YELLOW RIBBON REINTEGRATION PROGRAM®

Financial Literacy: Borrowing and Saving Basics

Facilitator Guide

FOR THOSE WHO SERVE AND THOSE WHO SUPPORT

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Financial Literacy: Borrowing and Saving Basics

Facilitator Note:

The following two symbols are used as indicators:
💻 (computer) indicates it is time to advance the slide on the associated PowerPoint;
✋ (hand) indicates there is an exercise associated with the content.

*Essential class content is noted in **bold**.*

All class handouts are available for download on the YRRP website at www.yellowribbon.mil/cms/event-handout. Unless otherwise specified as online only in the Materials section below, all handouts should be printed for distribution to class participants.

Class Description:

This class covers recommended borrowing and saving practices and discusses how to apply best practices related to borrowing and saving.

Stage:

Pre-deployment, During deployment, Post-deployment

DoDI:

1342.28 DoD Yellow Ribbon Reintegration Program (YRRP)

The content of this class has been developed for the Department of Defense Yellow Ribbon Reintegration Program. The Clearinghouse for Military Family Readiness at Penn State has reviewed the class and is responsible for content management.

Audience:

YRRP attendees

Time:

45 minutes

Equipment:

- Projector
- Laptop
- Pens
- Paper
- Calculators

Materials:

- Facilitator Guide
- Core Material Checklist
- PowerPoint Presentation
  1. Financial Literacy: Borrowing and Saving Basics
  2. Objectives
  3. Money
  4. Lending Money Is a Business
  5. Principal
  6. Interest
  7. Credit Utilization
  8. Ways to Improve Credit Utilization
  9. What Determines Your Credit Score?
  10. Annual Percentage Rate (APR)
  11. Finance Charge
  12. Debt-to-Income Ratio
  13. Borrowing Basics Recap
  14. Saving Money
  15. Cash Equivalents
  16. Savings/Share Account
  17. Certificate of Deposit (CD)
  18. Money Market Deposit Account
  19. Compound Interest
  20. Compounded Interest Examples
  21. Annual Percentage Yield (APY)
  22. Rule of 72
  23. Saving Basics Recap
  24. Financial Planning
  25. Review of Objectives
  26. Financial Literacy: Borrowing and Saving Basics
- Handouts

1. Amortization Schedule
2. Practice Problems for Credit Utilization and Debt-to-Income Ratio
3. Annual Percentage Rate Illustration
4. Car and Home Mortgage Loan Examples
5. Online Resources (online only)

Exercises:

1. Your First Borrowing Experience
2. Calculating Credit Utilization
3. Calculating Debt-to-Income Ratio
4. Financial Goal Setting Exercise

Objectives:

After completing this class, participants will be able to do the following:

1. Define borrowing and saving terms and concepts.
2. Identify the difference between interest rates and annual percentage rates.
3. Identify key borrowing ratios.
4. Identify best practices related to borrowing and saving that can impact financial stability and wealth.

Introduction

SHOW Slide 1: Financial Literacy: Borrowing and Saving Basics

Facilitator Note:

Introduce yourself as the facilitator. State your name, military experience or affiliation, and perhaps one additional brief bit of relevant personal information that establishes your credibility (i.e., your professional training or experience).

Please limit your personal introduction to no more than 2 minutes to maximize the time attendees are able to engage with course content, practice skills, and participate in self-reflection activities.

Welcome to Borrowing and Saving Basics. Today, we will discuss how you can save and borrow wisely to **minimize your cost when borrowing and to maximize your earnings when saving**. It can help you accumulate more money for your needs, while it minimizes the amount of your money that goes to increasing the bottom line for lenders.

SHOW Slide 2: Objectives

Mastering terms and concepts related to borrowing and saving is important; however, **using or practicing the behaviors associated with that knowledge is needed to improve financial stability and build wealth** (Consumer Financial Protection Bureau [CFPB], 2017).

In this class, we will discuss terms and concepts, related to these areas, that are important to know. We will cover tips and strategies that may increase your confidence as you move ahead with your borrowing and saving needs.

