Personal Finance

Test 2

**Banking**

* Depository
* Commercial- take deposits, personal & business loans
* Savings- deposits and personal loans
* Credit unions- non-profit

$- government will insure deposits up to $250,000

**What do they offer?**

* Checking
* Credit cards- better fraud protection, rewards, can dispute charges
* Debit card- no interest fees
* Safety deposits box
* Cashier’s checks- drawn out of 3rd party
* Travelers checks- drawn of 3rd party
* Money order- written by 3rd party- ex: travelers check

**What do you look for?**

* Interest rates
* Savings
* APR (annual percentage rate)
* Fees
* Convince

**Risk Free Rate**

* US Treasury bills- loan from the US to the government
* Maturity less than one year, 90 days (possibility of inflation is almost zero)
* > 2 years= bond, 1-2 Note
* Term Structure of Interest

**CREDIT**

Liquidly- sell something fast for the full value

Asset class- asset that behave the same way

* investments that don’t go down in nominal value

Money Market fund- buy treasury bills

3 months’ worth of expenses- keep in cash

**Credit**

* non- installment
	+ trade credit
* installments- credit you pay off in period of time
	+ credit cards
* revolving line of credit- given amount in credit, available when you need
* -open line of credit (think credit limit)

**THE GOOD**

* credit score- opportunities for lower interest rates
* don’t need to carry cash or checks
* free financing
* track expenses
* builds credit

**NO GOOD**

* get into debt easily
* high interest rates
* buy things you don’t need
* buy things you can’t afford
* temptation

**Credit Bureaus**

* one free report every year (credit score)
* 3 major one (Experian, TransUnion, Equifax

**FICO SCORES**

* > 750 = very good
* 600-750= good
* 570-600 = fair
* <570 = poor

**WHAT determines a Credit Score**

* payment history
	+ Late Fees?
* Credit Utilization (30%)
* Credit History (15%)
	+ How long have you had a credit card?
	+ Not just opening and closing accounts a ot
* New Credit (10%)
* Types of Credit
	+ What kind of loans you have?

**When should you use credit?**

* House
* Buy things that GO UP in value

-House & yourself

**Identify Theft**

* Know the signs
* Don’t throw stuff away
* Skimmers on ATM
* Phone calls

**Cash Investments**

* Money Market Investments
	+ Checking
	+ Very liquid
	+ Easy
	+ Overdraft protection available
	+ Stop payment
	+ Direct deposit
* *Why doesn’t everyone do this?*
	+ Fees
		- Like negative interest
	+ No interest
* *Now accounts*
	+ Similar to checking
	+ Pays interest
	+ Requires minimum balance
* *Savings account*
	+ Higher rates than NOW accounts
	+ No check writing
	+ Less liquid
	+ Automatic transfer from checking
		- Pay yourself first
* *CD – certificate of deposit*
	+ Require money to be invested for period of time
		- E.g. one month, three months, six months, year, 3 years
	+ The longer the period, the higher the interest
	+ Higher rates than savings accounts
	+ Less liquid than savings accounts
		- Penalty for early withdrawal
		- Consider a CD ladder
* *U.S. Treasury Bills*
	+ Risk-free asset
	+ Mature in less than one year
	+ Minimum $10,000
	+ Liquid
		- Can be sold on secondary market
* **Money market funds**
* Fund – investors pool their money to buy cash investments
	+ T-Bills
	+ Large CDs
	+ Commercial paper
* Liquidity
	+ Limited number of checks each month
* Get rates online
* *Asset Management Account*
	+ Offered by investment firms
	+ Combine deposit and brokerage accounts
	+ “Sweep” unused money into money market
	+ High minimum balances required, e.g. $15,000

**CASH RISKS**

* Default (credit) risk
* Interest rate risk
	+ Interest rates go up, value goes down
* Liquidity risk
	+ Can it be sold quickly for its value?
	+ Do you have to pay a penalty?
* Inflation risk
	+ Cash investments pay less than rate of inflation

**CASH ALLOCATIONS**

* Need for short-term goals
* Need for emergencies
	+ Loss of job
	+ Medical needs
	+ Unexpected expenses (e.g. repairs)
* KEEP 3+ MONTHS OF EXPENSE IN CASH INVESTMENTS

**Extra Review:**

* Commercials bank- both business & personal loans
* Depository bank- put in $$$

Savings Vs Commercial banks

* Savings- personal
* Commercial – personal and businesses
* Credit accounts aren’t free

Investments bank- handle the $, provides financial services

Long term rates- 10-year vs 20 year

Higher rate?- more risk, so longer time= higher rate

Term structure of interest rates – long loan $, higher rate & inflation risk,

* Higher risk, higher return

Examples of cash accounts

* Money market account (group of people)
* T- bills

Risk premium- amount you pay over risk free rate

* 90-day t bill
	+ .1
* 90-day CD
	+ .5
* What causes interest to up & down
	+ Expected inflation, fed reserve (.25% right now)