**Instructor’s Manual**

**To support your use of**

**14th Edition of**

**Personal Financial Planning**

**By**

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Thank you for reading this instructor’s manual. If I were you, I would not read it because I have not found instructor’s manuals to be useful. If you will keep reading, I hope that this manual will be an exception. My goal is to give you useful highlights and information to make your course better.

The personal financial planning course has the potential to be a life changing experience. If you can get the students to read the book, understand the concepts therein, and then apply them to their life, you will have done them a great service. And the students will be rewarded multiple times.

The goal of this book is to remove the mystery from the personal financial planning process and replace it with the tools your students need to take charge of their personal finances and life. To organize this process, the text is divided into six parts as follows.

• **Part 1:** Foundations of Financial Planning

• **Part 2:** Managing Basic Assets

• **Part 3:** Managing Credit

• **Part 4:** Managing Insurance Needs

• **Part 5:** Managing Investments

• **Part 6:** Retirement and Estate Planning

The summary of the learning goals at the end of the chapter should aid the student in reviewing the chapter when exam time comes. It will be useful to point out to the student how to use this material.

The organization of the Instructor’s Manual for each chapter is to

* Key issues listed by learning goal with suggestions for classroom use [This is the most useful section of the IM.]
* The Financial Fact or Fantasy features are listed just after the learning goals. These are also listed in the form of a True/False question that you can use as a Pre-test to introduce the chapter, as a quiz, or as part of an exam.
* Solutions for the “Test Yourself” questions – These may be used as quiz or exam questions. Also, I found that by going through each of the questions, I reread the chapter. The questions are in the order of the chapter and covers the key points of the chapter. By answers the Test Yourself questions, you will read the chapter.
* You Can Do It Now. These features gives the students links to interesting web sites. One option for using these is to assign two or three students to go to the sites and report back to the class what they found.
* Financial Impact of Personal Choices. Read and think about the choices being made. Do you agree or not? Ask the students to discuss the choices being made.
* Solutions to the Financial Planning Exercises – These may be used as quiz or exam questions
* Solutions to the Critical Thinking Exercises – These may be used as quiz or exam questions
* List of key terms from the chapter
* Outline of the chapter

I should point out that the Power Points slides that come with the book [only updated by me] are outstanding. They will be useful to you and I think you should use them. Since the color is well done, they will be best used if you can project them rather than print black and white.

**Understanding the**

**Financial Planning Process**

**Chapter 1**

***How Will This Affect Me?***

The heart of financial planning is making sure your values line up with how you spend and save. That means knowing where you are financially and planning on how to get where you want to be in the future no matter what life throws at you. For example, how should your plan handle the projection that Social Security costs may exceed revenues by 2017? And what if the government decides to raise tax rates to help cover the federal deficit? An informed financial plan should reflect such uncertainties and more.

This chapter overviews the financial planning process and explains its context. Topics include how financial plans change to accommodate your current stage in life and the role that financial planners can play in helping you achieve your objectives. After reading this chapter you will have a good perspective on how to organize your overall personal financial plan.

**LEARNING GOALS**

**LG1** Identify the benefits of using personal financial planning techniques to manage your finances.

Key concept in this section is the planning model as displayed in Exhibit 1.1. Your standard of living is greatly impacted by your spending habits and your commitment to saving.

ACTIVITY: Ask the students to assume that they have just inherited $100,000. What will you do with the money? Write down three ways you will spend or use the money.

Ask the students to share one item with the class and record what they say so that the entire class can reflex on the answers. Hopefully, at least a few will mention investing even if only $10,000 of the amount. Use their answers to discuss taking care of current needs versus future needs. Focus on their propensity to consume and its impact on accumulating wealth.

Use Exhibit 1.2 to show how the average person earns and spends their money and Exhibit 1-4 to help the student identify where they are now.

**LG2** Describe the personal financial planning process and define your goals.

Dwight Eisenhower, army general and president, is quoted as saying “Plans are useless; Planning is priceless”. The process of planning allows you to focus on the issues that are most important and to be ready when things change.

Exhibit 1.3 lists the six steps Financial Planning Process. The first and most important is defining your financial goals. Exhibit 1.6 lists goals by age to demonstrate how goals change over time. Use the examples in Exhibit 1.5 to ask students if the statement assumptions are realistic. Yes, the answer is in the exhibit, but many will not have read chapter at this point.

There are several worksheets in the book. Worksheet 1.1 gives the student a format to write down their goals. There is power in writing down goals [and most any other plan]. Recording the goal and then reviewing three months later will help you to keep focus on the goal.

The “DO IT NOW” feature for this section will make a good classroom discussion opportunity. It is:

**LG3** Explain the life cycle of financial plans, the role they play in achieving your financial goals, how to deal with special planning concerns, and the use of professional financial planners.

Exhibit 1.7 can help focus the attention on how goals differ between the various stages of life. Section 1-3b lists various decisions that you will have to make over your life. The section 1-3c addresses Special Planning Concerns. Worksheet 1.2 focuses on the financial benefit to the family of the second income. If the second income is from a minimum wage job, it may not be a good financial decision. Of course having a job, even a minimum wage job, may give the person psychic income that will override the financial impact.

While perhaps off topic, I recall a high school science teacher who was a smoker. He walked through the amount of money he spent on purchasing tobacco products. That computation had a lot to do with my decision to not smoke. How this relates to the course is that this is an illustration of how the financial impact of a decision can drive the decision.