After completing this class, you will be able to do the following:

1. **Define borrowing and saving terms and concepts.**
2. **Identify the difference between interest rates and annual percentage rates.**
3. **Identify key borrowing ratios.**
4. **Identify best practices related to borrowing and saving that can impact financial stability and wealth.**

SHOW Slide 3: Money

Money is a tool. By the time most of us are 3 years old, we understand that money is needed to buy toys or candy.

Money can be a conversation about life. What you do with your money directly influences how you live (e.g., the food you eat, where you reside, and the form of transportation you use) each day.

Freedom is something each of you understands and will be protecting as you and your families serve the country through military service and support. During today's class, I would like you to keep the words discipline and freedom in mind but with a financial twist. Why? Because much of what we talk about today will be fundamentals related to borrowing and saving. **Some of today's topics may be new to some of you**. However, if you master the terms and concepts we discuss and exercise discipline when it comes to handling your financial affairs, you will achieve a level of financial freedom that alludes many people in this country (Scheresberg, 2013). When it comes to money matters, **discipline is a key to building financial security and wealth**.

EXERCISE 1: Your First Borrowing Experience

Facilitator Note:

The purpose of this exercise is for participants to think about their past financial decisions. This should take approximately 5 minutes.

First, please raise your hand if you have ever borrowed money from a bank, a credit union, a payday lender, a finance company, or an insurance company. I want you to think about the first time you borrowed money.

PAUSE for participants to lower their hands after each of the following statements.

Lower your hand if any of the following statements are true:

1. You were 100% confident that the decision you were making was the best one you could have made.
2. You depended primarily on the loan officer/lender to guide you through the maze of paper.
3. You were clueless and dependent on a parent or other family member to decipher or explain the terms of the contract you were entering.

For those with a hand still raised, would you like to share your borrowing experience with the rest of us?

PAUSE for responses.

The reason for this brief exercise was to highlight that **most of us have probably made at least one borrowing decision as young adults without completely understanding the terms and conditions related to the agreement we were making**. That lack of knowledge may have cost us extra money. However, after today's session, **you will have enough basic information and resources to help you enter a loan agreement with confidence in your decisions**.

SHOW Slide 4: Lending Money Is a Business

Before we talk about key borrowing terms, we need to discuss the obvious about a fact for those in the money lending business. **Lending money is a business, and, typically, the purpose for any business is to make money.** Lenders make money by offering terms and conditions that help the borrower get what he or she needs or wants. In return, the lenders will charge fees, so they can cover their business expenses, such as pay the building rent, utilities, and support staff.

In short, when you borrow money, regardless of the source, the company's goal is to make a profit. How much they profit will, in part, depend on your knowledge and credit worthiness.

Whenever you borrow money, you need to do the following:

1. **Review your credit history weeks in advance so any corrections can be made if needed**;
2. **Obtain a recent credit score from one of the major credit reporting agencies**;
3. **Know how much you need to borrow**; and
4. **Compare the interest rates from the lenders you have on your list before deciding where to apply for the loan**.

Most importantly, understand that often lenders have the objective of increasing their profits. Be polite and friendly but do not let a lender's friendliness get in the way of your sound decision-making.

Now, let's talk about borrowing terms you need to understand before facing a lender.

SHOW Slide 5: Principal

Facilitator Note:

Handout 1 will be used. Participants will consider the example of an amortization schedule. This should take approximately 2 minutes.

Principal is the base amount of money you borrow from a lender.

When you borrow money, the initial amount you borrow is called the principal. When you repay the loan in installment payments, each payment is made up of two parts--part principal and part interest. Generally speaking, if you repay a loan in monthly installments for several years, the first year's payments have a larger portion of interest in the payments than principal. As you get closer to paying off the loan, the payments consist mostly of your principal. In short, lenders get most of their fees for a loan in the early days, months, or years of repayment. With each payment you make on an installment loan, the principal owed decreases and so does the amount of interest calculated on the outstanding principal owed.

