

ACCOUNTING AND FINANCE

LEVEL – II

Based on November, 2022, Curriculum Version II



MODULE TITLE: Developing and Using a Personal Budget and Savings Plan

Module code: LSA ACF2 M05 1122

Nominal duration: 100 Hours

Prepared by: Ministry of Labor and Skill

November, 2022

Adama, Ethiopia

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Acknowledgment

Ministry of Labor and Skills wish to extend thanks and appreciation to the many representatives of TVT instructors and respective industry experts who donated their time and expertise to the development of this Teaching, Training and Learning Materials (TTLM).

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Acronyms

SMART	Specific, Measurable, Attainable, Realistic, and Timely
ATM	Automated teller machines
FDIC	Federal Deposit Insurance Corporation
TTLM	Teaching, Training and Learning Materials

Introduction to the Module

Budget is very important to improve our live standard. The aim of personal budgets is to put people at the center of their own care and support. A personal budget recognizes an individual's strengths and preferences, and enables them to gain more choice in, and control over, the support they require to live their own lives. Simply Budget is a financial plan for a specified period. Plan your financial future early, and then live your plan. So this manual share concrete ideas and experiences on how you can apply the create budget process to the personal finance area, how you can create your vision of what you want to become, set goals, develop a plan, work on constraints, and then communicate it to help you accomplish your vision. This process is applicable to all areas of your Personal financial Plan. Catching the vision for your life is not simply writing a list of goals you would “like” to accomplish. Rather, it is a process of understanding yourself, **who you really are, your aspirations, desires, values**, and what you want to become and accomplish. Think all these like and encourage yourself.

So, according to that context, this learning module covers the knowledge, skill and attitude relative to **the competence** required to analyze and discuss budgeting as a financial tool, Develop a personal budget, Implement and monitor the personal budget, Discuss the place of saving and investing today, Understand risk as it relates to saving and investing, Develop your own savings plan, Implement your own savings plan.

This module covers the units:

- **Analyze and discuss budgeting as a financial tool**
- **Develop a personal budget**
- **Implement and monitor the personal budget**
- **Discuss the place of saving and investing today**
- **Understand risk as it relates to saving and investing**
- **Develop your own savings plan**
- **Implementing your own savings plan.**

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Learning Objective of the Module

- Understand budgeting as a financial tool
- Perform a personal budget
- Carry out the personal budget
- Identify the place of saving and investing today
- Understand risk as it relates to saving and investing
- Prepare your own savings plan

Module Instruction

For effective use this modules trainees are expected to follow the following module instruction:

1. Read the information written in each unit
2. Accomplish the Self-checks at the end of each unit
3. Perform Operation Sheets which were provided at the end of units

Unit One. Analyzing and discussing budgeting as a financial tool

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- 1.1. Discussing the role of budgeting in the lives of different groups
- 1.2. Explaining the importance of budgeting
- 1.3. Discussing the importance of setting financial goals
- 1.4. Discussing obstacles that prevent financial goals
- 1.5. Analysing types of behaviours and skills

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- understand role and importance of budgeting in the different groups
- Analyze importance of setting financial goals
- Understand obstacles that might prevent financial goals
- Explain types of behaviors and skills

1.1. Discussing the role of budgeting in the lives of different groups

1.1.1. Overview of personal budgeting

Budgeting is a planning and control system. Budget is the system of planning. Planning is determining the activities to be accomplished to achieve goals. According explained in introduction, every person of every age should create, use, and update a personal or family budget. If you don't have one already, this Module help you create one. A budget is simply a plan for how you are going to spend the money that is available to you. To create a budget, you determine your spendable income and allocate it to different categories of expenses. Then you track your actual spending against your budget. It is acceptable to go over in some categories if you are under by the same amount in others. A budget is a living document that is modified as conditions warrant.

Budgets generally include categories for food, housing, utilities, clothing, transportation, medical, recreation, debt reduction, and miscellaneous expenditures. It is often this last budget category, the miscellaneous category, which gets overlooked. Unexpected expenses always come up that don't fit neatly into your budget categories: a car repair, perhaps an engagement ring or even a wedding. In a marriage relationship, it is important that both the husband and the wife have a say in budget creation, and that they help each other live within their means and claim joy. In many marriages, one partner is a saver, and the other partner is a spender. Both play an important role. Early in a marriage, it is a great blessing when the saver can help the spender stay within the budget.

Generally Personal budgeting refers to preparation of a formal plan, which is expressed in financial term and limited to a time horizon. A personal budget allocates future incomes towards living expenses, savings and debt repayment. When income is less than expenses, you have a budget deficit too little cash to provide for your wants or needs. A budget deficit is not sustainable; it is not financially viable. The only choices are to eliminate the deficit by increasing income, or reducing expenses, or borrowing to make up the difference. Borrowing may seem like the easiest and quickest solution, but borrowing also increases

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expenses, because it creates an additional expense: interest. When income for a period is greater than expenses, there is a budget surplus. That situation is sustainable and remains financially viable.

Categories of Household Expenditures

Housing expenses consist of **shelter** (mortgage payments, property taxes, or rent; maintenance and repairs; and insurance), **utilities** (gas, electricity, fuel, cell/telephone, and water), and house furnishings and equipment (furniture, floor coverings, major appliances, and small appliances). Mortgage payments included principal and interest payments. Overall, principal payments constituted 15 percent of overall housing expenses.

Food expenses consist of food and nonalcoholic beverages purchased at grocery, convenience, and specialty stores, including purchases with Food Stamp Program (now the Supplemental Nutrition Assistance Program) benefits; dining at restaurants; and household expenditures on school meals.

Transportation expenses consist of the monthly payments on vehicle loans, down payments, gasoline and motor oil, maintenance and repairs, insurance, and public transportation (including airline fares).

Clothing expenses consist of children's apparel such as diapers, shirts, pants, dresses, and suits; footwear; and clothing services such as dry cleaning, alterations, and repair.

Health care expenses consist of medical and dental services not covered by insurance, prescription drugs and medical supplies not covered by insurance, and health insurance premiums not paid by an employer or other organization. Medical services include those related to physical and mental health.

Child care and education expenses consist of day care tuition and supplies; baby-sitting; and elementary and high school tuition, books, fees, and supplies. Books, fees, and supplies may be for private or public schools.

Miscellaneous expenses consist of personal care items (haircuts, toothbrushes, etc.), entertainment (portable media players, sports equipment, televisions, computers, etc.), and reading materials (non-school books, magazines, etc.).

Personal budget for different groups means:-

Budget can be prepared for different groups. Every person of every age should create, use, and update a personal or family budget. Different groups are;

- Families
- governments
- individuals like:
 - ✓ single
 - ✓ married
 - ✓ elderly
 - ✓ students
 - ✓ tourists, travelers etc are required budgeting for education fees, emergency fund, monies for buying a car or home, finances for starting a family, finances to use during retirement etc.

1.1.2. Role of budgeting in the lives of different groups

Personal budget plan is very role play in your live standard. Budgeting is the process of creating a plan to spend your money. This spending plan is called a budget. Creating this spending plan allows you to determine in advance whether you will have enough money to do the things you need to do or would like to do. Creating and using a budget is something everyone can benefit from and do. Budgeting is a powerful process that can help you develop a financial plan and build financial capability and empowerment. Your success with budgeting may depend on your perspective. Some think budgets are meant to be restrictive, take the fun out of life, and make you feel shameful about spending. Others may view budgets as too time consuming to make or too difficult to follow.

In reality, budgeting is an empowering process. It puts you in control of directing your money towards what you really want in life, including having fun. With this in mind, taking the time to create a realistic budget you can follow will be well worth it. If you develop your own Personal budget, you plan for live (**Vision and Goals**). Budget created what is good in man mind. This application of budget process is critical to your accomplishing all you need to in life. The right type of budgeting plan for you can be determined by various factors:

- Income
- expenses, and
- spending habits

Basically, a budget is a spending plan that maps out the amount of income versus the amount of expenses during a specific period of time. Many bills such as housing costs, utilities, subscriptions, and more are due on a monthly basis so the typical budget is prepared for an entire month.