**LG4** Examine the economic environment’s influence on personal financial planning.

For older folks, the financial crisis of 2008-2009 is fresh on our memory. To the student of 2016, that crisis is more of history than life. If you can share a war story on how you were personally impacted, it will help bring the impact of the world economy on financial plans to life. The book speaks how to manage this type of crisis, but you had to go through it to really understand the impact it had.

The value of professional advice is greatly understated. If by talking to a professional you can prevent making a mistake -- that can be of a great value. Section 1-3e speaks to the use of professional financial planners. Exhibit 1.9 lists out the various certifications that planners have.

Economic or business cycles are real. Perhaps the most useful thing about the cycles is that the knowledge that if things are bad, you know they will get better. Of course when life is good, you know that the cycle will come around again. Thus, financial planning requires saving in the good times for the bad times. See the “Test Yourself” question 1-17 for a short discussion of business cycles.

Power of compounding is rarely understood. Exhibit 1.8 shows how the amount $10,000 will grow over time. The longer the investment stays invested, the greater the amount – the power of compound interest.

**LG5** Evaluate the impact of age, education, and geographic location on personal income.

Exhibit 1.12 says it all.

**LG6** Understand the importance of career choices and their relationship to personal financial planning.

Exhibit 1.13 shows that the choice of a college major has a financial impact. Of course money cannot buy happiness, but having a bit helps. If you really want to be an elementary school teacher, you must recognize that you will not have as much wealth as a lawyer or financial analyst.

The summary of the learning goals at the end of the chapter should aid the student in reviewing the chapter when exam time comes. It will be useful to point out to the student how to use this material.

***Financial Facts or Fantasies?***

These may be used as “teasers” to get the students on the right page with you. Also, they may be used as quizzes after you covered the material or as “pre-test questions” to get their attention.

Your income level depends on your age, education, and career choice.

**Fact:** All three of these variables are important determinants of your income level, particularly when accompanied by adequate ambition and disciplined work habits.

Over the long run, gaining only an extra percent or two on an investment makes little difference in the amount of earnings generated.

**Fantasy:** Gaining an extra percent or two on an investment’s return can make a tremendous difference – often thousands of dollars – that increases the longer the investment is held.

Personal financial planning involves translating personal financial goals into specific plans and arrangements that put these plans into action.

**Fact:** Personal financial plans are based on the specific financial goals that you set for yourself and your family. Once in place, the plans are put into action using the various financial strategies explained in this book.

A savings account is an example of a tangible asset because it represents something on deposit at a bank or other financial institution.

**Fantasy:** A savings account, like stocks, bonds, and mutual funds, is an example of a financial asset – an intangible, a “paper” asset. Real assets, in contrast, refer to tangibles –physical items like houses, cars, and appliances.

An improved standard of living is one of the payoffs of sound personal financial planning.

**Fact:** The heart of sound financial planning and effective money management is the greater enjoyment of the money one makes by improving one’s standard of living.

**Financial Facts or Fantasies?**

These may be used as a quiz or as a pre-test to get the students interested.

1. True False Your income level depends on your age, education, and career choice

2. True False Over the long run, gaining only an extra percent or two on an investment makes little difference in the amount of earnings generated

3. True False Personal financial planning involves translating personal financial goals into specific plans and arrangements that put these plans into action.

4. True False A savings account is an example of a tangible asset because it represents something on deposit at a bank or other financial institution.

5. True False An improved standard of living is one of the payoffs of sound personal financial planning.

Answers:

1. True 2. False 3. True 4. False 5. True

**YOU CAN DO IT NOW**

The “You Can Do It Now” cases may be assigned to the students as short cases or problems. They will help make the topic more real or relevant to the students. In most cases, it will only take about ten minutes to do, that is, until the student starts looking around at the web site. But they will learn by doing so.

***Start a List of Your Financial Goals***

Yogi Berra summed it up: “If you don't know where you're going, you might not get there.” And so it is with your financial goals. Pick up some paper now and start a list of your financial goals. May be it’s as simple as saving $25 by the end of the month or as lofty as saving $200,000 for retirement by the time you’re 50. You’ll never achieve your goals if you don’t know what they are, much less know whether they’re realistic. Go ahead and dream. List your goals (short-term, intermediate, and long-term) and start laying out how you’ll get there. You can **do it now**.

**DO IT NOW**

***Start Building an Emergency Fund***

What would happen if you lost your job, got hurt, or had an unexpected big expense? Even if you’re not making much money now, you could start building an emergency fund by putting aside even $10 a month. As this chapter points out, your goal is to eventually set aside enough to last at least 6 month. Considering the risk of not doing so, you can **do it now**.

**DO IT NOW**

***Recognize that YOU are Your Most Important Asset***

Your greatest asset is YOU. So it’s important to build the value of your best asset by investing in your education and career. The amount you can consume, save, and invest is directly related to your earning ability. Consider that over an entire career, the average bachelor’s degree holder will earn $1.19 million, which is about twice what the typical high school grad earns and $335,000 more than the typical associate degree holder. (For additional motivating information, see the source of these statistics: The Hamilton Project at the Brookings Institution, http://hamiltonproject.org/earnings\_by\_major/). It’s so important to realize you’re your greatest asset and act on it – **do it now**.

**Financial Impact of Personal Choices**

Read and think about the choices being made. Do you agree or not? Ask the students to discuss the choices being made.

***Bob Cuts Back on Lunch Out and Lattes***

Bob buys lunch out most days and buys a latte every morning. He believes he could cut back a bit and save $5 a day, which is $35 a week and $140 a month. So what's the impact of this seemingly modest cut-back?