Let's look at the repayment schedule, also called the amortization schedule, for a $5,000 personal loan. See **Handout 1: Amortization Schedule** for an example. Notice that while the monthly payment amount listed in Column B remains the same throughout the 2-year repayment period, the amount of principal and interest of each payment changes each month. Column C shows an increasing amount of principal being paid each month, and Column D shows a decreasing amount of each payment being interest. By the end of year one, the borrower has repaid 74% ($116.32) of the interest on the loan.

Borrowing Basics

SHOW Slide 6: Interest

Interest is a fee you pay a lender to borrow money, or it could be a fee you are paid when you put money in a savings account at a bank.

Let's talk about interest and interest rates when borrowing. For this discussion, we will use the term interest rate for clarity.

In lending situations, your interest rate is the cost of borrowing money expressed as a percentage, for example 2%, 5%, and 7%. **The interest rate lenders charge can depend on two factors**:

1. **Your creditworthiness**—in short, do you have a favorable credit rating, which suggests you are reliable and will repay as promised. **If you have misused credit in the recent years, it will cost you more to borrow money.**
2. The conditions in the economy and **how much it may cost lenders if they need to borrow money from a larger bank are also considerations**. In general, **if interest rates are high, it is more difficult to get a loan**. Regardless of whether the trending interest rates are low or high, it will be easier for credit-worthy consumers--those with a favorable credit history--to borrow money at a lower interest rate. Consumers who have negative information, especially unfavorable repayment information, will most likely have a higher interest rate.

Let's take a deeper look at creditworthiness by first looking at credit utilization.

SHOW Slide 7: Credit Utilization

Credit utilization is specific to credit cards. Simply put, **credit utilization is a ratio of your total credit card limit and the amount of credit that is actually used**. **Ideally, you want to keep your credit utilization to 30% or less of your credit card limit in order to not lower your score.** For example, suppose you have a credit card with a $1,000 limit. To stay in the ideal credit utilization zone, you will never want to charge more than $300 per billing period.

If you have several credit cards with different credit limits, you will want to keep the credit utilization for each card under 30%. Keeping credit card utilization under 30% signals to lenders you are a responsible borrower who is not overextending your access to credit. Credit utilization impacts your credit score. Therefore, it is important to keep your use of credit cards low and at or under 30%. Borrowing more than 30% signals to lenders you are stretching your credit card borrowing capacity. Finally, some refer to credit utilization as **balance-to-limit** ratio or **debt-to-limit** ratio.

EXERCISE 2: Calculating Credit Utilization

Facilitator Note:

Handout 2 will be used. The purpose of this exercise is for participants to calculate credit utilization. Participants will complete the example problems on page 1. This should take approximately 4 minutes.

Let's practice calculating credit utilization. Example problems are provided on **Handout 2: Practice Problems for Credit Utilization and Debt-to-Income Ratio**. Are there any questions before we begin?

PAUSE for responses.

GIVE participants approximately 4 minutes to complete their calculations.

Would anyone like to share their calculations?

PAUSE for responses. (Possible answers: card 1 = 53%; card 2 = 2.4%; card 3 = 5%; card 4 = 20%)

Good job everybody. I encourage you to calculate your own credit utilization and to look back at your 2 or 3 most recent statements to determine your actual utilization ratio for your cards.

SHOW Slide 8: Ways to Improve Credit Utilization

If you want or need **to improve your credit utilization rate, there are several things you can do**. You can do the following…

- **Pay off credit card balances on existing cards monthly.**
- **Put a balance alert on your card.** For example, if my maximum credit utilization limit on a card is $1,500, the balance alert could be $1,400.
- **Increase the credit card limit but still maintain a 30% or less utilization rate.** One or two credit cards with large credit limits allows you to charge more per month without worrying too much about your credit card utilization rate. For example, if you have a credit card with a $5,000 limit, you can charge $1,500 a month. Of course, you need to pay the bill in full each month in order to charge the $1,500 in following months. This strategy may work for you if you are disciplined and use your credit card as a tool to help you track your spending.

