,585
35	11,462	22,924	34,386	45,847	57,309
40	18,460	36,919	55,378	73,838	92,296
45	29,729	59,458	89,186	118,915	148,644
50	47,879	95,757	143,635	191,514	239,392
55	77,109	154,217	231,326	308,435	385,543
60	124,185	248,369	372,553	496,737	620,921
65	**200,000**	**400,000**	**600,000**	**800,000**	**1,000,000**
Assumes a 10 percent return that is compounded annually					

In the world of investing, money definitely increases with time. Read the following examples as you study the information in the table:

- Juliette, age twenty, only needs to invest $2,743 to have $200,000 at age 65. If she waits until age thirty-five to begin investing, she will need to invest $11,462 to arrive at the same amount. On the other hand, if she invested that $11,462 at age twenty, she will have over $800,000 by the time she is sixty-five!

- If you want to be a millionaire by the time you are sixty-five, invest $13,719 at age twenty!

Using the information in the table above, answer the following questions:

1. If you are thirty years old, how much money do you have to invest to acquire $600,000 at age sixty-five?
2. You need to invest $17,676 by what age if you want $800,000 at age sixty-five?
3. If you invest $5,487 at age twenty, how much money will you have at age sixty-five?

Open document **Invest Today Check Sheet** to check your answers.

Choosing a Financial Planner

While investing can help your money grow, it can certainly complicate your financial picture. Some people welcome this challenge and enjoy managing their own portfolios; others prefer to pay for expert advice and money management skills. A financial planner can help you to determine your long-term goals and can give you guidance on how to reach them. He/she can also help you to re-evaluate these goals when your circumstances change. For example, you may want to take fewer risks with your money when your approach retirement age. A financial planner has the knowledge to manage your money in a tax-effective manner. Because this person will have access to your financial data, it is important to choose wisely.

When selecting a financial adviser, you want someone who is well-qualified, knowledgeable and trustworthy. It must be a person who is a good listener with whom you can honestly discuss your plans for the future. Limit your search by eliminating anyone who is not a certified financial planner (CFP). This ensures that an individual is licensed and has taken courses on several different aspects of finance. Trusted friends and professionals that you have met through you own banking experiences may have some recommendations. He/she must be able to explain the risks as well as the rewards of particular investments in a manner that it understandable to you. If possible, interview at least three candidates, and prepare your questions in advance. During these meetings, try to direct the same questions to all the candidates. Clarify how each one charges their fees (hourly or flat-rate), and check out their credentials. Remember—it is very easy to pull a fake resume off the Internet! This process takes time, but an excellent financial planner can prove to be a valuable asset.

Investment Recap

There are many different ways to invest your money. Money markets and certificates of deposit (CD) are safe. If you don't have a lot of money to invest, mutual funds allow you to invest small amounts. The stock market is high risk, but if you know what you are doing, it offers a good opportunity to make money. Retirement accounts offer tax advantages on the money you save for retirement. Whatever investment strategy you follow, remember to contribute early in your career so your money has time to grow.

Philanthropy

We have covered a great deal of information concerning money, including setting goals, establishing financial plans, budgeting, banking, using credit wisely, spending carefully and investing to build wealth. What we haven't talked about is using money to help others.

Lee Iacocca, a wealthy businessman, said "My father used to say, '*You can spend a lot of time making money. The tough time comes when you have to give it away properly*.' How to give something back, that's the tough part in life." ***Philanthropy*** is a desire to improve the material, social and spiritual welfare of humanity, especially through charitable activities. There are many who believe that money and social responsibility are closely related. Computer guru, Bill Gates, asks, "*Is the rich world aware of how four billion of the six billion live? If we were aware, we would want to help out; we'd want to get involved*."

There are many different ways to go about helping others. Some people contribute money to their church and others to charitable organizations. Some believe it is more important to give their time and talents to others by collecting supplies for flood victims, helping out at a soup kitchen or working at a food pantry. Some want to be involved in their own communities; others look to worldwide causes. It doesn't matter how you decide to give back. The important thing is to "*understand our place in the world, doing what we can to help sustain others, and respecting and protecting our environment*" (Shelly, 2001, p.36).

Contributing to Charities

When my uncle was alive, he was a strong believer in giving to others and would do so to the tune of $10,000 a year. I was asked to take over his finances after he became ill. I began to research his charities and discovered over half of them were not legitimate or directed very little money to the actual cause. These groups took advantage of my uncle and his generosity.

Make sure your donations are being directed appropriately, and research the organization or cause before giving. An easy way to research a charity is to visit the ***Charity Navigator*** website. Charities are rated on efficiency, use of funds (i.e. overhead, promotion, salaries, etc.), and potential for growth. Charity Navigator uses a four star system. A charity that receives four stars is considered a good choice, whereas a charity that receives no stars is one to avoid. For additional information visit: http://www.charitynavigator.org/.

For many, charity begins at home. All communities have need for volunteers. Find an organization or cause you believe in; then, donate your time and/or money. For example, Kendall, a high school senior, participates in Big Brothers, Big Sisters. He believes the time he spends with his '*little brother*' makes a difference for both of them. Sarah's aunt is a breast cancer survivor so she contributes to organizations that raise money for cancer research. Ken's next door neighbor Charlie is elderly and can't do what he could in the past. Ken shovels Charlie's driveway in the winter and mows his lawn in the summer. If you ask Ken, he will tell you, "*It is no big deal*." Regardless, Ken is participating in philanthropy in his own way.

Keep money in perspective. Learn to appreciate and enjoy what you have and remember to "*care for the world you live in and the people with whom you share it*" (Shelly, 2001, p.38).

One of my favorite Garth Brook's songs is ***The Change***. I think the song captures what it means to be socially responsible.

One hand
Reaches out
And pulls a lost soul from harm
While a thousand more go unspoken for
They say what good have you done
By saving just this one
It's like whispering a prayer
In the fury of a storm

And I hear them saying you'll never change things
And no matter what you do it's still the same thing
But it's not the world that I am changing
I do this so this world will know
That it will not change me

This heart
Still believes
The love and mercy still exist
While all the hatred rage and so many say
That love is all but pointless in madness such as this
It's like trying to stop a fire
With the moisture from a kiss

And I hear them saying you'll never change things
And no matter what you do it's still the same thing
But it's not the world that I am changing
I do this so this world will know
That it will not change me

As long as one heart still holds on
Then hope is never really gone

I hear them saying you'll never change things
And no matter what you do it's still the same thing
But it's not the world that I am changing
I do this so this world we know
Never changes me

What I do is so
This world will know
That it will not change me

From: http://www.elyrics.net/read/g/garth-brooks-lyrics/the-change-lyrics.html