

Concepts for Saving and Investing 5-8

Inflation

When prices go up over time, it's called inflation. And inflation tends to go up faster when most people are working and earning money. That's because when people have jobs and money, they're usually willing to pay more for the items that they want to buy. And the more people earn, the higher prices tend to rise.

Think about it this way: The more money you have, the less you'll worry about spending some of it. If you have only \$10, a ride in a hot air balloon might not be worth \$5, or half your life's savings. But if you have \$100, you might be willing to pay \$5 for a ride. And when prices rise, businesses charge more for their goods and services to maintain a profit.

Simple and Compound Interest

Suppose you have \$100 in a savings account earning 3% interest. If the account pays simple interest and you don't add or subtract any money, you'll earn 3% on your deposit each year, or \$3. After 25 years, you'll have a balance of \$175 ($\$100 + (25 \times \$3) = \175).

But with compound interest your account will grow faster, because your interest starts earning interest, too. You would earn \$3 the first year. But then, the second year you would earn \$3.09, or 3% of your \$103 balance. And after 25 years of compound interest, you'd have a \$209 balance!

Just remember that if you add money to your account, your balance might grow a lot more. And, if you withdraw, or take money out, it might grow much less. When you add or take away from your account, you're changing the amount you can earn as well. And when you're building a mountain of savings, every cent counts.

Short-Term Saving

A savings account will almost always come in handy. No matter what your savings goals are – sports car, college tuition, climbing expeditions – putting money away little by little is always a good idea.

Jeannie's pretty smart about spending her money – and saving it, too. She's serious about going to college, and she loves mountain sports that tend to cost money. Plus, she needs money to take care of her growing record collection and a set of turntables.

Every week, Jeannie deposits her allowance into her savings account, where it grows dollar by dollar. And even though she can spend the money if she needs it, she's less tempted to do so. Plus, she doesn't have to worry about losing it on the mountain.

Jeannie really likes having access to her money while watching it grow. But every so often, at birthdays or holidays, she receives a larger sum of money that she would rather save towards long-term goals like college.

Long-Term Range

Last summer, Jeannie sent her pet monkey Fred to summer camp for a few months. When he came back to her in August, he was not only tanned and more fit – he'd grown five inches, too.

So when she received a total of \$500 on her 15th birthday, she wanted to do something similar with all that money: send it away for a while so it could grow.

So, she put her \$500 into a savings account that she decided not to touch for several years. She knows that if she doesn't touch that account, her money will keep growing and earning interest.

Jeannie also could have put her money into a certificate of deposit, or a CD. When you put your money into a CD, you agree to leave your money in an account for a fixed amount of time. Your money will earn interest while it's in that account, and you won't be able to spend it while it's there. So make sure you have enough money in another account to cover your other expenses, like Sneaker Town sneakers and spelunking adventures, in the meantime.

Quiz

- 1) If I have 8 weeks to save money for a Pulp Post subscription that costs \$104, how much money would I have to save each week?
 - a. \$12.75
 - b. \$14
 - c. \$13
 - d. \$23.25
 - e. \$21

- 2) What is interest?
 - a. The money you earn as a percentage of your investment
 - b. When prices increase as time goes by
 - c. The money you pay as a fee when you use a debit card
 - d. When prices decrease as time goes by
 - e. The total amount of money in a bank or in an investment account

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- 4) Suppose I open a savings account with a \$100 deposit. If I don't touch the account and it earns 3% interest every year, what would my balance be after 1 year?
 - a. \$100.03
 - b. \$100.30
 - c. \$103.00
 - d. \$130
 - e. \$300

- 5) What if the account was earning 3% simple interest every year? What would the balance be after 3 years?
 - a. \$103.33
 - b. \$106.09

- c. \$109.00
 - d. \$109.09
 - e. \$600.00
- 6) If I could choose among savings accounts that pay compound interest, which one would be worth the most after one year? An account that compounded:
- a. Annually?
 - b. Monthly?
 - c. Daily?
 - d. Quarterly?

Match the terms with their definitions below.

CD

Checking Account

Piggy Bank

Savings Account

- A. You have access to your money whenever you want, but it doesn't grow, isn't protected, and isn't insured.
- B. You have access to your money whenever you want, but it doesn't grow, isn't protected, and isn't insured.
- C. You can add or withdraw money whenever you want. Your money may earn some interest, and it's always insured, so you can't lose it.
- D. Your money might not earn interest, but you can spend it without having to carry around a lot of cash.