Preparing a Budget

Establish goals

Before you write out your budget you need to write down your goals. Short term and long term goals are important and will play a part in how you create your budget. Think about the goals you have. Common goals include purchasing a **home** and/or **car**, **earning a degree**, **owning a business**, **writing a book**, **vacationing**, **traveling the world**, and many more. Some of these goals should be saved for (education and travel) while others need to be paid for (home and cars). If you implement your goals into your budget, you maximize the potential of accomplishing them when and how you want. That's really what budgeting is all about; creating a plan to accomplish your **goals, hopes, and dreams**.



Figure1.1. Everything is in your hand

Determine income

A key element to preparing a budget is to do so before you actually receive any income, so before your next paycheck and before the month begins. This is crucial because you are not tempted to spend your earnings before creating a plan for how you really want to spend them. Determine all types of income you will receive such as wages, gifts, refunds, etc. All that money that comes to you should be considered income.

Tithes and gifts

Once you have determined your budgeted income, you can move on to tithes and giving. Tithing is a command brought to us in the Old Testament and mentioned again as a something Christians should do in the New Testament. Deuteronomy 14:22 states: “Be sure to set aside a tenth of all that your fields produce each year.” Again in Proverbs 3:9 it says: “Honor the Lord with your wealth, with the first fruits of all your crops.” While Christians no longer set aside produce

anymore as an offering to the Lord, we set aside the first 10% of our income to give back to the Lord through our local church as a tithe. This is why tithes are recorded just below income on the budget. Additional gifts after tithes such as donations, sponsorships, etc. can be recorded below the tithes.

Determine saving

By including a section to save a portion of your money, you are able to visually and physically allocate funds for the future. Savings can be on a pre-tax basis from your payroll deductions like retirement. It can also be a post-tax basis from your net income by putting it aside for an emergency fund, your next car, your next house, or a vacation. These post-tax savings goals are known and unknown upcoming expenses. Known expenses such as a house down payment are simple to save for as you know how much money will be needed for the expenses. It is crucial to prepare for the unknown through an emergency fund although it is slightly more difficult to plan for emergencies that may occur. An emergency fund is meant to cover unforeseen financial expenses such as medical bills, plumbing problems, a car breakdown, and so forth.

Debt payments

Debt payments include mortgage payments, auto loans, student loans, credit cards, and any other outstanding account balances.

Insurance

After debt payments, you'll list out all of the insurance payments you have for one month. Insurance payments typically include renter's or homeowner's insurance (unless it's added in to the monthly cost), auto insurance, life insurance, and health insurance. There may be more in your life, so if there are be sure to add them to your budget!

Bills

Bills and living expenses can often be the main focus of a budget as they consist of the primary expenses that individuals (young and old) experience. Some financial planners do not separate bills from expenses; however for the purpose of this article they have been separated. The

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distinguished items allow individuals to prioritize their expenses and clearly see what expenses are optional (non-essential) and essential. All bills are essential which basically means they are nonnegotiable. No matter what, these expenses must be paid each month.

- Utilities
- Water
- Electricity
- Telephone

Living expenses

These expenses are purchases you make in relation to your lifestyle. How many times you eat out and what grocery stores you shop at determine the amount of money you spend on food. Same with the type of car you drive and the commute to work also contributes to how much you spend on gasoline in a month. Food and transportation specifically are month essential expenses while the rest shown are optional. This means that other than food and transportation the remaining items could be eliminated from the budget because they are not essential.

Understanding the difference between essential (**non-discretionary**) and nonessential (discretionary) expenses will help you in the event of loss of income when you no longer can afford all the usual items in your budget.

The key concepts of budget are:

- **Vision-** your vision is what you want to become or how you want to live your lives. It is your ultimate destination and what you want to be like.
- **Goals-** Goals constitute your destination or where you want to get to become your vision.
- **Plans-** Plans are your tactical strategies or plans that will allow you to accomplish your goals.
- **Constraints-** These are the conditions or circumstances that are critical for you to accomplish your goals.
- **Accountability-** Finally, accountability is how you let others know what you are trying to accomplish and how you enlist their help in your process.

Activity .1.

1. Did you have Own plan for live? If you say ‘yes’, explain what you will want to be? And your **vision** and **goal**, if you say no, why? **Discuss.**

1.2. Explaining iimportance of budgeting

A budget helps create financial stability. By tracking expenses and following a plan, a budget makes it easier to pay bills on time, build an emergency fund, and save for major expenses such as a car or home. Overall, a budget puts a person on stronger financial footing for both the day to day and the long term. Since budgeting allows you to create a spending plan for your money, it ensures that you will always have enough money for the things you need and the things that are important to you. Following a budget or spending plan will also keep you out of debt or help you work your way out of debt if you are currently in debt. The importance of budgeting cannot be understated. A budget, also known as cash flow, is arguably more important than the actual cash that you have in your bank and investment accounts. Your cash flow is what allows you to pay for everything (or not). Without knowing your cash flow, you could be putting yourself into a bad financial situation and not even know it. You can only get by without knowing your cash flow for so long before you get into financial trouble, so make the time you know the flow of your cash. Budgeting should be something that everyone does, regardless of their financial situation.

Budgeting is a wonderful tool for managing your finances, but many people think it's not for them. Some importance of budgeting are:-

- Helps put you in control.
- Helps you create a visual spending picture.
- Helps you determine how much money you have to spend.
- Helps you decide how you want to spend your money.
- Helps you prevent impulse spending (the decision-making strategy of spontaneity).
- Helps you decide what you can and cannot afford.
- Helps you to keep track of how you spend your money.

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- Helps you create a savings plan.
- Helps you stay out of financial trouble.

In short, importance of budgeting is:-

- Manages your money
- Directs your money flow
- Increase your saving
- Avoid spending money unnecessary
- Achieves your personal goals.

1.3. Importance of setting financial goals

First of all when you want to financial plan, you must set financial goals. Personal financial planning is the process of managing your money to achieve personal economic satisfaction. This planning process allows you to control your financial situation. Every person, family, or household has a unique financial position, and any financial activity therefore must also be carefully planned to meet specific needs and goals.

You should analyze your financial values and goals. This activity involves identifying how you feel about money and why you feel that way. Are your feelings about money based on factual knowledge or on the influence of others? Are your financial priorities based on social pressures, household needs, or desires for luxury items? How economic conditions affect your goals and priorities? Specific financial goals are vital to financial planning. Others can suggest financial goals for you; however, you must decide which goals to pursue. Your financial goals can range from spending all of your current income to developing an extensive savings and investment program for your future financial security. And also think about personal finance when you setting goals. **Personal finance** relates specifically to how you as an individual or part of a household manage your money. Personal finance is the financial management which an individual or a family unit is required to do to obtain, budget, save, and spend monetary resources over time, taking into account various financial risks and future life events.

Personal Finance Activities

- **Obtaining-** Get resources from employment, investments
- **Planning-** Plan spending and saving through budgeting process
- **Saving-** Money for emergencies and short-term goals
- **Borrowing-** Wise borrowing habits; not misusing credit
- **Spending-** Considering consequences; spending < earnings
- **Managing Risk-** Adequate insurance coverage for risks
- **Investing-** Select securities for income and Long Term growth
- **Retirement and Estate Planning-** Financial security in later life.

A personal financial plan is a report that showing an individual's current financial situation, financial needs and future financial activities. Personal financial planning is the process of managing your money to achieve personal economic satisfaction. The seven key areas of personal financial planning are:

- **Financial position planning:** is concerned with managing the personal resources available by examining your net worth (assets-liabilities)
- **Financial cash flow planning :** refers to the aggregating all the expected income sources in a given year, minus all expenses that are expected within the same year.
- **Adequate protection:** is about conducting an analysis to determine how best a household can be protected from unforeseen risks. The risks can be categorized as property, liability, disability, death, health and long term care. Among the risks, there are those that can be self-insured although most of them call for the purchase of an insurance contract.
- **Tax planning:** income tax is typically the expenses that most individuals incur. Tax planning therefore determining the amount that will be paid as tax and the time when the taxes will be paid.