If Bob invests his $35 savings a week every month at 5 percent, he will have the following in the future:

20 years: $57,545

30 years: $116,516

40 years: $213,643

So the seemingly small act of investing only $5 a day would have a dramatic long-term effect on Bob's future accumulated wealth.

Test Yourself Questions

**1-1 What is a *standard of living?* What factors affect the quality of life?**

*Standard of living,* which varies from person to person, represents the necessities, comforts, and luxuries enjoyed by a person. It is reflected in the material items a person owns, as well as the costs and types of expenditures normally made for goods and services.

Although many factors such as geographic location, public facilities, local costs of living, pollution, traffic, and population density affect one’s quality of life, the main determinant of quality of life is believed to be wealth.

**1-2 Are consumption patterns related to quality of life? Explain.**

 Generally,consumption patternsare related to quality of life, which depends on a person’s socioeconomic strata. This implies that wealthy persons, who are likely to consume non-necessity items, quite often live higher quality lives than persons whose wealth permits only consumption of necessities.

**1-3 What is *average propensity to consume?* Is it possible for two people with very different incomes to have the same average propensity to consume? Why?**

 The *average propensity to consume* is the percentage of each dollar of a person’s income that is spent (rather than saved), on average, for current needs rather than savings. Yes, it is quite possible to find two persons with significantly different incomes with the same average propensity to consume. Many people will increase their level of consumption as their incomes rise, i.e., buy a nicer home or a newer car. Thus, even though they may have more money, they may still consume the same percentage (or more) of their incomes as before.

**1-4 Discuss the various forms in which wealth can be accumulated.**

An individual’s *wealth* is the accumulated value of all items he or she owns. People accumulate wealth as either financial assets or tangible assets. *Financial assets* areintangible assets such as savings accounts or securities, such as stocks, bonds and mutual funds. Financial assets are expected to provide the investor with interest, dividends, or appreciated value. *Tangible assets* are physical items, such as real estate, automobiles, artwork, and jewelry. Such items can be held for either consumption or investment purposes or both.

**1-5** **What is the role of money in setting financial goals? What is the relationship of money to utility?**

 *Money* is the exchange medium used as the measure of value in our economy. Money provides the standard unit of exchange (in the case of the U.S., the dollar) by which specific personal financial plans—and progress with respect to these plans—can be measured. Money is therefore the key consideration in establishing financial plans. *Utility* refers to the amount of satisfaction derived from purchasing certain types or quantities of goods and services. Since money is used to purchase these goods and services, it is generally believed that greater wealth (money) permits the purchase of more and better goods and services that in turn result in greater utility (satisfaction).

**1-6 Explain why financial plans must be psychologically as well as economically sound. What is the best way to resolve money disputes in a relationship?**

 Money is not only an *economic* concept; it is also a *psychological* one that is linked through emotion and personality. Each person has a unique personality and emotional makeup that determines the importance and role of money in his or her life, as well as one’s particular money management style. Personal values also affect one’s attitudes to money. Money is a primary motivator of personal behavior and has a strong impact on self-image. To some, money is of primary importance, and accumulation of wealth is a dominant goal. For others, money may be less important than lifestyle considerations. Therefore, every financial plan must be developed with a view towards the wants, needs, and financial resources of the individual and must also realistically consider his or her personality, values, and money emotions.

 Money is frequently a source of conflict in *relationships*, often because the persons involved aren’t comfortable discussing this emotion-laden topic. Each person may have different financial goals and personal values, leading to different opinions on how to spend/save/invest the family’s money. To avoid arguments and resolve conflicts, it is essential to first become aware of each person’s attitude toward money and his or her money management style, keep the lines of communication open, and be willing to listen and to compromise. It is possible to accommodate various money management styles within a relationship or family by establishing personal financial plans that take individual needs into account. Some families are able to avoid conflict by establishing separate accounts, such as yours, mine and household, with a set amount allocated to each account each pay period. This way, no one feels deprived, and enough has been set aside to pay the bills and to meet common financial goals.

**1-7 Explain why it is important to set realistically attainable financial goals. Select one of your personal financial goals and develop a brief financial plan for achieving it.**

 Realistic goals are set with a specific focus and a reasonable time frame to achieve results. It is important to set realistically attainable financial goals because they form the basis upon which our financial plans are established. If goals are little more than “pipe dreams,” then the integrity of the financial plans would be suspect as well

 Students’ descriptions of the steps to achieve a specific goal will, of course, vary. They should follow the general guidelines in the chapter: define financial goals, develop financial plans and strategies to achieve goals, implement financial plans and strategies, periodically develop and implement budgets to monitor and control progress toward goals, use financial statements to evaluate results of plans and budgets, and redefine goals and revise plans as personal circumstances change.

**1-8** **Distinguish between long-term, intermediate, and short-term financial goals. Give examples of each**.

 Individual time horizons can vary, but in general individuals would expect to achieve their *short-term* financial goals in a year or less, *intermediate-term* goals in the next 2-5 years, and *long-term* financial goals in more than 5 years. Refer to Worksheet 1.1 for examples of financial goals.

In making personal financial goals, individuals must first carefully consider their current financial situation and then give themselves a pathway to reach their future goals. People in the early stages of their financial planning life cycle may need more time to accomplish long-term goals than those who are already established in their careers and may also need to give themselves more flexibility with their goal dates.

