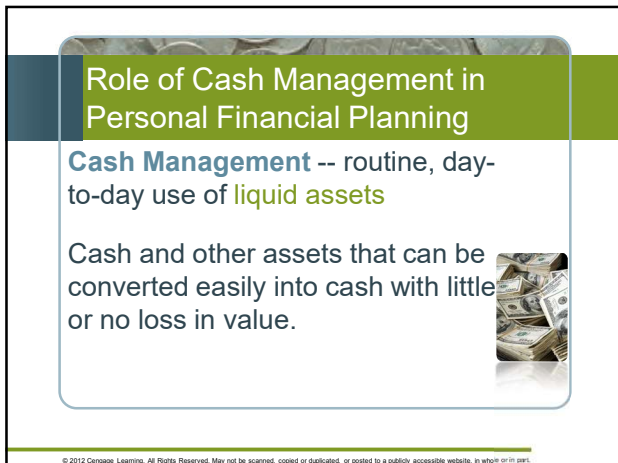




#4 MANAGING YOUR CASH AND SAVINGS

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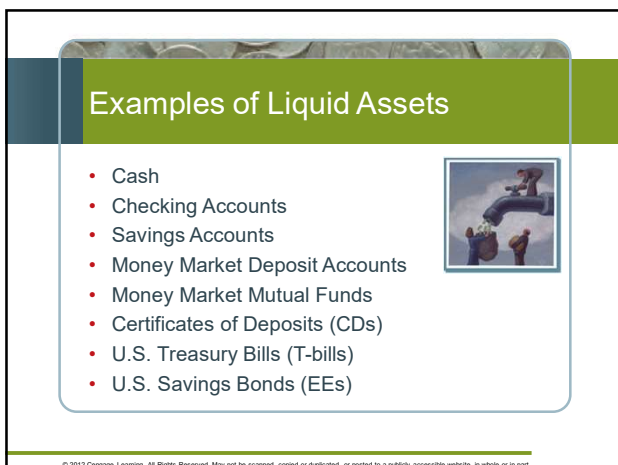
Role of Cash Management in Personal Financial Planning

Cash Management -- routine, day-to-day use of **liquid assets**

Cash and other assets that can be converted easily into cash with little or no loss in value.

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Examples of Liquid Assets

- Cash
- Checking Accounts
- Savings Accounts
- Money Market Deposit Accounts
- Money Market Mutual Funds
- Certificates of Deposits (CDs)
- U.S. Treasury Bills (T-bills)
- U.S. Savings Bonds (EEs)

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Today's Financial Services Marketplace

<b style="color: #76923c;">Financial Products <ul style="list-style-type: none"> checking and savings accounts credit cards loans and mortgages insurance mutual funds 	<b style="color: #c00000;">Financial Services <ul style="list-style-type: none"> financial planning tax preparation securities brokerage real estate trusts estate planning
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Types of Financial Institutions

<b style="color: #76923c;">Depository <ul style="list-style-type: none"> Commercial Banks Savings & Loans Savings Banks Credit Unions 	<b style="color: #c00000;">Nondepository <ul style="list-style-type: none"> Stock Brokerage Firms Mutual Funds Life Insurance Companies Finance Companies
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Types of Depository Financial Institutions Part 1

Commercial Banks

- Largest type of traditional financial institution
- Offer full array of financial services
- Only financial institution to offer noninterest-paying checking accounts

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Types of Depository Financial Institutions Part 2

Savings & Loan Associations (S&Ls)

- Offer services similar to commercial banks
- May pay slightly more on savings deposits
- Channel depositors' savings into mortgage loans

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Types of Depository Financial Institutions Part 3

Savings Banks

- Located primarily in New England
- Offer interest-paying checking accounts
- Rates similar to Savings & Loan Association
- Most are mutual associations

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Types of Depository Financial Institutions Part 4

Credit Unions

- Provide financial products and services to people with a common tie
- Nonprofit, member-owned financial cooperative
- Interest rates higher than other institutions

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How Safe is Your Money?

Most financial institutions are federally insured

Federal Deposit Insurance Corporation (FDIC) insures accounts at banks, savings banks, and S&Ls

National Credit Union Administration (NCUA) insures accounts at credit unions

Frank-Dodd Wall Street Reform and Consumer Protection Act of 2010 increased maximum deposit insurance from \$100,000 to \$250,000.

