DO BANKS OFFER MORE THAN SAVINGS OR CHECKING ACCOUNTS?

Many banks offer a wide range of financial choices. These choices include money market funds and certificates of deposit, also called "CDs." Many common investments, such as stocks, bonds, and mutual funds, need to be purchased elsewhere.

The chart below shows the possible power of compound interest on a single investment of $100, compounded annually.

Saving or Investing Your Money

	Interest rate	**1-year total**	**10-year total**	**20-year total**	**30-year total**
Money market	2.5 %	$102.50	$128.01	$163.86	$209.76
CD	3.75%	$103.75	$144.50	$208.82	$301.75
Stocks	11%	$111.00	$283.93	$806.23	$2,289.23
Mutual funds	8%	$108.00	$215.89	$466.10	$1,006.27

Here are a few of the most common types of savings and investments.

Money market funds

A money market fund is one way to save—not invest—money. Most banks and investment firms offer money market funds. The advantages of a money market fund are that you can still get to your money rather quickly and there is little risk of losing the money. In fact, the funds offered by banks are federally insured.

The main drawback of a money market fund is that the interest you will earn is small—probably only a little bit more than a savings account.

Certificates of deposit

When you buy a certificate of deposit (known as a CD), you agree to "lock up" your money for a set period of time. This time period could be anywhere from three months to five years. When the time period is over, you get your initial investment back—plus interest. Usually, the longer you have a CD, the more interest it will earn.

CDs are very safe; in fact, they are insured. Still, the amount of interest you will earn will be small. So, CDs are better thought of as a way to save than a way to pay for long-term goals.

Stocks

When you own stock in a company, you become a part owner of that company—albeit a small owner. If your company does well (and the economy does well), your stock becomes more valuable. It might even pay part of its profits to you in the form of a "dividend." If your company doesn't do well, your stock will lose value.

Because the value of the stock depends on how well the company performs, stocks can be risky. Over time (and the "time" part is important), most stocks do increase in value. You may be able to earn much more with stocks than with CDs or money market funds. How can you lower the risk that comes with investing in stocks? Buy stock in more than one company. In other words, diversify. For most people, the best way to do that is to invest in stock mutual funds.

Bonds

When you buy a bond, you are loaning your money to a company or government. The company or government agrees to pay back your money plus interest at a set time—usually several years down the road. Because the interest rate usually is much higher than bank accounts, bonds are a form of investment.

The amount of interest to be paid depends on the credit rating of that bond. The higher the credit rating, the lower the rate of interest. The lower the credit rating, the higher the rate of interest that will be paid. Of course, the higher interest rates mean there is a greater chance that the company won't have the money to repay the loan when it comes due.

Mutual funds

When you put money into a mutual fund, you are pooling your money with many other investors. The manager of the fund then invests this pooled money in stocks, bonds, and other areas.

There are two main advantages to a mutual fund. First, the fund will be professionally managed. You won't have to pick your own stocks or bonds; someone with more knowledge will do that. Second, your money is divided—or diversified—across many companies. This lowers your risk. The person who originally said, "Don't put all of your eggs in one basket," could have been describing mutual funds.

I THINK I GOT IT NOW

Let's test your knowledge. Fill in these blanks using the information you have just learned about savings and investment choices.

1. When you pool your money with other investors in stocks, bonds, and other investments, you have invested in a ____________________.
2. When you lock up your money for a fixed period of time, usually three months to five years, and a fixed interest rate, you have invested in a ____________________.
3. When you invest in ____________________, you become a part owner of the company and you make money when the company pays dividends or when the stocks increase in value.
4. When you loan your money to a company or government for a set period of time, you have invested in ____________________.
5. If you save your money in a fund that is federally insured and pays a low interest rate, you have put your money in a ____________________.

Answers:
1. Mutual Fund
2. Certificate of Deposit, or CD
3. Stocks
4. Bonds
5. Money Market Fund

CAN'T I JUST SAVE OR INVEST?

It really pays to both save *and* invest. The amount of money placed in savings or investments is called **principal**. With savings, principal is safe and earns a low rate of return. With investments, the principal is at greater risk, but there is also the chance for greater return. That's why most experts say to have some money in both savings and investments.

Usually, you begin by making some savings choices. When you have more money to put away for longer time periods, you can begin to make investment choices.

Congratulations! You are learning about the difference between savings and investments. And now that you know the benefits of compound interest, we are confident that you will save and invest your money early so you can benefit from the time value of money.

Chapter 1, Is There More to Money Than Spending and Saving?,

completed (date) ______________________________

I did all the exercises and answered all the questions in Chapter 1.

By (sign your name)______________________________

Caregiver signature ______________________________

You are over the hurdle and ready for Chapter 2!