- **Investment and wealth planning:** It is prudent to have regular savings behavior while earmarking various areas of investments. It is prudent to diversify the investments so as to reduce risks.
- **Retirement planning:** this involves understanding the cost of living after retirement, and developing a plan to guard against any income shortfall. .

Principles of personal finance:-

- **Financial literacy:** The essential features of financial literacy are: actual and perceived knowledge, skills for application of that knowledge, financial behavior and attitude and financial experiences. It is important to boost your financial literacy.
- **Always plan:** for, education, savings, expenditures, borrowing, retirement etc. Failing to plan is planning to fail.
- **Time value of money:** money received today is worth more than money received, say after a year from now. This principle allows one to understand how investments grow overtime
- **Understand taxes:** Personal financial decisions are affected by taxes. The principle makes it possible for one to understand how taxes affect the return of an investment.
- **Importance of liquidity:** it is necessary to plan for the unexpected. It means that you must have some liquid money available at any time to cater for the unexpected. 6. Smart spending-avoid wastage and impulse buying
- **Emergency fund:** Protect yourself against major catastrophes e.g. Insurance can protect one against major catastrophes like floods, hurricanes, earthquakes, fires etc.

Goal-setting guidelines

Financial goals are the long-term, short-term and intermediate plans you have for your finances. The best financial goals align with your values and personal goal. Financial goals are savings, investment or spending targets you hope to achieve over a set period of time. The stage of life you're in usually determines what type of goals you wish to achieve. For example, if you're in college, it may be an easy short-term goal like saving for a new pair of shoes or something more challenging like saving for a car. On the other hand, a person with a growing family would have

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a long-term goal of going from renting a home to owning one. Saving for a child’s college education and saving for your own retirement are other popular financial goals.

Goal setting is central to financial decision making. Your financial goals are the basis for planning, implementing, and measuring the progress of your spending, saving, and investing activities.

Make Your goals SMART

Setting goals is a skill that usually improves with experience. According to a popular model, to be truly useful goals must be **Specific, Measurable, Attainable, Realistic, and Timely** (SMART).

- **S- Specific.** Goals should be specific. Answer the questions of who, what, where, when, and why. so you know exactly what your goals are so you can create a plan designed to achieve.
- **M- Measurable.** Goals should be measurable. You must be able to track progress toward your goal. With a specific amount. For example, “To save birr1000, 000 in commercial bank within three years” is more measurable than “saving into a Commercial bank.
- **A – Attainable.** Goals should be achievable. Achievable goals are goals that your attitudes, abilities, skills, and interests can help you accomplish. Is action-oriented. The action provides the basis of the personal financial activities you will undertake. For example, “Reduce current debt balances” will usually mean actions to pay off amounts owed.
- **R- Realistic.** involving goals that are set after considering your life situation and income. For example, it is unrealistic for a full-time student to expect to purchase a new car each year.
- **T- time-based,** indicating a time frame within which the set goals are to be achieved. Setting a time frame helps one to measure the progress made towards the financial goals. Designs of products and work places.

Importance of personal financial plan

- Increases the effectiveness in obtaining, using, and protecting your financial resources throughout lifetime.
- Boost your control of financial affairs by safeguarding against bankruptcy, excessive debt and relying on others for economic security.
- Relieve you from financial uncertainties/worries because one is able to anticipate future incomes and expenses
- They facilitate achievement of individual financial goals.
- Help realizing your personal financial independence.
- They enable your account for your money.
- They improved personal social relationships.

1.4. obstacles that prevent financial goals

Many factors influence daily financial decisions, ranging from age and household size to interest rates and inflation. Three main elements affect financial planning activities:

- life situation
- economic factors, and
- . personal values

Details of factors affecting the financial planning

- **Economic factors** such as inflation, interest rate, loss of income, business cycles and consumer prices affect the ability to implement the plans. Market forces of demand and supply for goods and services usual affect the prices
- **life situation or Personal factors** such as age, income, size of households, marital status, health, career choices, personal consumption patterns, personal beliefs, and ethics and personal values affect the financial behavior .
- **personal value :-** In addition to being defined by your family situation, you are defined by your values the ideas and principles that you consider correct, desirable, and important. Values have a direct influence on such decisions as spending now versus saving for the future.

- **Government policies** e.g. tax policies may be favorable or not to your plans.

1.5. Types of behaviours and skills

Financial literacy Financial literacy as a combination of financial awareness (experiences), knowledge, capability, attitude and behaviors necessary to make sound financial decisions and ultimately achieve individual financial wellbeing. Financial experiences refer to the practices individuals undergo in the credit and loan market as they manage their financial resources. These practical experiences detail the processes undergone in the debt cycle such as obtaining the loan, how to avoid, reduce or repay debt while maintain a good credit rating. Individuals who adhere to responsible debt experiences report lower levels of financial problems. Responsible financial experiences include debt restructuring, seeking financial advice, seeking financial counseling and avoiding multiple loans.

Financial knowledge: A person is regarded as financially knowledgeable if he possesses skills, education and current information on how to manage his financial obligations. Financial knowledge is acquired through education and training. Financial capability refers to the capacity to make financial decisions given a set of financial skills, education and information. Financial capability covers four areas namely:-

- planning how to obtain
- managing obtained money
- making prudent buying decisions and
- Staying informed about financial realities.

Financially capable persons should therefore be able to keep track of their own finances, and plan their future financial commitment by personal financial planning, budgeting and budgetary control.

Financial behaviors and attitudes involve certain traits, habits and biases usually influenced by a range of personality, psychological and environmental factors. Example of good financial behavior is self-control, self-confidence and self-independence. A self-control problem refers to a situation where an individual is not able to balance between short-term and

long-term preferences. It also influences saving choices and usually leads to impulse buying and excess borrowing. Individual with higher level of self-confidence score higher in financial literacy. On the other hand, self-confidence leads people to set and pursue ambitious goals meaning it is an antecedent of motivation. Peer independence occurs when individual fail to mimic others. Peer influence refers to how social interactions affect key financial decisions of compatriots in the social group.

Self-check 1

Part-I: Choose the correct answer

- According to personal Finance Activities one of the following is odd?
A. Obtaining B. Planning C. Saving D. none
- One the following are key concepts of budget but not one
A. Goal B. vision C. plan D. none
- One of the following is elements affect financial planning activities:
A. life situation B. economic factors, C. personal values D. all

Part II Matching

Instruction: select the correct answer for the given column.

A

B

- | | | |
|---------------------------|----------------------------|----------------|
| 1. Goals | Importance budget | A. Vision and |
| 2. Household Expenditures | B. Increase your saving | |
| 3. individual | You plan for live | C. families or |
| 4. | Budget for different group | D. Food |
| 5. | Economic factors | E. Inflation |

Test III: short Answer writing

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Directions: Answer all the questions listed below.

1. Explain the criteria of setting budget goal.
2. Discuss about obstacles that prevent financial goals

Part IV writing

1. Define the Budgets and budget plan.
2. Explaining and list the importance of budgeting
3. Explain categories of personal spending.

Unit Two. Developing a personal budget

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Estimating Income and expenses
- Developing spreadsheet
- Identifying fixed and variable expenses
- Subtracting total expenses from the total income
- Exploring reason for a deficit budget
- Investigating ways to reduce expenses or increase income
- Exploring and identifying allocation of surplus fund

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Estimate all income and expenses for a six month period (semi-annual)
- Develop budget spreadsheet and records
- Use budget spreadsheet for all income, fixed expenses and variable expenses
- Calculate total expenses and subtract from the total income to determine a surplus or deficit
- Understand reasons for a deficit budget and ways to reduce expenses or increase income
- Perform allocation of surplus funds towards saving and meet financial goals

2.1. Estimating income and expenses

2.1.1. Develop personal budget format

A **budget** is a summary of estimated income (money in) and expenses (money out) for a specific period of time (such as a week, month or year). Budgeting is an important money management tool that helps you to understand how you earn and spend your money. Anyone can use a budget because it allows you to tailor it to fit your financial realities. A good budget has a detailed list of your various sources of income and your expenses. Expenses should be separated and categorized as necessary household expenses (food, shelter, and loan payments), **optional** household expenses (soda or extra clothes), and savings.