SHOW Slide 9: What Determines Your Credit Score?

A **credit score is a number calculated from the data on a credit report**, like credit utilization and payment history. **A credit score helps lenders to determine your credit worthiness** (CFPB, n.d.).

Let's look at what factors go into calculating a credit score. The greatest factor, 35%, comes from whether you pay your bills on time; that is, do you make at least the minimum payments by the due date.

The second greatest factor, 30%, is based on how much you owe. This links to credit utilization and why it is important to keep your credit use to 30% or less of the credit available to you. When your credit utilization is above 30%, it decreases your credit score. A low credit score means you pay more in the way of higher annual percentage rates or interest rates to use credit.

Other factors that influence your credit score include length of credit history, new accounts, and type of credit used.

The credit score is calculated using information in your credit report. In short, your credit report is your financial reputation on paper. In many ways, it is your financial report card. A credit report tells lenders how reliable you are in repaying loans and if you can handle additional debt.

If you have not seen your credit report in the past 12 months, you can visit the Annual Credit Report website at www.annualcreditreport.com to request a copy of your report. Your request will not affect your credit score but will provide you with real data that potential creditors will see when considering your loan application. **Checking your credit report is also important for guarding against fraud.** Thanks to federal legislation, you get your credit report for free every 12 months from these three credit reporting agencies:

- Experian
- TransUnion
- Equifax

This means that you can obtain a total of three free credit reports a year. You are responsible for ensuring that your credit report is accurate and updated, so it is important to regularly check it.

Protecting your credit is an important thing to do as a civilian and as a member of the military. **While you are training or deployed, you can place Active Duty alerts on your credit reports**. The website links for placing these alerts can be found on Handout 5: Online Resources and can be downloaded from YRRP website at www.yellowribbon.mil/cms/event-handout. In addition, there is a link to information about the Servicemembers Civil Relief Act, which is a program that provides certain protections from civil actions against Service members who are called to Active Duty. This is very important to be familiar with this prior to any deployment.

SHOW Slide 10: Annual Percentage Rate (APR)

Facilitator Note:

Handout 3 will be used. Participants will consider the examples presented. This should take approximately 2 minutes.

Now, let's take a look at annual percentage rate or APR. The **APR is the annual charge borrowers pay to lenders for loans**. The **APR is the advertised interest rate plus any fees lenders require borrowers to pay when taking out a loan**. For big-ticket items, like a mortgage, this could take decades to repay, so **the APR should be**

the focus of borrowers instead of the interest rate. Why? **Because when you include fees required by the lender for the loan, the APR will usually be more than the advertised interest rate.** Two lenders with the same advertised interest rates and different required fees could have APRs that are very different. Assuming that all services are equal in terms of what you need, in general, the higher the APR, the more it will cost you to borrow money. In other words, if everything about two lenders is equal and you need a tiebreaker to make a decision, APR could be the deciding factor.

Let's look at **Handout 3: Annual Percentage Rate Illustration** to see this in numbers. In Table 1, the loan amount is $10,000. There are two lenders with the same advertised loan interest rate of 3%. However, the lenders have different amounts for a required fee that are not advertised but will be financed with the principal amount borrowed - the $10,000. This fee may not be revealed early in the loan process unless the borrower asks enough questions prior to signing the loan paperwork or reads the fine print to see if additional fees are part of the loan. See the column labeled APR or annual percentage rate. Even though the advertised interest rate is the same for both lenders, because they have different required fees for the loan, the APR is higher for Lender B. You will also note the total amount repaid to Lender B is higher - $10,728 vs. $10,521.80.

Table 2 has the same loan amount but a longer repayment period - 5 years. In addition to the same points made by Table 1, a key take away from this table is **the longer the repayment period, the more you will pay in interest for a loan** even though the APR for the loan is lower than the APR for a loan with a shorter repayment period and the same advertised interest rate.

SHOW Slide 11: Finance Charge

Facilitator Note:

Handout 4 will be used. Participants will consider the examples presented. This should take approximately 2 minutes.