**1-9** **What types of financial planning concerns does a complete set of financial plans cover?**

Financial plans provide the roadmap for achieving your financial goals. The six-step financial planning process (introduced in Exhibit 1.3) results in separate yet interrelated components covering all the important financial elements in your life. Some elements deal with the more immediate aspects of money management, such as preparing a budget to help manage spending. Others focus on acquiring major assets, controlling borrowing, reducing financial risk, providing for emergency funds and future wealth accumulation, taking advantage of and managing employer-sponsored benefits, deferring and minimizing taxes, providing for financial security when you stop working, and ensuring an orderly and cost effective transfer of assets to your heirs.

**1-10** **Discuss the relationship of life-cycle considerations to personal financial planning. What are some factors to consider when revising financial plans to reflect changes in the life cycle?**

 Personal needs and goals change as you move through different *stages of your life*. So, too, do financial goals and plans, because they are directly influenced by personal needs. When your personal circumstances change, your goals must reflect the new situation. Factors such as job changes, a car accident, marriage, divorce, birth of children or the need to care for elderly relatives must be considered in revising financial plans.

**1-11 Chad Jackson’s investments over the past several years have not lived up to his full return expectations. He is not particularly concerned, however, because his return is only about 2 percentage points below his expectations. Do you have any advice for Chad?**

 The loss of *two percentage points* on investment returns is anything but inconsequential, particularly if the loss occurs annually over a period of several years. For example, if Chad had invested $1,000 at an 8 percent return and subsequently had invested all earnings from the initial investment at 8 percent, in 40 years he would have accumulated $21,725 from the initial $1,000 investment. If, on the other hand, he had earned a 10 percent return on the same investment, he would have accumulated $45,259 in 40 years—more than double his return at 8 percent! Clearly, two percentage points over time can make a significant difference! Calculate various rates of return on a $1,000 investment to see that for every 2 percent increase in return, your investment results will more than double over a 40-year period.

By carefully considering his investment and banking choices, it is likely that Chad would be able to get a 2 percent greater rate of return without taking on additional risk. This can be done both by choosing investments and bank accounts that hold down expenses, as well as by finding investments of the same type that have performed better.

1-12 **Describe employee benefit and tax planning. How do they fit into the financial planning framework?**

 *Employee benefits,* such as insurance (life, health, and disability) and pension and other types of retirement plans, will affect your personal financial planning. You must evaluate these benefits so that you have the necessary insurance protection and retirement funds. If your employer’s benefits fall short of your needs, you must supplement them. Therefore, employee benefits must be coordinated with and integrated into other insurance and retirement plans.

*Tax planning* involves looking at an individual’s current and projected earnings and developing strategies that will defer and/or minimize taxes. For income tax purposes, income may be classified as active income, passive income, or portfolio income. While most income is currently subject to income taxes, some may be tax free or tax deferred. Tax planning considers all these dimensions and more. Tax planning is an important element of financial planning because it guides the selection of investment vehicles and the form in which returns are to be received. This means that it is closely tied to investment plans and often dictates certain investment strategies.

**1-13 “There’s no sense in worrying about retirement until you reach middle age.” Discuss this point of view.**

 This statement reflects a very limited and too often expressed point of view. Due to the inconsistencies and vagaries of our economic system—and of life itself!—the goals of and plans for retirement should be established early in life. If retirement goals are incorporated into an individual’s financial planning objectives, short- and long-term financial plans can be coordinated. Thus, financial plans can guide present actions not only to maximize current wealth and/or utility, but also to provide for the successful fulfillment of retirement goals. Furthermore, if retirement is desired earlier than anticipated, the plans may still permit the fulfillment of retirement goals.

**1-14 Discuss briefly how the following situations affect personal financial planning:**

1. **Being part of a dual-income couple**

Couples should discuss their money attitudes and financial goals and decide how to manage joint financial affairs *before* they get married. Take an inventory of your financial assets and liabilities, including savings and checking accounts; credit card accounts and outstanding bills; auto, health, and life insurance policies; and investment portfolios. You may want to eliminate some credit cards. Too many cards can hurt your credit rating, and most people need only one or two. Each partner should have a card in his or her name to establish a credit record. Compare employee benefit plans to figure out the lowest-cost source of health insurance coverage, and coordinate other benefits. Change the beneficiary on your life insurance policies as desired. Adjust withholding amounts as necessary based on your new filing category.

1. **Major life changes, such as marriage or divorce**

Major life changes such as marriage and divorce:

*Marriage.* Finances must be merged and there may be a need for life insurance.

*Divorce.* Financial plans based on two incomes are no longer applicable. Revised plans must reflect any property settlements, alimony, and/or child support.

1. **Death of a spouse**

The surviving spouse is typically faced with decisions on how to receive and invest life insurance proceeds and manage other assets. In families where the deceased made most of the financial decisions with little or no involvement of the surviving spouse, the survivor may be overwhelmed by the need to take on financial responsibilities. Advance planning can minimize many of these problems.

**1-15 What is a *professional financial planner?* Does it make any difference whether the financial planner earns money from commissions made on products sold as opposed to the fees he or she charges?**

 Unlike accounting and law, the field professional financial planning field is largely unregulated, and almost anyone can call themselves a *professional financial planner.* Most financial planners are honest and reputable, but there have been cases of fraudulent practice. So, it’s critical to thoroughly check out a potential financial advisor–preferably interview two or three.

Most financial planners fall into one of two categories based on how they are paid: commissions or fees. *Commission-based planners* earn commissions on the financial products they sell, whereas *fee-only planners* charge fees based on the complexity of the plan they prepare. Many financial planners take a hybrid approach and charge fees and collect commissions on products they sell, offering lower fees if you make product transactions through them.

