WHAT IS SAVINGS AND WHY IS IT IMPORTANT?

Savings is the portion of income not spent on current expenditures. Because a person does not know what will happen in the future, money should be saved to pay for unexpected events or emergencies. An individual's car may breakdown, their dishwasher could begin to leak, or a medical emergency could occur. Without savings, unexpected events can become large financial burdens. Therefore, savings helps an individual or family become financially secure.

Money can also be saved to purchase expensive items that are too costly to buy with monthly income. Buying a new camera, purchasing an automobile, or paying for a vacation can all be accomplished by saving a portion of income.

HOW MUCH MONEY SHOULD BE SAVED?

To be considered financially secure, an individual or household should save at least six months' worth of expenses. For example, a household that has $2,000 per month of expenses should have at least $12,000 in savings ($2,000 multiplied by 6 months). To reach this amount, it is recommended that 10-20% of net income should be saved until the appropriate amount of savings is reached. Net income is the amount of an individual's take-home pay after taxes and other deductions have been taken out of a paycheck.

WHERE CAN MONEY BE SAVED?

Some savers place their money in a jar, coffee can or a piggy bank. For short periods of time and small amounts of money, the piggy bank method may work, but long-term savers should use a safer method. It is wise to store money at a depository institution. A depository institution is a business that offers financial services to people, such as savings and checking accounts. Unlike money stored at home which could be lost to a fire, burglary, or some other type of disaster, money stored at a depository institution is protected from loss.

Depository institutions offer accounts that earn interest, allowing customers to take advantage of the time value of money. The time value of money means money paid out or received in the future is not equivalent to money paid out or received today. Interest is the price of money. When depositing money at a depository institution, an
individual may earn money from interest. The amount of interest earned is determined by calculating a percent of the total amount of money deposited. This percentage rate is known as the interest rate. Savings accounts, money market deposit accounts, and Certificate of Deposits are the most common depository institution accounts that earn interest.

A savings account is an account with a depository institution that holds money not spent on current expenditures. Money can be kept in a savings account until the owner needs to use it for emergencies or to purchase expensive items.

A money market deposit account is a type of account that pays a higher interest rate than a savings account. However, money market deposit accounts usually require more money to open and have limits on the number of times money can be withdrawn from the account every month.

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A Certificate of Deposit (CD) is an account that pays interest on a lump sum of money. However, once money is placed into a CD, it is required to stay there for a specific period of time. If money is withdrawn early, the owner will have to pay a penalty fee. Once the time period is complete, the money and interest earned can be withdrawn. The interest rate money earns in a CD is usually higher than a money market deposit account and increases as the time period a person agrees to keep their money in the account increases and as the amount of money placed in the CD
increases.

When money is saved in one of these accounts, the owner of the money has to do nothing and the value of money automatically increases! The higher the interest rate, the more money is earned. In addition to the interest rate, the amount of money saved and the length of time money is saved affects the time value of money. The larger the amount of money saved, the larger the amount of interest earned will be. The longer money is left in a depository institution account, the longer money will have to earn interest. Table 1 shows how $500.00 saved at 3% for five years increases to a total of $579.64.
Initial amount saved $500.00

Year	Amount of money account is worth
1	$515.00
2	$530.45
3	$546.36
4	$562.75
5	$579.64

HOW TO BEGIN SAVING MONEY

To help a person choose saving over spending money, money should not be viewed as what is remaining after current needs and wants have been satisfied. Pay yourself first is a popular and very effective saving strategy that can help individual's choose saving over spending money. Paying yourself first means to set aside a portion of money (10-20% of net income is recommended) for saving each time a person is paid before using any of the money for spending.

To successfully practice the pay yourself first strategy a person should set personal goals. Setting goals helps a person choose to save rather than spend money. A goal is defined as the end result of something a person intends to acquire, achieve, do, reach, or accomplish. Financial goals are specific objectives to be accomplished through financial planning and include saving money. Setting goals helps an individual identify and focus on items that are most important to them and then make decisions that help obtain those items.

While in the process of setting goals, an individual should consider the trade-offs to those goals. A trade-off is giving up one thing for another. Every decision involves a trade-off. Being more financially secure in the future by saving is a trade-off to spending money in the present. If a person clearly understands what they are giving up in exchange for the benefits of saving money, then their saving goals will become more attainable and realistic. When considering the trade-offs to achieving savings goals, an individual should examine their current spending as well. Spending may have to be adjusted in order to reach a financial goal and practice the pay yourself first strategy.

Explore the value of saving money and learn strategies that help people choose to save money over spend money. Learn the advantages of saving money at a depository institution.

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