The finance charge is the sum of all of the fees you pay when borrowing money. The fees that you pay are impacted by factors, such as interest rate, service charges, and length of the loan period.

To illustrate how interest rate and length of repayment period influence the finance charge paid, let's look at **Handout 4: Car and Home Mortgage Loan Examples**. In the Car Loan Example 1, focus first on row one (1) that lists the repayment periods of 60 months, 48 months, and 36 months. Now, look at row 4 that is labeled Total Interest Paid/Finance Charge. You can see that as the loan repayment period decreases, even though the interest rate is higher for the shorter repayment period of 36 months, the

total amount repaid is less - only $1,546.73 for a 3-year repayment period vs. $2,295.32 for a loan repaid over 5 years with a lower interest rate of 4.36%.

To illustrate further, please examine how the loan repayment period influences the total amount you repay in Car Loan Example 2. The interest rate is the same, 4.36%, for each repayment period. Now, look at row 4 labeled Total Interest Paid/Finance Charge. Again, you can see that the longer the loan repayment period, the more finance charges you pay even though the amount you pay per month is smaller.

The difference in the finance charge in the Home Mortgage Example of 30 years vs. 15 years repayment should motivate many homeowners to try and repay their mortgage in 15 years instead of 30 years. That said, for some individuals, owning a home or car may only be possible if they make use of longer-term loans, which reduces the cost per month of monthly payments.

Additional factors that can contribute to a lender's loan decision include credit utilization and debt-to-income ratio.

SHOW Slide 12: Debt-to-Income Ratio

OK, let's talk about debt-to-income ratios.

A ratio is just a comparison of two numbers. **The debt-to-income ratio compares your monthly debt payments to your monthly gross pay.** Lenders use the debt-to-income ratio to help determine if you can comfortably take on more debt. **A debt-to-income ratio of 36% or lower is considered ideal.**

It is easy to calculate the debt-to-income ratio. Let's **take a minute to calculate the ratio for the example provided**.

Let's say you have four monthly payments.

Step 1: Total the monthly payments.

$800	Rent/mortgage
$600	Student loan payment
$400	Car payment
$200	Credit card bill
$2,000	**Total monthly payments**

Step 2: Determine your monthly gross pay. This is your pay before any taxes or deductions are subtracted by your employer. This number can be found on a monthly or biweekly pay stub. Let's assume we have a monthly gross pay of $5,000.

Step 3: Divide the total of your monthly debts by your monthly gross pay. The result will be your debt-to-income ratio.

$2,000/$5,000 = 40%

In this example, your debt-to-income ratio is 40%.

Remember, the lower the debt-to-income ratio, the better. Each lender will have his or her own cut-off for lending money. **The lower your debt-to-income ratio the more likely you are to get the loan you need with favorable conditions**. A general rule of thumb is to keep your total debt payments below one third of your pretax income, and, for most people, even lower will be less stressful. In the example above, the individual's debt-to-income ratio is high.

EXERCISE 3: Calculating Debt-to-Income Ratio

Facilitator Note:

Handout 2 will be used. The purpose of this exercise is for participants to practice calculating debt-to-income ratio. Participants will complete the 3 steps on page 2. This should take approximately 3 minutes.

Now, let's practice calculating a debt-to-income ratio. Using the example on **Handout 2: Practice Problems for Credit Utilization and Debt-to-Income Ratio**, calculate the 3 steps under the Debt-to-Income Ratio Practice Problem.

PAUSE for participants to fill out the debt-to-income practice problem on the handout.

Step 1: What is the total of the three recurring monthly debts?

PAUSE for responses. (Answer: $1,500)

Step 2: What is the gross pay?

PAUSE for responses. (Answer: $5,000)

Step 3: What ratio did you calculate for this practice problem?

PAUSE for responses. (Answer: $1,500/$5,000 = 30%)

So, let's review the difference between credit utilization and debt-to-income ratio by comparing key features of each.