 The way a planner is paid—commissions, fees, or both—should be one of your major concerns. Obviously, you need to be aware of potential conflicts of interest when using a planner with ties to a brokerage firm, insurance company, or bank. Many planners now provide clients with disclosure forms outlining fees and commissions or various transaction costs.

**1-16 Discuss the following statement: “The interactions among government, business, and consumers determine the environment in which personal financial plans must be made.”**

 Government, businesses, and consumers are the three major participants in the economic system. *Government* provides the structure within which businesses and consumers function. In addition, it provides a number of essential services that generally improve the quality of the society in which we live. To create this structure, various regulations are set forth, and to support its activities and provision of essential services, taxes are levied. These activities tend to constrain businesses and consumers.

 *Businesses* provide goods and services for consumers and receive money payments in return. They also employ certain inputs in producing and selling goods and services. In exchange they pay wages, rents, interest, and profit. Businesses are a key component in the circular flow of income that sustains our economy. They create the competitive environment in which consumers select from many different types of goods and services. By understanding the role and actions of businesses on the cost and availability of goods and services, consumers can better function in the economic environment and, in turn, implement more efficient personal wealth maximizing financial plans.

 *Consumers* are the focal point of the personal finance environment. Their choices ultimately determine the kinds of goods and services that businesses will provide. Also, consumer spending and saving decisions directly affect the present and future circular flows of income. Consumers must; however, operate in the financial environment created by the actions of government and business. Consumers may affect change in this environment through their elected officials, purchasing decisions and/or advocacy groups. Yet, basically, change occurs slowly and tediously, often with less than favorable results. Thus, consumers should attempt to optimize their financial plans within the existing financial environment.

**1-17 What are the stages of an economic cycle? Explain their significance for your personal finances**.

 The stages of the economic cycles are *expansion, peak, contraction*, and *trough.* Each of these stages relates to real gross domestic product (GDP), which is an important indicator of economic activity.The stronger the economy, the higher the levels of real GDP and employment*.* During an *expansion,* employment is high, the economy is active and growing, and prices tend to rise. During an expansion, real GDP increases until it hits a peak, which usually signals the end of the expansion and the beginning of a contraction. During a contraction, real GDP falls into a trough, which is the end of a contraction and the beginning of an expansion. An understanding of these four basic stages, coupled with knowledge of the stage in which the economy is presently operating, should permit individuals to adjust and implement financial actions in order to efficiently and successfully achieve their personal financial goals.

**1-18 What is *inflation*, and why should it be a concern in financial planning?**

 *Inflation* is a state of the economy in which the general price level is rising. It is important in financial planning because it affects what we pay for goods and services; it impacts how much we earn on our jobs; it directly affects interest rates and, therefore, it affects such things as mortgage and car loan payments. The most common measure of inflation is the *consumer price index,* which is based on the changes in the cost of a typical “market basket” of consumer goods and services. This can be used to compare changes in the cost of living over time for the typical family. Inflation is measured by the percentage change in the consumer price index from one time period to another, so that as the CPI rises, the cost of living also increases.

**1-19.** **“All people who have equivalent formal education earn similar incomes.” Do you agree or disagree with this statement? Explain your position.**

 Disagree. Although higher levels of education may result in higher levels of income, this does not mean that everyone with a given level of education will achieve a specified level of income. Factors such as age, marital status, geographical location, and career choice also impact a person’s level of income. A number of other factors, such as the degree of personal motivation and the methods by which one utilizes his or her formal education, can also affect one’s income level.

**1-20** **Discuss the need for career planning throughout the life cycle and its relationship to financial planning. What are some of your own personal career goals?**

 *Career planning* is a critical part of the life cycle of the personal financial planning process. The choice of a career affects the amount you earn. By setting both short- and long-term career goals, you can incorporate them into your financial plans. For example, if you need additional education and/or other training for a particular job, you may include a savings plan to obtain the needed funds. You should reevaluate your career decision periodically to see if it still meets your personal and financial goals. Other important considerations with regard to a specific job (and company) include the earnings potential, advancement opportunities, and benefits, plus how well the job fits your lifestyle and values. In today’s rapidly changing job environment, you should expect to change careers several times. It is important to keep up with developments in your industry, acquire a broad base of experience, and continue to learn new skills, both general and technical.

 Each student will, of course, have a different list of personal career goals based upon his or her career orientation and goals. However, responses should include discussion of personal financial planning and associated career planning goals and how a career choice would best fulfill quality of life, standard of living, and wealth maximization objectives. Goals might include getting a bachelor’s, master’s or other degree, working in a specific industry, owning one’s own business, finding a job in a different area of the country or overseas, achieving a desired salary and/or responsibility level by a certain age, or finding a job that meets lifestyle needs.

#### **Financial Planning Exercises**

1. ***Benefits of Personal Financial Planning.* How can using personal financial planning tools help you improve your financial situation? Describe changes you can make in at least three areas.**

Student answers will vary. In general, personal financial planning tools help individuals to organize their finances, evaluate their current financial condition, and track changes in their financial condition throughout their life to see if they are making progress toward their financial goals. Use of Budgets, Income Statements, and Balance Sheets will provide the information you need to maintain a financial plan.