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Checking and Savings Accounts

Checking Account = Demand Deposit

If sufficient funds, banks must pay amount of check or ATM withdrawal

Savings Account = Time Deposit

Expected to remain on deposit for a longer time period



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Types of Checking Accounts

Regular checking accounts

- Offered by commercial banks
- Pay no interest

Interest-bearing checking accounts

- Include NOW, share draft, and money market deposit accounts
- Offered by banks, savings banks, S&Ls, and credit unions

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Interest Paying Checking Accounts

- **NOW Accounts** - Interest paid, may have minimum balance
- **Money Market Deposit Accounts (MMDAs)**- Convenient, safe, federally insured
- **Money Market Mutual Funds (MMMFs)**- Pool investors' funds to purchase high-return, short-term marketable securities

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Asset Management Accounts

Comprehensive deposit account combining checking, investing, and borrowing activities offered by brokerage firms and mutual funds

Account usually includes MMDA with unlimited free checking, debit card, use of ATM, and loans

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Electronic Banking Services

Electronic Funds Transfer Systems (EFTS) offer:

- ATM service
- Debit cards linked to checking account
- Pre-authorized deposits and payments
- Banking by phone
- Online banking and bill payment services



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Electronic Funds Transfer Act of 1978

- Regulates EFTS services
- Errors must be reported within 60 days



Limit losses by immediately reporting theft, loss, or unauthorized use of credit card or account!

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Other Bank Services

- **Safe-deposit boxes** – rented drawer in a bank's vault.
- **Trust Services** - provide investment and estate planning advice



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Opening and Using a Checking Account

- Consider costs
- Individual or joint account
- Checking account procedures
- Overdrafts
- Stopping payment

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Special Types of Checks

Special checks guarantee payment

- Cashier's Check - drawn on the bank
- Traveler's Check - used for making purchases worldwide
- Certified Check - drawn on account but guaranteed by bank

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Establishing A Savings Program

**PAY
YOURSELF
FIRST**

On payday - deposit
money into savings
account, using check or
debit card

- Create emergency fund
- Set aside funds for financial goals
- Utilize direct deposits and automatic transfers
- Make suitable choices based on goals and time horizon

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Earning Interest on Your Money

Simple Interest
interest paid
only on initial
deposit

Compound Interest
interest paid at set
intervals and
added back to
principal

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Earning Interest on Your Money (continued)

- **Nominal rate** - named or stated interest rate
- **Effective rate** - annual rate of return actually earned

If interest is compounded more frequently than once a year, the **effective rate** will be greater than the **nominal rate** of interest

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How Is Interest Calculated? Part 1

- If **simple interest** is used, there is no compounding

$$\begin{aligned}\text{Interest} &= \text{Principal} \times \text{rate} \times \text{time} \\ &= \$1000 \times .05 \times 1 \\ &= \$50\end{aligned}$$

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How Is Interest Calculated? Part 2

- If **compound interest** is used and the compounding occurs semiannually then

1st 6 months' interest:

$$\$1000 \times .05 \times 6/12 = \$25.00$$

2nd 6 months' interest: +

$$\$1025 \times .05 \times 6/12 = \$25.63$$

Total annual interest = \$50.63

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How Is Interest Calculated? Part 3

Nominal rate = 5% ...but....

Effective rate = 5.063%

$$\begin{aligned}\text{Effective Rate} &= \$50.63 \div \$1000 \\ &= 0.05063 \\ &= 5.063\%\end{aligned}$$

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How Much Interest Will You Earn?

Amount of interest earned depends on

- Frequency of compounding
- Balance on which interest is paid
- Interest rate paid



Time value of money concepts are used in compounding to find interest earned



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A Variety of Ways to Save

Certificates of Deposit (CDs)

- Funds remain on account for a given time period
- Early withdrawals incur an interest penalty

U.S. Treasury Bills

- Debt securities issued by U.S. Treasury
- Sold at a discount; \$1000 minimum
- Mature in 1 year or less

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A Variety of Ways to Save (continued)

Series EE Bonds

- Purchased at a discount
- Accrual-type security with interest paid when cashed in
- Exempt from state, local taxes
- New bonds must be held 1 year
- Income taxes may be avoided if redeemed for educational purposes



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