

Name: _____ Class: _____

Financial Literacy

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There are many decisions a person needs to make in regards to money. Not only do people need to decide what to do with their money, but they need to know the costs and benefits of these decisions. In this informational text, Jessica McBirney discusses in greater detail the various choices a person can make with their money. As you read, take notes on how you would respond to the options McBirney gives the reader.

- [1] Money is one of the most complicated and controversial things in the world. Some people are very cautious about having and using it, while others try to earn (or even steal) as much of it as possible. Financial systems are extremely complicated, which unfortunately means there are too many people who do not understand how to use their money in the best ways.

In order to understand money and some of the ways you can use it, let's do a thought experiment: a very generous aunt just gave you \$1,000 and said you can use it however you want. What are some of the options you have?



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Banks

Maybe the first idea you had was to put your \$1,000 into a bank. There are two different ways to put money into a bank. The first option is to put money into a checking account. This is the simplest option, because a checking account holds your money and allows you to access it very easily at any time you would like.

The second option is to use a savings account. Money in a savings account is harder to access on demand, but the bank will pay you a small percentage of the total for keeping your money in that account. This is called interest. For example, if you put all \$1,000 in a savings account, and the bank's interest rate is 3%, at the end of the year you will have \$1,030.

- [5] Why does the bank want your money, if they have to pay to hold it for you? Actually, banks are very happy when you store your money with them, because they use the money when you do not. If you put \$1,000 into a savings account, the bank will hold onto a small portion of it, maybe \$100, and give the other \$900 out to other customers as loans.

Loans

A bank gives loans to people who temporarily need more money than they have. For example, you might need some extra money in the form of a loan to buy a house or start a business.

Banks like to give out loans because when someone borrows money, they have to pay that money back along with interest on the money (it's the same idea as the interest you'll receive from your savings account, except this time the customer is paying it).

Remember that \$900 the bank is borrowing from your savings account? If the bank gave that \$900 as a loan to a customer, at a 10% interest rate, then at the end of the year that customer will owe the bank \$990. Now the bank has made a profit from that loan.

Credit

Credit and credit cards are special types of loans. When you use a credit card to buy things, instead of paying for them immediately, each purchase goes onto a big list. At the end of the month, the credit card company adds everything on the list together and sends you a one bill for the total amount of money you spent that month.

- [10] The special feature of credit cards is that you do not have to pay back the entire bill right then. Imagine you spent \$5,000 last month. When you get the bill, you might only have to use your \$1,000 to pay the bill, but you still have all \$5,000 worth of stuff you bought.

This functions as a loan because the credit card company has, in a round-about way, loaned you that leftover \$4,000. As with a loan, you will still have to pay that \$4,000 back eventually, and the credit card company will charge you interest on it. So, in the end, you might owe \$4,500 (plus the \$1,000 you used to pay the minimum part of the original bill).

It is usually not smart to pay off only small portions of your monthly credit card bill. The longer you wait to pay it off, the more money you will eventually owe to the credit card company.

Credit Scores and Banks

A credit score keeps track of how often you are not able to pay back your full credit card bill right away, as well as other data related to your credit usage. If you pay your whole bill on time every single month, you will have a very good credit score. This usually means a number around 700 or higher. But if you frequently pay only the minimum requirement, or if you often pay your bills late, you will have a bad credit score. This is usually a number below 600.

Banks are more likely to give out loans to people with very high credit scores. People with high credit scores will probably be more responsible with the loan and are far more likely to pay the loan back on time and with interest. This is why it is important to spend money wisely and be careful how you use credit cards.

The Stock Market

- [15] Let's go back to your \$1,000. One other option you have is to invest it in the stock market. The stock market is a place where you can buy stocks, or very small percentages, of big companies like Walmart or Facebook. Each stock can cost anywhere from a few dollars to a few hundred dollars. If the company makes money, each stockholder gets to share a small percentage of their profit.

This is how you can earn money on the stock market. Let's say you use your \$1,000 to buy 20 stocks in Facebook, at \$50 per stock. You are taking a gamble – if Facebook does well in the next year, the value of those stocks will go up, but if it does poorly, their value will go down. Fortunately for you, at the end of the year, you discover Facebook's value has increased! Now each stock is worth \$55. This means your total is \$1,100, and you made \$100. But it was still a gamble, because Facebook's value might have decreased. If each stock dropped to \$45, your total would be only \$900, and you could have lost \$100.

So, what do you think you will do with the \$1,000 from your aunt? Now you know you have some options: to put it in a checking account for easy access, or to keep it in a savings account to earn interest. You've learned how the bank could use that money to provide loans to other people. You might even choose to use the money your aunt gave you to invest in the stock market. Yes, there are many options and you could choose from any one of them. Just don't spend it all at once!

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Text-Dependent Questions

Directions: For the following questions, choose the best answer or respond in complete sentences.

1. PART A: Which of the following identifies the central idea of the text?
 - A. People who invest in the stock market will most likely lose money.
 - B. Most financial institutions trick their financially illiterate customers out of money.
 - C. Financial choices can be confusing, but knowledge can help a person make good decisions.
 - D. Understanding how to manage finances is relatively easy, as most of it is common sense.

2. PART B: Which detail from the text best supports the answer to Part A?
 - A. "Financial systems are extremely complicated, which unfortunately means there are too many people who do not understand how to use their money in the best ways." (Paragraph 1)
 - B. "Money in a savings account is harder to access on demand, but the bank will pay you a small percentage of the total for keeping your money in that account." (Paragraph 4)
 - C. "It is usually not smart to pay off only small portions of your monthly credit card bill. The longer you wait to pay it off, the more money you will eventually owe to the credit card company." (Paragraph 12)
 - D. "People with high credit scores will probably be more responsible with the loan and are far more likely to pay the loan back on time and with interest." (Paragraph 14)

3. PART A: Which sentence best describes one aspect of the relationship between banks and their clients?
 - A. Banks often use their clients' money without their knowledge or permission.
 - B. Banks exist only to profit from their clients by charging them unnecessary fees.
 - C. Banks can use clients' money for loans and clients can make money on interest.
 - D. Banks control how much money their clients can withdraw from all of their accounts.

4. PART B: Which quote from the text best supports the answer to Part A?
- A. "a checking account holds your money and allows you to access it very easily at any time you would like." (Paragraph 3)
 - B. "Money in a savings account is harder to access on demand, but the bank will pay you a small percentage of the total for keeping your money in that account." (Paragraph 4)
 - C. "If you put \$1,000 into a savings account, the bank will hold onto a small portion of it, maybe \$100, and give the other \$900 out to other customers as loans." (Paragraph 5)
 - D. "Banks like to give out loans because when someone borrows money, they have to pay that money back along with interest on the money" (Paragraph 7)
5. What is the effect of the author proposing a "thought experiment" at the beginning of the text?

Discussion Questions

Directions: Brainstorm your answers to the following questions in the space provided. Be prepared to share your original ideas in a class discussion.

1. What experiences do you have with the different options available for spending and saving money discussed in the text? How do you think you will manage money in the future?
2. In the context of the text, does money buy happiness? How does saving money versus spending money lead to different types of happiness? What are the benefits and disadvantages of both?
3. In the context of the text, what is the goal of education? In what ways do you think “financial literacy” is a form of education? Should financial literacy be a class in school? What would be a good method for teaching financial literacy?