Both numbers, your credit utilization rate and your debt-to-income ratio, impact your

ability to get loans. Your credit utilization rate has a bigger impact on your credit score and ideally should be 30% or lower. You will recall that a high credit score is a key to getting a low interest rate loan.

The debt-to-income ratio focuses on all outstanding monthly debt payments in relationship to your gross pay. This ratio affects your ability to get additional loans.

SHOW Slide 13: Borrowing Basics Recap

PAUSE for responses after each question.

What are some ideas to keep in mind when borrowing money from a lender?

What are some practices you use can use to improve your chances of paying a low interest rate when you borrow money?

What borrowing concepts do you recall and can you explain?

REVIEW the concepts listed below if they were not mentioned during the recap discussion.

Principal: the base amount that you borrow from a lender.

Interest: a fee you pay a lender to borrow money, or a fee you are paid when you put money in a savings account at a bank.

Interest rate: the cost of borrowing money expressed as a percentage, for example, 2%, 5%, and 7%.

APR: the annual charge borrowers pay to lenders for loans. The APR is the advertised interest rate plus any fees lenders require borrowers to pay when taking out a loan.

Finance charge: the total cost you pay for a single borrowing decision. The finance charge you pay is impacted by the interest rate of the loan, service charges, and the length of the loan period.

Credit utilization: a ratio of your total credit card limit and the amount of credit that is actually used. Ideal credit utilization is 30% or less of your credit card limit. Sometimes called the balance-to-limit ratio or the debt-to-limit ratio.

Credit score: a number calculated from a formula kept secret by lenders. A credit score helps lenders determine your credit worthiness.

Debt-to-income ratio: a comparison of your monthly debt payments to your monthly gross pay. Maintain a debt-to-income ratio of 36% or less.

Saving Basics

SHOW Slide 14: Saving Money

Now, let's look at some basics of saving money.

Think of **savings as short-term actions or behaviors that lead to long-term benefits**, such as a secure financial future. **Saving is a precursor to investing**. Some reasons we save are to have access to cash for emergencies (e.g., 3 to 6 months of living expenses), to accumulate cash for down payments on large-ticket items (e.g., a home), or to pay for short-term financial goals (e.g., replace an aging washer or dryer).

SHOW Slide 15: Cash Equivalents

Accounts used for savings, such as savings accounts, certificates of deposits, and money market deposit accounts are also known as cash equivalents. These accounts can easily be converted to cash without losing value.

SHOW Slide 16: Savings/Share Account

Savings accounts are deposit accounts that earn interest and have a low minimum balance to open or maintain.

Money can be deposited and withdrawn as needed in savings accounts. Although the term savings account is used in reference to accounts at banks and credit unions, generally credit unions call these accounts share accounts. These accounts are very safe (i.e., low risk) and, therefore, earn very little interest. In other words, the money you deposit will be there when you decide to withdraw it, regardless of how financial markets are performing.

Federally insured banks and credit unions will have signs posted on the buildings and/or websites. For banks, look for FDIC, which stands for Federal Deposit Insurance Corporation, and, for credit unions, look for NCUA, which stands for National Credit Union Administration. **It is important to ensure that you are banking with an FDIC or NCUA because this means that if the financial institution goes out of business, you would get your money back.** Currently, the rule is that you would be insured for up to $250,000 per account holder.

SHOW Slide 17: Certificate of Deposit (CD)

A certificate of deposit or CD is a deposit of money that you agree to leave in the bank or credit union for a predetermined amount of time at a certain interest rate. On the maturity date of the CD, you can renew it or take the cash. The maturity date is

the last day in the predetermined length of time you agreed to leave your money deposited in a CD. If you do nothing, most CDs will renew for the same time period (e.g., 6 months, 1 year, 2 years) at the current interest rate. Generally, the longer the term of the CD, the higher the interest rate you will earn.

SHOW Slide 18: Money Market Deposit Account

A money market deposit account operates like a checking account with some restrictions. They have a minimum deposit that can vary by institution. Money market deposit accounts also have a limit on the number of checks that can be written on the account each month. They usually pay more interest than a regular savings account. A money market deposit account is found at a bank or credit union. Remember, if housed in a federally insured institution, the deposits are insured up to $250,000.