1. ***Personal Financial Goals and the Life Cycle. Use Worksheet 1.1.* Describe your current status based on the personal financial planning life cycle shown in Exhibit 1.7. Fill out Worksheet 1.1, “Summary of Personal Financial Goals,” with goals reflecting your current situation and your expected life situation in 5 and 10 years. Discuss the reasons for the changes in your goals and how you’ll need to adapt your financial plans as a result. Which types of financial plans do you need for your current situation, and why?**

Student answers will vary depending on their personal situation. The purpose of this exercise is to encourage students to focus on how their personal goals and plans will change over their financial planning life cycle and also to help them be specific in setting their goals by designating dollar amounts and dates.

1. ***Personal Financial Goals.* Recommend three financial goals and related activities for someone in each of the following circumstances:**

**a. A junior in college**

**b. A 30-year-old computer programmer who plans to earn an MBA degree**

**c. A couple in their 30s with two children, ages 3 and 6**

**d. A divorced 42-year-old man with a 16-year-old child and a 72-year-old father who is ill**

Student answers will vary. Suggestions may include the following:

1. Junior in college—pay off all credit card debt by graduation; pay off all student loans within 10 years of graduation; save $2,000 for a down payment on another vehicle during the next 2 years.
2. 30-year old computer programmer who plans to earn an MBA—pay off auto loan before beginning degree; find a cheaper place to live; set aside $5,000 for emergency use during school.
3. Couple in their thirties with two children, ages three and six—begin college fund for each child; fund Roth IRAs for both parents; max out employer-sponsored retirement plan, such as 401k, each year.
4. Divorced 42-year old man with a 16-year old child and a 72-year old father who is ill—engage the help of friends or family in carpooling teenager to school and activities; explore community or church programs which might provide assistance for the father, such as Meals on Wheels or a visitation program; help father with estate planning needs, hiring an attorney if needed.
5. ***Life Cycle of Financial Plans.* Ben Saunders and Ashley Tinsdale are planning to get married in six months. Both are 30 years old have been out of college for several years. Ben uses three credit cards and has a bank account balance of $7,500 while Ashely only uses one credit card and has $9,500 in her bank account. What financial planning advice would you give the couple?**

Two issues are presented here: Number of credit cards and number of checking accounts. Having too many credit cards can lower you FICO score and your credit rating because you have the potential of maxing out on each of the cards and getting into financial difficulty. Ben should reduce his cards to one. Ashley should keep her card.

Two bank accounts can work OK if the various expenses are allocated between the two spouses. If one spouse has the job of paying all the bills, that spouse needs to have access to all accounts, which defeats the purpose of multiple accounts. Most couples have only one checking account.

1. ***Impact of Economic Environment on Financial Planning.* Summarize current and projected trends in the economy with regard to GDP growth, unemployment, and inflation. How should you use this information to make personal financial and career planning decisions?**

Answers on economic trends will depend on current economic conditions. If the GDP is growing, the economy is expanding and general economic conditions are considered favorable. Unemployment is probably low, and jobs are available. If the GDP is slowing, the economy may not be doing well, and jobs may be scarce. Changes in the CPI indicate the level of inflation. If inflation is rising, purchasing power is declining, and you will need more money to achieve your financial goals. In periods of high inflation, interest rates rise making it more difficult to afford big-ticket items.

1. ***Financial Impact of Career Decisions.* Alice Reynolds and Tricia Bostwick, both freshman and friends at a major university, are interested in going into a health sciences career. While they're not just interested in the money they can make, they do want to have a sense of the compensation in different health sciences careers. What do the data in Exhibit 1.13 tell Alice and Tricia?**

The income level of “doctors and pharmacists” is six figures which should provide a comfortable standard of living. The registered nurse salary, $68,910, if doubled [Ben and Tricia both are RNs], provides a similar six figures standard.

Of course, any of these careers can lead to management positions in large health care organizations that can result is a very comfortable standard of living.

So in summary, health sciences careers look favorable for high level of standard of living.

1. ***Career Choices and Financial Planning.* Assume that you graduated from college with a major in marketing and took a job with a large consumer products company. After three years, you are laid off when the company downsizes. Describe the steps you’d take to “repackage” yourself for another field.**

Possible steps to “repackage” yourself might include:

* Analyzing skills and experience to identify transferable skills
* Looking for companies in related fields and industries
* Considering your own interests to see if other career paths make sense
* Networking extensively
* Researching fields that use your skills
* Developing functional resume focusing on skills rather than job titles**inane**

**Critical Thinking Cases**

***1.1 Jim’s Need to Know: Personal Finance or Golf?***

During the Christmas break of his final year at the University of Maryland (UMD), Jim Curtis plans to put together his résumé in order to seek full-time employment as a software engineer during the spring semester. To help Jim prepare for the job interview process, his older brother has arranged for him to meet with a friend, Lisa Bancroft, who has worked as a software engineer since her graduation from UMD two years earlier. Lisa gives him numerous pointers on résumé preparation, the interview process, and possible job opportunities. After answering Jim’s many questions, Lisa asks Jim to update her on UMD. As they discuss courses, Lisa indicates that of all the electives she took, the personal financial planning course was most useful. Jim says that, although he had considered personal financial planning for his last elective, he’s currently leaning toward a beginning golf course. He feels that the course will be fun because some of his friends are taking it. He points out that he doesn’t expect to get rich and already knows how to balance his checkbook. Lisa tells him that personal financial planning involves much more than balancing a checkbook, and that the course is highly relevant regardless of income level. She strongly believes that the personal financial planning course will benefit Jim more than beginning golf—a course that she also took while at UMD.