In the ideal budget, your income is greater than or equal to your expenses. If your budget shows that your expenses are greater than your income, you must correct this difference. You can make this correction by finding additional sources of income such as seeking additional work, taking out a loan, decreasing expenses, or using a bit of your savings. Creating a budget helps you to make these decisions in advance before you spend any money or realize that you have already overspent. In the budgeting process, you can choose your most important expenses, such as key goals and necessary expenditures.

A budget is only a plan for how you want to spend your money. How you actually spend your money based on your day-to-day realities may be different. Since a budget is for a specific period, it is essential to carefully record and track how you actually spend your money and what you earn during that period. Comparing how much you planned to spend and earn with the amount you actually spent and earned can help you to make adjustments to the next budget.

Understanding income and expenses

Income is the money that flows into your household. It is the money earned from selling goods, providing services, or other income generating activities. Money and goods received as gifts, remittances and loan disbursements count as income. To estimate your total income, add up the total value of all the money you expect to receive from all of your different income sources in a given period.

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An expense is the money you spend. One of the first steps of money management is to understand how you spend your money. A good way to start is to record each of your expenses over a short period of time, such as a week. With this knowledge, you can prepare a realistic budget. Planning your expenses for a specific period of time has many benefits. It can help you plan how to cover major expenses and achieve your financial goals. Having a greater goal in mind helps you reduce the temptation to buy things that are lesser spending priorities.

Steps in Budgeting

- Set financial goals
- Estimate your income
- Record what you spend
- Prepare one month Budget

A. Set Financial Goals

Make sure your goals are **SMART**

Specific- Clearly state what you want to do

Measurable- Measure by time and/or money needed

Attainable- Make sure your goal is realistic and possible

Relevant- Make sure goals fit your needs

Time related- Set a definite target day (**day/month/ year**)

Identify and write them down

- Long term
- Short term

B. Estimate Your Income

Make a list of each income stream that you receive on a regular basis each month. The key is to only include that income you get every month. Include both monthly wages earned from your job(s) as well as monthly supplemental income (i.e. child support, disability, etc.) Mark down the date these are received, calculate the monthly income total. **Building a budget takes a little time.** But it's absolutely vital to financial health.

C. Record What You Spend

Track your expenses for a month to start a budget. What did you buy? What bills did you pay? Basically, where did your money go? Then categorize your spending into groups such as clothing, food, music downloads, auto, etc. Think of other areas in which you might spend money on a regular basis. Don't forget to include some money for **savings**.

Identify your income. Only include regular sources of income such as paychecks and allowances. If you get paid monthly or semi-monthly, it is easy to calculate your monthly income. If you get paid weekly or biweekly, multiply your weekly income by 52 or 26 respectively to get your annual salary. Then divide by 12 to get your monthly income. Now that you have your expenses and income quantified, it's time to examine and fine-tune your budget.

Subtract expenses from income. This is to determine how much money you have left over at the end of the month. If you have more income than expenses, that's good. If you spend more money than you earn, you're going to have to decrease your expenses or increase your income. Keep in mind it's easier to decrease your expenses.



Figure 2.1 Income – Expenses

Timing is important. If you get paid once a month, be sure to budget money to last the whole month. If you get paid twice a month, but you have several large expenses at the beginning of the

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month, make sure you save some of your money from the end of the month to help with the next month's bill

D. Prepare one month budget

List all income and expenses required

Income
Salary Income, salary, wages from all sources
Investment income ,Dividends, interest, capital gains
Overtime
Rent Income
Other benefits etc
Total income (A)
Expenses
Health care expenses
Food expenses
Transportation expenses
Clothing expenses
Housing expenses
Child care and education expenses
Miscellaneous expenses
Total expenses(B)
Amount planned to save(A-B)

Example of One month budget

Income	
Net income	8000
Other income	6540
Total income(A)	<u>14540</u>
Expenses	
Health care expenses	1200
Food expenses	7200
Transportation expenses	650
Clothing expenses	800
Housing expenses	2000
Total expenses(B)	<u>11850</u>
Amount planned to save(A-B)	<u>2690</u>

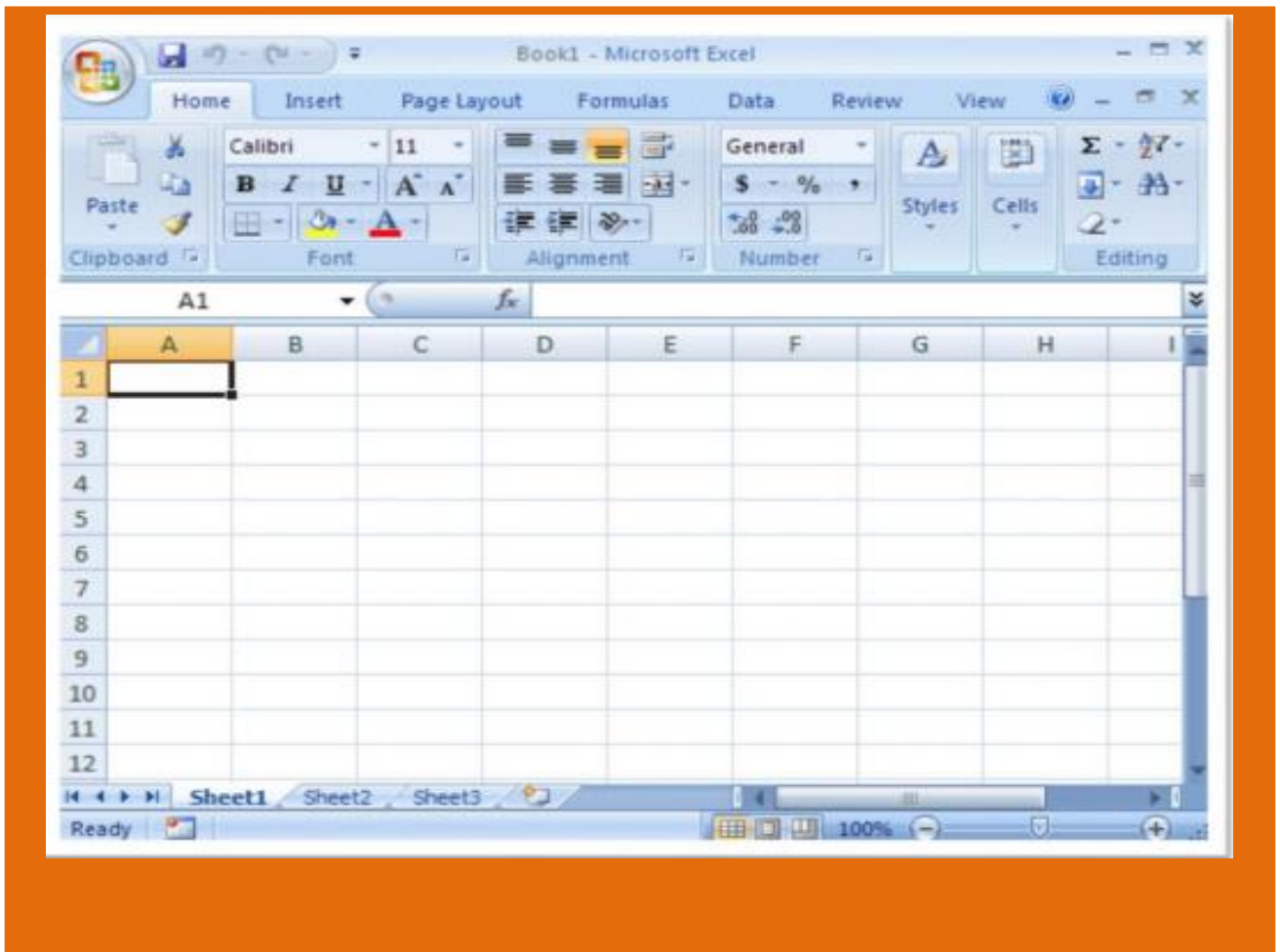
2.2. Develop spreadsheet

A spreadsheet is a large sheet having data and information arranged in rows and columns. As you know, Excel is one of the most widely used spreadsheet applications. It is a part of Microsoft Office suite. Spreadsheet is quite useful in entering, editing, analyzing and storing data. Arithmetic operations with numerical data such as addition, subtraction, multiplication and division can be done using Excel. You can sort numbers/ characters according to some given criteria (like ascending, descending etc.) and use simple financial, mathematical and statistical formulas. A personal budget spreadsheet offers an individual a way to determine the state of his finances and help him or her plan spending over the course of a period of usually a month or a year