Visit Handout 5: Online Resources on YRRP website at www.yellowribbon.mil/cms/event-handout for information regarding military savings programs for which you may be eligible, such as the Thrift Savings Plan (TSP), Blended Retirement System, and Savings Deposit Program (SPD).

SHOW Slide 19: Compound Interest

Compound interest or compounding. Unlike simple interest that is paid once a year on the principal amount deposited, **with compounding interest, you earn interest on the principal and interest amount each compounding period.** Compounding occurs daily, monthly, quarterly, semi-annually, or annually and varies among types of financial accounts and the institution where you have deposited your money. Your money grows faster when it is compounded. The more frequent the compounding period, the faster your money grows.

For example, on January 1 of any year, you deposit $100 in a savings account. The interest rate paid on that deposit is 3%. At the end of a period, the bank adds $3 to your account to represent the interest your $100 deposit has earned. The account value is now $103.

For the next period, you will earn 3% on the principal and the interest from the last period. At the end of the second period, the bank adds $3.09 to your account to represent the interest your $103 has earned. The account value is now $106.09.

If we leave that $100 in the bank for 5 years at the 3% interest rate, the value at the end of 5 years is $115.93.

SHOW Slide 20: Compounded Interest Examples

Here you can see the difference in the total amount of interest paid over 5 years for an account with annual compounding interest and semi-annual compounding interest.

Using $100 as the principal amount may not look impressive when you look at the total amount of interest earned. Think long term how account values can grow. When you start saving, the initial amount may be small, but, over time with additions and no withdrawals, the account values will grow.

Those who use compound interest to their advantage can put their money to work for them. For example, compare the savings account interest rates for local federally insured banks with the rates of federally insured online banks. **If the interest rates are the same for local and online banks but the compounding periods are different, choose the account that has the most frequent compounding period.**

SHOW Slide 21: Annual Percentage Yield (APY)

Annual percentage yield (APY) is the percentage that is based on the total interest you would receive for 365 days given an institution's annual simple interest and compounding frequency.

The Truth in Savings Act of 1991 requires banks and credit unions to use APYs for advertising, so depositors have a standard way to compare various savings deposit accounts (interest rates, fees, and terms) among institutions. It applies to personal or household accounts but not business accounts.

SHOW Slide 22: Rule of 72

While we live in an age where there is always a calculator at our fingertips, there is still a tool that relies on the basic math you learned in elementary school - **Rule of 72**. This rule simply states that **if you divide the number 72 by the annual interest rate you expect to earn on an account, you will have an idea of the length of time it takes that deposit to double**. For example, if you have a $10,000 inheritance or lottery winning, how long will it take the money to double to $20,000 if deposited into an account earning 8% annually? Of course, no withdrawals or additional deposits are considered.

72/8 (% interest rate) = 9 years.

As you can see from the slide, the lower the interest rate for the account, the longer it takes the money to double.

SHOW Slide 23: Saving Basics Recap

What saving terms/concepts do you recall and can you explain?

REVIEW the concepts listed below if they were not mentioned during the recap discussion.

Cash equivalents: accounts that can be converted to cash quickly without losing value (savings accounts, certificates of deposits also known as cash equivalents).

Share account: name used for savings accounts held in credit unions.

Certificate of deposit: a deposit of money that you agree to leave in the bank or credit union for a predetermined amount of time at a certain interest rate.

Compound interest: you earn interest on the principal and interest amount each compounding period. Compounding occurs daily, monthly, quarterly, or semi-annually and varies among types of financial accounts and the institution where you have deposited your money.

Annual percentage yield (APY): the percentage that is based on the total interest you would receive for 365 days given an institution's annual simple interest and compounding frequency.

Rule of 72: this rule simply states that if you divide the number 72 by the annual interest rate you expect to earn on an account, you will have an idea of the length of time it takes that deposit to double in value.