***Critical Thinking Questions***

1. Describe to Jim the goals and rewards of the personal financial planning process.

2. Explain to Jim what is meant by the term *financial planning* and why it is important regardless of income.

3. Describe the financial planning environment to Jim. Explain the role of the consumer and the impact of economic conditions on financial planning.

4. What arguments would you present to convince Jim that the personal financial planning course would benefit him more than beginning golf?

**Jim’s Need to Know: Personal Finance or Golf?**

1. Personal financial planning is a process through which financial plans are developed and implemented to achieve personal financial goals. An individual can develop these goals in a fashion consistent with his or her emotional needs and preferences. As a process, personal financial planning is dynamic and prospective as well as immediate and retrospective. Furthermore, it can be adjusted to changes in goals, emotional orientation, available resources, and the economic environment.

2. Personal financial planning covers the key elements of one’s financial affairs and provides a plan to achieve financial goals. Income level is one input in the process but does not dictate its importance. An efficient, well-developed personal financial plan can help to maximize an individual’s wealth and quality of life given his or her income and goals. If desired goals cannot be met with a given level of income, financial planning will help evaluate what is really important and establish realistic and attainable goals. Thus, financial planning is important regardless of one’s income.

3. The personal financial planning environment is made up of three key groups, all of which Jim will contact directly or indirectly. *Government* establishes an intangible structure in which an economy or society must function. It levies taxes to fund its operations and institutes regulations which direct and control the actions of the participants in the economic environment. *Businesses* produce goods and services, employ labor, and use land and capital. They receive money as payment for their goods and services and pay wages, rents, interest, and profit. Businesses are a key part of the circular flow of income supporting our economy. Businesses establish the price and availability of goods and services in our economy through competitive interaction with each other and interfacing with government and consumers. Finally, the *consumer* is the focal point of the financial planning environment. Consumer choices determine the types of products and services businesses provide. Because consumers are net providers of funds to government and businesses, their decisions to spend or save have a major effect on the planning environment. However, government and businesses place a number of constraints on the environment, and consumers must therefore function within those limits.

 The economy is a dynamic mechanism that reacts to numerous inputs. Economic fluctuations can cause significant changes in one’s wealth, thereby affecting financial plans. Changes in price levels result from increases in inflation, which can directly affect an individual’s present and future consumption patterns, level of wealth, standard of living, and quality of life. Changes in economic conditions also affect nearly all aspects of one’s financial life, from career choices to retirement. Thus, the state of the economy and its fluctuations are important factors defining the financial planning environment and affecting how one implements a financial plan.

4. Although beginning golf would probably provide a great deal of personal satisfaction, personal finance would, in the long run, provide more benefits. The personal finance course will help Jim better understand the financial environment, thereby allowing him to establish a realistic quality of life and personal financial goals. He could then develop a plan to achieve his goals and a methodology for monitoring the ongoing effectiveness of that plan. With an understanding of the personal finance environment, the financial planning process, and goal setting techniques, Jim can optimize the use of his assets, provide for a secure financial future, and acquire the resources to realize his quality of life goals. Finally, the rewards achieved from using these financial planning techniques could, in the future, allow Jim to take not only beginning golf but also intermediate golf and possibly join a golf club.

**1.2** **Brad’s Dilemma: Finding a New Job**

**Brad Smitham,, a 53-year-old retail store manager earning $75,000 a year, has worked for the same company during his entire 28-year career. Brad was recently laid off and is still unemployed 10 months later, and his 10 months’ severance pay and 6 months’ unemployment compensation have run out. Because he has consistently observed careful financial planning practices, he now has sufficient savings and investments to carry him through several more months of unemployment. Brad is actively seeking work but finds that he is overqualified for available lower-paying jobs and underqualified for higher-paying, more desirable positions. There are no openings for positions equivalent to the manager’s job he lost. He lost his wife several years earlier and is very close to his two grown children, who live in the same city.**

**Brad has these options:**

**• Wait out the recession until another retail store manager position opens up.**

**• Move to another area of the country where store manager positions are more plentiful.**

**• Accept a lower-paying job for two or three years and then go back to school evenings to finish his college degree and qualify for a better position.**

**• Consider other types of jobs that could benefit from his managerial skills.**

***Critical Thinking Questions***

**1. What important career factors should Brad consider when evaluating his options?**

**2. What important personal factors should Brad consider when deciding among his career options?**

**3. What recommendations would you give Brad in light of both the career and personal dimensions of his options noted in Questions 1 and 2?**

**4. What career strategies should today’s workers employ in order to avoid Brad’s dilemma?**

This case asks students to consider the long-range implications of career and financial planning. In today’s business world, changes in the economy and in corporate strategies often result in workforce downsizing. Many students may be faced with the loss of a job during their working years. They may find themselves in Brad’s position, overqualified for some jobs and underqualified for others. Knowing what steps to take to avoid this situation is an important aspect of career and financial planning.

There are many correct answers to these questions; some possibilities are given below.

1. Important career factors for Brad to consider when looking for a new job include salary, opportunity for advancement, his transferable skills that could apply to a field other than retailing, availability of benefits, available training programs, types of industries and companies (size, work environment, etc.) that interest him, and tuition reimbursement policies so he can finish his degree.

2. Personal factors that Brad should take into account as he investigates job opportunities include location/need to relocate (his children live in the area), personal lifestyle needs (is he willing to travel, work overtime, commute further?), type of work situation most suitable for him (managing others, part of a team, level of public contact, etc.), and any personal interests that could open doors to a new career. (There is some overlap between career and personal factors.)