Create a Budget Spreadsheet

Budget spreadsheets can help an individual track his spending and plan his future expenditure. That is why creating one is of greatest importance. So create a budget spreadsheet as follow:-

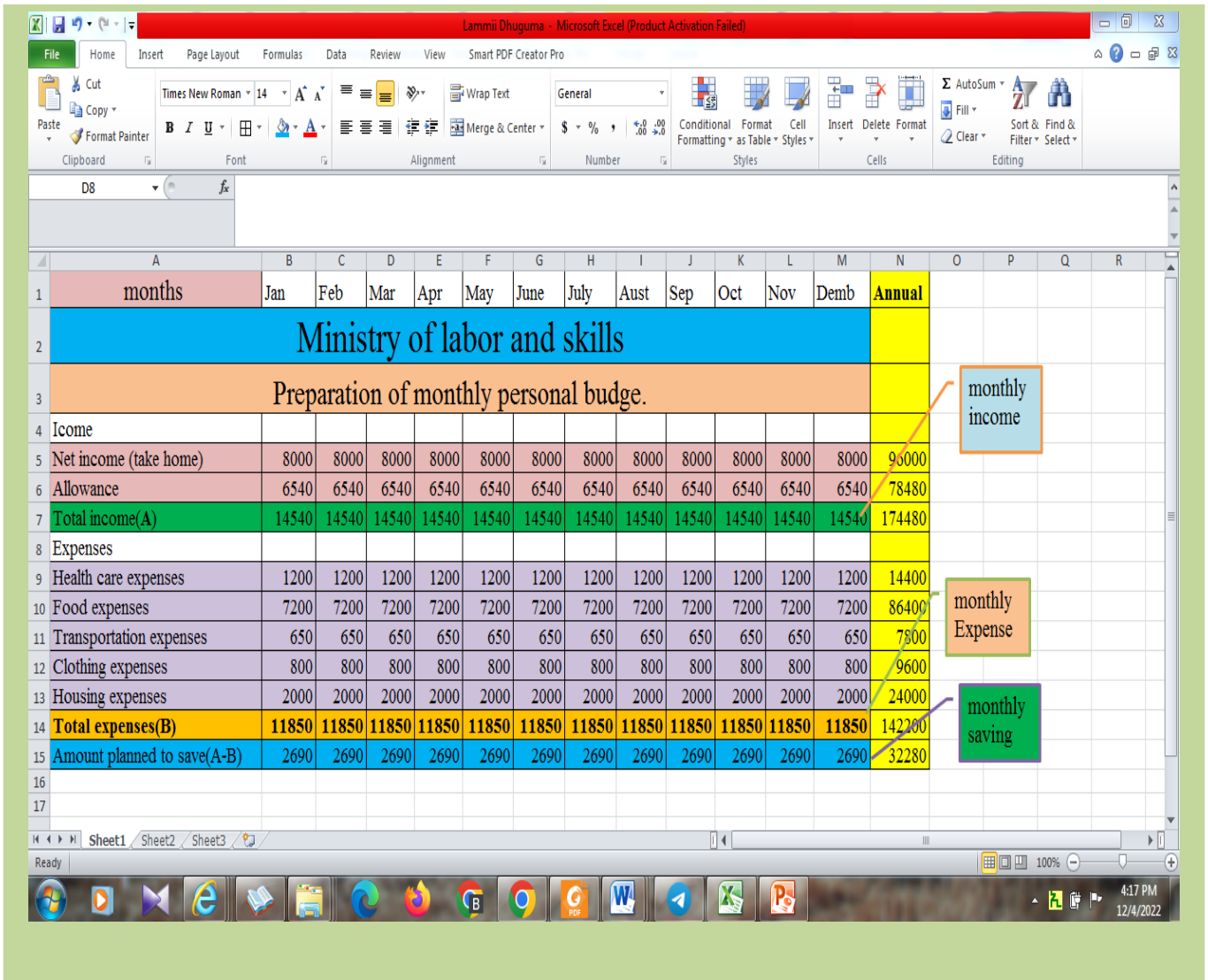
1. Firstly, making one requires a desktop or laptop computer with MS Excel already installed.
2. Run the Excel program on the computer and open a new file or spreadsheet.
3. Put in the necessary details on the spreadsheet in order for it to calculate the figures involved in the file. Basic budget spreadsheets are often labeled with Income and Expenditure, which will be totaled by the file itself.
4. Indicate the months that are included in the duration of the budget. If it applies for half a year, write January to June on every cell along one row.
5. Then, type Income on one cell a row below the different months of the year. Under the category should be the types of income that you expect to receive each month.
6. After the types of income, skip one cell and then write Expenditure, under which are the different types of expenses like shopping, groceries, bills, and others.
7. After they've been put on the spreadsheet, you can begin writing down the calculation or formula which Excel will use at a later date once you need to see the total.
8. Choose the part of the spreadsheet where you can write the total.
9. Click the Menu button and click **Autosum**. Highlight the cells that you need to include in the **Autosum** by clicking on them and dragging them.
10. Step 9 should be repeated with the Expenditure.



Formulas: In spreadsheets, formulas process data automatically. It takes data from the specified area of the spreadsheet as input then processes that data, and then displays the output into the new area of the spreadsheet according to where the formula is written. In Excel, we can use formulas simply by typing “=Formula Name(Arguments)” to use predefined Excel formulas. When you write the first few characters of any formula, Excel displays a drop-down menu of formulas that match that character sequence.

The basic components of spreadsheets are:

- **Title Bar:** The title bar displays the name of the spreadsheet and application.
- **Toolbar:** It displays all the options or commands available in Excel for use.
- **Name Box:** It displays the address of the current or active cell.
- **Formula Bar:** It is used to display the data entered by us in the active cell. Also, this bar is used to apply formulas to the data of the spreadsheet.



months	Jan	Feb	Mar	Apr	May	June	July	Aust	Sep	Oct	Nov	Demb	Annual
Ministry of labor and skills													
Preparation of monthly personal budge.													
Income													
Net income (take home)	8000	8000	8000	8000	8000	8000	8000	8000	8000	8000	8000	8000	93000
Allowance	6540	6540	6540	6540	6540	6540	6540	6540	6540	6540	6540	6540	78480
Total income(A)	14540	14540	14540	14540	14540	14540	14540	14540	14540	14540	14540	14540	174480
Expenses													
Health care expenses	1200	1200	1200	1200	1200	1200	1200	1200	1200	1200	1200	1200	14400
Food expenses	7200	7200	7200	7200	7200	7200	7200	7200	7200	7200	7200	7200	86400
Transportation expenses	650	650	650	650	650	650	650	650	650	650	650	650	7800
Clothing expenses	800	800	800	800	800	800	800	800	800	800	800	800	9600
Housing expenses	2000	2000	2000	2000	2000	2000	2000	2000	2000	2000	2000	2000	24000
Total expenses(B)	11850	11850	11850	11850	11850	11850	11850	11850	11850	11850	11850	11850	142200
Amount planned to save(A-B)	2690	2690	2690	2690	2690	2690	2690	2690	2690	2690	2690	2690	32280

Column Headings: the spreadsheet is named by letters or a combination of letters.