SHOW Slide 24: Financial Planning

EXERCISE 4: Financial Goal Setting Exercise

Facilitator Note:

The purpose of this exercise is for participants to reflect on and begin planning to meet their financial goals. This should take approximately 5 minutes.

Borrowing and saving are just tools to help you reach your financial goals. **What are some financial goals you have?**

PAUSE for responses. (Possible answers: retirement; college; buying a car; going on a trip; buying a house; starting a business)

You can use your understanding of saving and borrowing to create a plan to achieve your goals.

Let's practice setting and planning for a financial goal. On your note card, write down three financial goals that you would like to achieve. Then, for each goal, write down a step you can take in the next month- or few weeks from now – to start making that goal happen. For example, if you want to buy a car, you may want to start shopping around for loans first.

I encourage you to set an alert on your phone for a few weeks from now so that you are reminded to check in with yourself and evaluate the progress that you have made.

Summary

SHOW Slide 25: Review of Objectives

We covered a lot of information today. We discussed terms you should understand before borrowing, we covered fundamental facts related to saving money, and we highlighted ways to increase your credit worthiness and power as a borrower.

Let's see if we met the objectives:

1. **What is the difference between APY and APR?** *PAUSE for responses.*
   (Possible answers: APY relates to saving and is the total interest you would receive on a deposit for 365 days given an institution's annual simple interest and compounding frequency; APR relates to borrowing and is the annual or yearly cost borrowers pay lenders for loans; APR includes fees that are required by lenders for loans; you can use APR to compare the cost of loans from two or more institutions that may advertise the same interest rate; the higher the APR, the more the loan will cost you)

2. **What is the difference between interest rates and the APR?** *PAUSE for responses.*
   (Possible answers: in the case of loans, the interest rate is the cost of borrowing money expressed as a percentage [2%, 5%]; loan ads usually highlight the interest rates; APR is the annual charge borrowers pay lenders for loans; APRs include required fees related to loans; once the required fees are included in the loan, the APR will be higher than the advertised interest rate, thereby, increasing the cost of the loan; when shopping for loans, use the APR to compare your total costs)

3. **What are two key ratios related to borrowing money and what formula or information is needed to calculate each ratio?** *PAUSE for responses.*

(Possible responses: credit utilization: the amount of credit used divided by the credit card limit; e.g., $500 charged/$5000 credit limit = 10% credit utilization debt-to-income ratio: compares your monthly debt payments to your monthly gross pay - lenders use this ratio to help them determine if you can handle an additional loan; debt-to-income ratio is the total monthly debt payment divided by your monthly gross income [e.g., $1,000 monthly payments/$10,000 monthly income = 10% debt-to-income ratio])

4. **What is the ideal credit utilization ratio?** *PAUSE for responses.*
   (Possible answer: less than 30%)

5. **What is the ideal debt-to-income ratio?** *PAUSE for responses.*
   (Possible answer: each lender will have their own desired debt-to-income ratio; lower is better. More than 33% could be a negative signal)

6. **What are some best practices related to borrowing and saving that impact financial stability and wealth?** *PAUSE for responses.*
   (Possible answers: start saving early and each month; borrow only what you need; compounding interest will help your account values increase faster [i.e., make your money grow faster]; keep credit card utilization to 30% or less; keep debt-to-income ratio to 43% or less)

SHOW Slide 26: Financial Literacy: Borrowing and Saving Basics

I expect some of today's topics may have been a review or refresher for some of you.

I want to encourage all of you to think long term when it comes to money matters and that small amounts can add up to large amounts over decades. Becoming financially stable and being in a position to build wealth are highly dependent on your understanding and use of key concepts related to borrowing and saving. Discipline is a key to building wealth. Your discipline with money matters is in your hands.

Remember that Handout 5: Online Resources is available on the YRRP website at www.yellowribbon.mil/cms/event-handout and provides a list of resources that contain information related to borrowing and saving.

Good luck to all of you.

Before we conclude, are there any final questions or comments you wish to share?

PAUSE for responses.

Thank you, and please complete your evaluation for this class.

References

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