3. Brad should consider a lower-paying job on a short-term basis and at the same time look for a managerial job in another field. He cannot afford to wait out the recession; his funds will run out in a few months. This two-pronged approach is therefore preferable to one or the other. A job at a lower salary, particularly one with good benefits and a tuition reimbursement policy, would allow him to finish his degree or obtain other job training to qualify for a better position. Because he has no dependents, he should be able to cover his living expenses, although he may have to cut back on some discretionary expenses. He should look in several fields and not limit himself to retailing, particularly if he does not wish to relocate to another area of the country away from his grown children. If he is committed to staying in retailing, he probably will have to move. He needs to determine his personal priorities to make these decisions. We do not have enough information to know what they would be. He may want to participate in some career workshops or get some career counseling to work out some of these issues.

4. There are many strategies today’s workers can employ to avoid being placed in Brad’s position. Staying with one employer and one basic type of work for 28 years, as Brad did, will be the exception rather than the rule. Job changes, whether voluntary or involuntary, should be made with certain objectives in mind, such as broadening your base of experience and learning new skills—for example, computer skills and management responsibility. Keeping up with industry trends and overall economic conditions is very important. This can alert you to the skills needed for future success and provide advance warning of possible downsizings. Don’t allow yourself to be “pigeonholed” into one very specific type of job for too long; look for opportunities to transfer within your company or to another firm to get more diverse experience. Think of your capabilities in terms of general skills that can be applied to other jobs, companies, and industries. Develop and maintain a network of professional contacts in firms and industries that appeal to you, and be willing to share your knowledge with others who need your help.

**Key terms**

**average propensity to**

**consume** The percentage of each dollar of income, on average, that a person spends for current needs rather than savings.

**consumer price**

**index (CPI)** A measure of inflation based on changes in the cost of consumer goods and services.

**Contraction** The phase of the economic cycle when real GDP falls.

**expansion** The phase of the economic cycle when levels of employment and production are high and the economy is growing, generally accompanied by rising prices for goods and services.

**financial assets** Intangible assets, such as savings accounts and securities, that are acquired for some promised future return.

**financial goals** Results that an individual wants to attain, such as buying a home, building a college fund, or achieving financial independence.

**flexible-benefit**

**(cafeteria) plan** A type of employee benefit plan wherein the employer allocates a certain amount of money and then the employee “spends” that money for benefits selected from a menu covering everything from child care to health and life insurance to retirement benefits.

**gross domestic**

**product (GDP)** The total of all goods and services produced in a country; used to monitor economic growth.

**goal dates** Target dates in the future when certain financial objectives are expected to be completed.

**Inflation** A state of the economy in which the general price level is increasing.

**money** The medium of exchange used as a measure of value in financial transactions.

**peak** The phase of the economic cycle when an expansion ends and a contraction begins.

**personal financial planning** A systematic process that considers important elements of an individual’s financial affairs in order to fulfill financial goals.

**professional**

**financial planner** An individual or firm that helps clients establish financial goals and develop and implement financial plans to achieve those goals.

**standard of living** The necessities, comforts, and luxuries enjoyed or desired by an individual or family.

**tangible assets** Physical assets, such as real estate and automobiles, that can be held for either consumption or investment purposes.

**trough** The phase of the economic cycle when a contraction ends and an expansion begins.

**utility** The amount of satisfaction received from purchasing certain types or quantities of goods and services.

**wealth** The total value of all items owned by an individual such as savings accounts, stocks, bonds, home, and automobiles.

**Chapter Outline**

**Learning Goals**

**I. The Rewards of Sound Financial Planning**

 A. Improving Your Standard of Living

 B. Spending Money Wisely

 1. Current Needs

 2. Future Needs

 C. Accumulating Wealth

 \*Test Yourself\*

**II. The Personal Financial Planning Process**

A. Steps in the Financial Planning Process

B. Defining Your Financial Goals

 1. The Role of Money

 2. The Psychology of Money

 C. Money and Relationships

D. Types of Financial Goals

E. Putting Target Dates on Financial Goals

 1. Long-term Goals

 2. Short-term Goals and Intermediate Goals

 \*Test Yourself\*

**III. From Goals to Plans: A Lifetime of Planning**

A. The Life Cycle of Financial Plans

B. Plans to Achieve Your Financial Goals

 1. Asset Acquisition Planning

 2. Liability and Insurance Planning

 3. Savings and Investment Planning

 4. Employee Benefit Planning

 5. Tax Planning

 6. Retirement and Estate Planning

C. Special Planning Concerns

 1. Managing Two Incomes

 2. Managing Employee Benefits

 3. Managing Your Finances in Tough Economic Times

 4. Adapting to Other Major Life Changes

D. Technology in Financial Planning

E. Using Professional Financial Planners

F. Types of Planners

G. Choosing a Financial Planner

\*Test Yourself\*

**VI. The Planning Environment**

A. The Players

 1. Government

 a. Taxation

 b. Regulation

 2. Business

 3. Consumers

B. The Economy

 1. Economic Cycles

 2. Inflation, Prices, and Planning

 \*Test Yourself\*

**V. What Determines Your Personal Income?**

 A. Demographics and Your Income

 B. Your Education

 C. Where You Live

 D. Your Career

 E. Planning Your Career

 \*Test Yourself\*

**Summary**

**Key Terms**

**Financial Planning Exercises**

**Applying Personal Finance**

Watch Your Attitude!

**Critical Thinking Cases**

 1.1 Jim’s Need to Know: Personal Finance or Golf?

 1.2 Brad’s Dilemma: Finding a New Job

**Money Online!**