Row Headings: the spreadsheet is named by a number.

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Cell: In a spreadsheet, everything like a numeric value, functions, expressions, etc., is recorded in the cell.

2.3. Identifying fixed and variable expenses

- **Fixed expenses:** Expenses, like bills, that must be paid each month and generally cost the same amount. Some fixed expenses, like a utility bill, may also be variable because the amount changes each month depending on usage. Look at your list of bills and note which ones are the same every month or you expect will be the same for several months.
- **Variable expenses:** Expenses that change in amount from month to month.

Write down all of your current expenses and be sure to make an honest and realistic appraisal of your spending. You can track your expenditure for a month or more for an accurate assessment of how much you spend. It is useful to categorize your spending, such as fixed expenses, variable expenses and discretionary expenses, as listed below.

Fixed expenses:-

- Mortgage payment/rent
- Vehicle loan or lease
- Other loans
- Insurance
- Education
- Savings plan if possible and etc any other expenses with fixed monthly/weekly payments

Variable expenses

- Groceries
- Utilities
- Phone
- Maintenance
- Clothing
- Transport

- Medical

Discretionary expenses are any expense not directly essential to day to day living, such as:

- Entertainment
- Clothing
- Furniture
- Holidays
- Sport
- ‘Pocket money’ look the following:-

Example Monthly Family Living Budget

Income	Monthly	Annual	
Salary (take home)	birr 3,000	birr 36,000	Income
Allowance	1,500	18,000	
Total income	4,500	54,000	
Fixed Expenses			
Car payment	677	8,124	Fixed expenses
Child care	475	5,700	
House payment	1,043	12,516	
Retirement account	400	4,800	
Insurance	200	2,400	
Total fixed expenses(A)	2,795	33,540	
Variable Expenses			
Auto fuel	225	2,700	Variable expenses
Auto repair	75	900	
Clothing	70	840	
Association	275	3,300	
Dining out	75	900	
Groceries	325	3,900	
Medical	50	600	
Telephone	105	1,260	
Utilities	125	1,500	
Christmas (save)	125	1,500	
Discretionary expenses	255	3,060	
Total variable expenses	1,705	20,460	
Total Expenses (B)	4,500	54,000	
Net Surplus/deficit(A-B)	birr <u>0</u>	birr <u>0</u> no deficit, no surplus is Balanced	

2.4. Subtracting total expenses from the total income

For example, if you budget birr 120 for your monthly power bill and you only need to pay birr 80 during a mild spring month, then send the power company birr 80 and put the remaining birr 40 in an interest-bearing savings account. That birr 40 may not earn much interest, but it will earn some. When you get a higher bill in the summer or winter, or other period of time you'll have the money in your savings account to cover the difference. Look the above example Monthly Family Living Budget.

Example:-1

Total income of month (4500) – Total expenses of month (4500) = 0

Income	Monthly	Annual
Total income (A)	<u>4,500</u>	<u>54,000</u>
Total fixed expenses	2,795	33,540
Total variable expenses	1,705	20,460
Total Expenses (B)	<u>4,500</u>	<u>54,000</u>
Surplus/deficit (A-B)	<u>0</u>	<u>0 balanced</u>

2.5. Exploring reason for a deficit budget

Surplus occurs when you have a positive cash flow. Deficit occurs when you have a negative cash flow. **Discretionary** income is the money you have left over after paying for essentials. Discretionary income is used to evaluate the strength of a person's income. Represents the money you can spend on wants. Generally when revenue greater than the expenses the difference is called **surplus**, and when expenses greater than the income the difference is called **deficit**

Example

Total income-----16400
Total expense-----18400
Deficit Budget ----- (2000)

Budget surplus

A budget surplus occurs when income exceeds expenditures. The term often refers to "**savings**" rather than a "budget surplus."

Example Monthly Family Living Budget

Income	Monthly	Annual
Salary (take home)	birr 3,000	birr 36,000
Allowance	1,500	18,000
Total income	4,500	54,000
Fixed Expenses		
Car payment	677	8,124
Child care	475	5,700
House payment	1,043	12,516
Retirement account	400	4,800
Insurance	200	2,400
Total fixed expenses(A)	2,795	33,540
Variable Expenses		
Auto fuel	225	2,700
Auto repair	75	900
Clothing	70	840
Association	275	3,300
Dining out	75	900
Groceries	325	3,900
Medical	50	600
Telephone	105	1,260
Utilities	125	1,500
Christmas (save)	125	1,500
Total variable expenses	1,705	20,460
Total Expenses (B)	4,245	50,940
Net Surplus/deficit(A-B)	bir <u>255</u>	birr <u>3055</u>

Surplus/
personal
saving

A **budget surplus** might be used to make a purchase, pay off debt or save for the future

Budget deficit

When expenditures exceed income, the outcome is a budget deficit.

Example Monthly Family Living Budget		
Income	Monthly	Annual
Salary (take home)	birr 3,000	birr 36,000
Total income	3000	36,000
Fixed Expenses		
Car payment	677	8,124
Child care	475	5,700
House payment	1,043	12,516
Retirement account	400	4,800
Insurance	200	2,400
Total fixed expenses(A)	2,795	33,540
Variable Expenses		
Auto fuel	225	2,700
Auto repair	75	900
Clothing	70	840
Association	275	3,300
Dining out	75	900
Groceries	325	3,900
Medical	50	600
Telephone	105	1,260
Utilities	125	1,500
Christmas (save)	125	1,500
Discretionary expenses	255	3,060
Total variable expenses	1,705	20,460
Total Expenses (B)	4,500	54,000
Deficit(A-B)	<u>birr (1500)</u>	<u>birr(18000)</u>

Deficit

A budget deficit occurs when expenditures/expenses exceed revenue. The term "budget deficit" is most commonly used to refer to government spending rather than business or individual spending. When referring to accrued federal government deficits, the term "national debt" is also used. The opposite of a budget deficit is a **budget surplus**, and when total expenditure equals

total Income, the budget is considered **balanced**. When individual or businesses experience budget deficits, they have to borrow money in order to avoid bankruptcy/ decrease discretionary expenses. Individuals use budget deficits to measure the overall health of their finance. While Deficits are always a warning signal for individual/business, it is important to understand to find solution why occurs deficit.

Example Assume that Obbo Oliqa has the following budgeted

Task	Jan 1 budget	Jan. 30 actual	Deference
Income	12400 birr	1600 birr	0
Rent expense	500	400	0
Utility expense	300	350	(50)
Educational payment	200	250	(50)
Gift & contribution	100	90	10
Saving	200	200	0
House operation	300	280	20

Total shortage = 100

Total excess = 30

In general Obbo Oliqa personal budget performance is shortage by 70 birr

Saving –shortage =200-70 =130 decline the saving amount to **130**

2.6. Investigate ways to reduce expenses or increase income

Financial independence is achieved by reducing spending, earning more, saving more, and avoiding negative cash flow. A spending plan is a tool to assist one in tracking and monitoring income and expenses and avoiding negative cash flow.

Reduce Spending

- Doing comparison shopping
- Using coupons
- Avoiding impulse purchases
- Buying items “on sale”
- Carpooling, walking, or riding a bike
- Eating at home
- Eliminating/reducing impulse purchases – vending machines, convenience stores, etc.
- Shopping at thrift stores
- Wearing hand-me-down clothes etc.

Increase Income

- After school/weekend job
- Additional chores around the house
- Yard work
- Babysitting
- Summer job
- House sitting
- Provide a service

2.7. Exploring and identifying allocation of surplus fund

A budget surplus occurs when income exceeds expenditures. Running a budget surplus means additional money. It is allocated for the following purpose.

- It is important to pay off debts
- Reinvest
- Save for future
- A large surplus also reduces the need for borrowing.
- By your wants

Self-check 2

Part-I: Choose the correct answer

- Which of the following not fixed expense?
A. Insurance B. Other loans C. Mortgage payment/rent D. Utilities
- One the following are basic components of spreadsheets except one
A. Title Bar B. toolbar C Name Box D. mouse
- Which of the following is health expense?
A. Tele phone B. medicine C. food D. mortgage
- One of the following is elements utilities expense?
A. Electric usage B. food expense C. discretionary expense D. all

Part II Matching

Instruction: select the correct answer for the given column.

A

B

- | | | |
|---------------------------|-----------------------------|------------|
| 1. | Expenses exceed revenue | A. surplus |
| 2. Revenue exceed expense | B. deficit | |
| 3. Increase Income | C. Holidays | |
| 4. Decrease expense | D. Eating at home | |
| 5. Discretionary | E. After school/weekend job | |

Test III: short Answer writing

Directions: Answer all the questions listed below.

1. Explain fixed expense and variable expenses
2. Discuss about surplus and deficit

Part IV writing

4. Explaining the step of develop budget
5. Explain all categories of personal income and expense.

Operation sheet 2.1: performance budget

- **Operation title: Develop personal budget**
- **Purpose:** To prepare personal budget
- **Instruction:** Using information prepare personal budget.

Task budget for October 1

- Income 12000
- Rent expense700
- Utility expense200
- Saving 1700
- House expense 8200
- Loan payment 1200

Actual income and expense for October 30

Activity October actual

- Income 12000
- Rent expense 700
- Utility expense 200
- Saving
- House operation 840
- Loan payment 1200

Unit three. Implement and monitor the personal budget

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Following the budget according to plan
- Recording actual expenses and income of the budget
- Comparing the actual and budgeted expense and income
- Modifying the budget
- Discussing Handy hints
- Conducting ongoing review of the budget

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Perform budget plan for a period of time
- Calculate and compare actual expenses and income for the period of budget plan
- Review handy hint of personal budget
- Carry out Ongoing review of the budget and ensure updates

3.1. Following the budget according to plan

Moving on to reviewing

Compare what you budgeted for yourself at the start of the month with how much you actually spent at the end of the month for each category. Did over/under your budget? Next, why did over or under? Did you have control of why? Last is to revise your budget in the areas where it went wrong. If you over spent and it was something you could control. Determine if you should allocate more or less to certain items in your budget and keep adapting it until it works. Review the budget at least monthly.

- On necessary adjustments for the situation.
- Consider the following in your review if :

Income sources

Income cover expenses

Where and when spending money

Saving regularly

Anything has affected your income, spending, and saving you are achieving your personal and financial goals.

3.2. Recording and comparing actual expenses and income of the budget

Example **implementation budget performance**

Income	Budget plan	Actual	deference
Net income	8000	8000	0
Other income	6540	6540	0
Total income(A)	<u>14540</u>	<u>14540</u>	<u>0</u>
Expenses			
Health care expenses	1200	1500	(300)
Food expenses	7200	7500	(300)

Transportation expenses	650	740	(90)
Clothing expenses	800	750	50
Housing expenses	2000	2000	0
Total expenses(B)	<u>11850</u>	<u>12490</u>	<u>(640)</u>
Amount planned to save(A-B)	<u>2690</u>	<u>2050</u>	<u>(640)</u>

Activity - The family budget

The total income of the family for the month of January is birr 15400 during the month of January, and the family has the following budget allocation and actual expenditures for the month of January. The budget allocation is 15%, 30%, 10%, 10%, 5%, 10%, 5% respectively, then prepare budget performance report for the month of January

Description	Budget allocation for January	Actual expenditure
Housing expense	-----	2300
Food expense	----	4580
Transportation expense	1540	1530
Clothing	-----	1540
medical care	770	800
Education	1540	1540
Gift contribution	770	700
Saving	-----	-----

3.3. Modifying the budget

Review Spending .To fix your finances, you need to get a handle on your outlay first categorize spending so you can make adjustments. Many people find that just by looking at aggregate figures for discretionary expenses, they are spurred to change their patterns and reduce excessive spending. Then Eliminate Unnecessary Expenses. Once you've got a sense of where the money goes, it's time to tighten up. All cutbacks should start with items you wouldn't miss or habits you should change anyway like reducing your fresh food purchases if you find ingredients spoiling before you can eat them. Or preparing meals at home more instead of going to restaurants or getting takeout. Some expenses you shouldn't drop but might be able to adjust could include reducing your auto insurance rate by switching carriers. Monitor your progress for a few months. You can do this by writing everything you spend in a notebook. How you track your money isn't as important as how much you are tracking. Focus on ensuring that every cent is accounted for by dividing your expenses into categories. Adjust the spending as needed after each month.

NEEDS

- Housing Cost
- Groceries
- Utilities
- Healthcare Costs
- Transportation

SAVINGS
Emergency Fund
Essential Expenses
Retirement Savings

DEBT
Student Loans
Credit Card
Other

Discretionary spending
Entertainment
Vacations
Technology

3.4. Discussing Handy hints

Handy hints is how to avoid getting into financial difficulties and, ways to cut back on spending or change negative spending habits. Restructure your expenses set an amount of money that is reasonable for you to spend each week/or each months after all your fixed and variable expenses have all been accounted for. This requires that you realistically examine the expenses that you can and cannot alter. Handy hint is very important for you to identify the expenses essential or not. Your values are those ideas and beliefs that really matter to you. Your values will determine

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what you will do with your money. Asking yourself, “How do I use my money now?” will tell you a lot about your money values. People use money two ways:-

- They buy things they need or want now
- They save for things they may **need** or **want** later. It’s not about how much money you have, but how you use your money. It is all about the choices you make.

Difference between Needs and Wants

- Here’s a good rule about money: It is very important to make your needs come first. That’s why it is important to know the difference between your needs and your wants. Before you start planning how to use your money, let’s be clear about the difference between needs and wants.
- A **need** is something you must have to survive, like a place to live and enough food to eat.
- A **want** is something you might like to have, but you don’t have to have it right away. You can save to have it later.

A. Spending Plan

Show you where to cut spending, provide methods for keeping good records of spending, allow you to spend money without feeling guilty, create a way to measure your progress, improve communication with other people, etc.

Assess Needs

Make a realistic list of needs and wants

Needs

Food
Clothing
Housing
Transportation
Child Care
Insurance
Medicines

Wants

Lots of Money
Cell Phone
Big TV
New Car
Designer Jeans
Vacations

Most people earn less income than what they need to purchase everything they need or want. to help you decide which expenses to prioritize and include in your budget, label each expense as a need or a want. It may be helpful to draw pictures of your expenses and separate them. After you have separated your expenses, it will be easier to decide what to cut from your budget based on your expected income. You may choose to add in savings towards one of your financial goals. You can review your expenses to see which ones are most important to have now and those that can be purchased at a later time.



Figure 3.1. Needs and Wants

3.5. Conducting ongoing review of the budget

Budget review means a meeting hold by the parties to review and discuss the draft Annual Budget. “Brand” means brand name provided by operator according to star rating. Reviewing your budget is the process of assessing, adjusting and fine-tuning the amount of money you have allocated to the various budgeting categories. This small, important action gives the insight into your financial habits, and allows you to find areas for improvement. So, if they are spending a little more money than you originally planned in one area, and a little less in another, you can tweak your budget to better align with your spending habits.

Reviewing Budget Important

Reviewing the budget helps you to better manage your spending habits, increase your savings, and make progress toward your long-term financial goals. It’s an important component of proper money management, and a key element of personal finance .Think about it, if you were to create a budget once and never review it, how would the know if the drifting off-track in regard to the financial dreams? Additionally, how would find areas for improvement in your spending? Taking the time to look back and assess the budget will help you see beyond the day-to-day life, and improve the future financial decisions

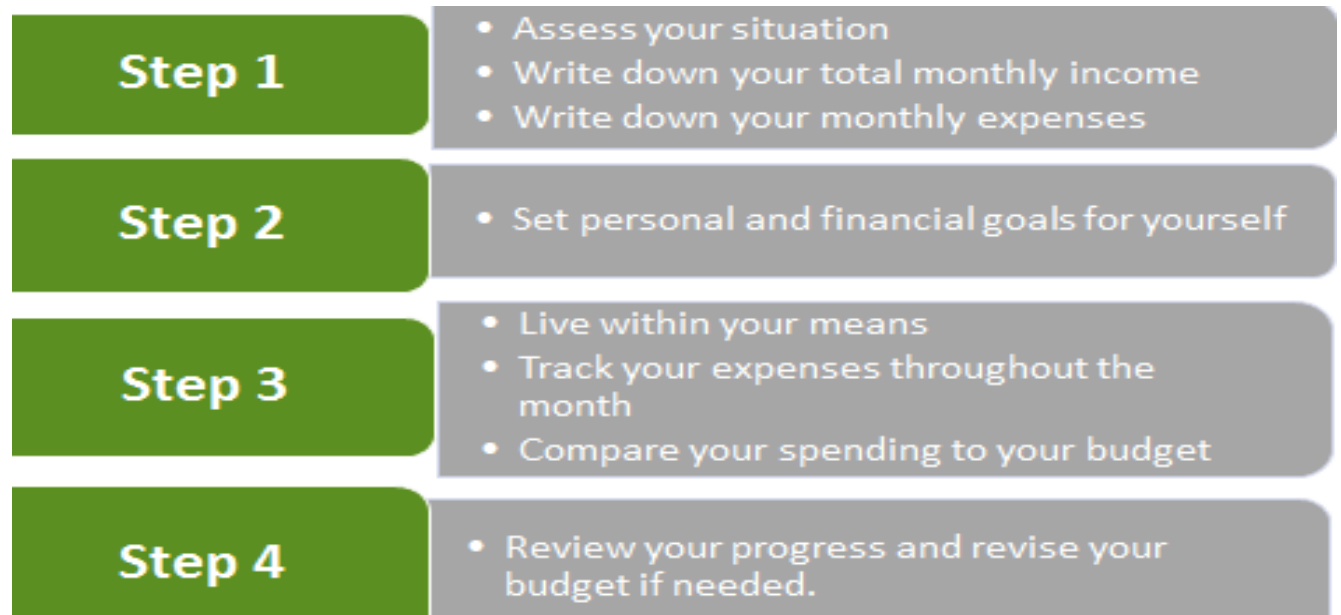
Reviewing Budget vs. Tracking Expenses

Before we get too much further into this post, I want to clarify something: reviewing your budget is not the same thing as tracking and keeping up with the budget. In fact, there is a very big difference. Reviewing the budget is the act of analyzing how accurate and effective the budget has been all while looking for areas to improve the budgeting process. In other words, reviewing the budget is the chance to assess what’s working, what’s not working, and how can you improve the budget. That’s why you can get away with reviewing your budget once a month.

Meanwhile, tracking the expenses (i.e. keeping up with the budget) is something should do on a daily basis. After all, if you only track the expenses once a month, there’s no way to adjust the spending habits in time to stay within the monthly budget. Think of it like this:

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reviewing the budget is how stay on track to achieve the long-term financial goals.
Whereas, tracking the expenses is how you stay on track to live within the monthly budget.
Look the following diagram about reviewing and tracking the expenses.



In order to stay on track with your budget, continuously update your incurred expenses throughout the month. There a many different tools and apps designed to track your spending as well.

Self-check 3

Part I: short Answer writing

Directions: Answer all the questions listed below.

1. Discuss about need assessment
2. Explain Needs and wants
3. Discussing Handy hints

Operation sheet 3.1: Budget performance

Operation title: preparation of budget

- **Purpose:** To prepare performance budget
- **Instruction:** Using the information prepare performance budget.

The family budget

The total income of the family for the month of January is birr 14200 during the month of January, and the family has the following budget allocation and actual expenditures for the month of January. The budget allocation is 15%, 30%, 10%, 10%, 5%, 10%, 5% respectively, then prepare budget performance report for the month of January

Description	Budget allocation for January	Actual expenditure
Housing expense	-----	2300
Food expense	-----	4180
Transportation expense	-----	1230
Clothing	-----	1040
medical care	-----	800
Education	-----	1540
Gift contribution	-----	700
Saving	-----	-----

Unit Four Discuss the place of saving and investing today

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Discussing the impact of high cost of living
- Discussing increasing levels of consumer debt in Ethiopia
- Discussing different attitudes to savings and investment

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Understand the impact of high cost of living
- Understand levels of consumer debt in Ethiopia
- Explain importance of setting financial goals and developing a saving and investment plan
- Understand different attitudes to savings and investment of individual's own spending habits

4.1. Discussing impact of high cost of living

What's the Difference Between Inflation and Cost of Living?

People often use the phrases “**cost of living**” and “**inflation**” as if they were synonymous. They are not the same, although closely related. Inflation is the big picture: As the cost of goods and services rises, the buying power of the dollar falls. The inflation rate is often measured by the Consumer Price Index(CPI).

Cost of living, on the other hand, is a more focused picture. This number averages the cost of an accepted standard of living that includes food, housing, transportation, taxes and healthcare. Cost of living is frequently used to compare life in different locations around the country.

When the Going Gets Expensive

It's easy for most people to feel the effects of cost of living increases in their daily life. But rising prices housing the lower and middle classes especially hard. Higher food, gasoline and utility costs mean less money remains once these necessities are paid for, leaving little for savings or discretionary spending. To compensate for the rise in prices, consumers tend to buy less, switch to less expensive substitutes or drive farther to find bargains. High costs of living exert greatest impact on persons, mainly retired persons, with fixed incomes composed of savings bank interest, life insurance annuities, pensions, or social security benefits. Families of workers whose wages are low also bear a heavy burden during times of inflation.

cost of living, monetary cost of maintaining a particular standard of living, usually measured by calculating the average cost of a number of specific goods and services required by a particular group. The goods and services used as indexes may be the minimum necessary to preserve health or may be what is considered average for a given income group, depending on the purposes of the index. Measurement of the cost of a minimum standard of living is essential in determining relief payments, social insurance benefits, family allowances, tax exemptions, and minimum wages. Measurements of change in the cost of living are important in wage negotiations. It is difficult, however, to make precise comparisons over time, because consumer tastes and the

availability of products change. Increase household expenses (food, school fees, medicine, housing, weddings) etc

Consumer Prices as above mentioned inflation is a rise in the general level of prices. In times of inflation, the buying power of the birr decreases. For example, if prices increased 5 percent during the last year, items that cost birr100 one year ago would now cost birr 105. This means it now takes more money to buy the same amount of goods and services. The main cause of inflation is an increase in demand without a comparable increase in supply. For example, if people have more money to spend because of pay increases or borrowing but the same amounts of goods and services are available, the increased demand can bid up prices for those goods and services. Inflation is most harmful to people living on fixed incomes. Due to inflation, retired people and others whose incomes do not change are able to afford smaller amounts of goods and services. Inflation can also adversely affect lenders of money. Unless an adequate interest rate is charged, amounts repaid by borrowers in times of inflation have less buying power than the money they borrowed. If you pay 10 percent interest on a loan and the inflation rate is 12 percent, the dollars you pay the lender have lost buying power. For this reason, interest rates rise in periods of high inflation.

4.2. Discussing increasing levels of consumer debt in Ethiopia

There are many types of consumer debt in Ethiopia.

May refer to:

- credit card debt
- mobile telephone debt
- mortgages on residential and investment properties
- personal loans to purchase:
 - Motor vehicles
 - Travel
 - Domestic white goods
 - Student loans the Higher Education.

For these purposes the following services are provided banks.

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Checking Accounts

A checking account is a service that gives customers a way to pay bills by check, and to deposit money. Checking accounts don't often pay **interest**, or if they do, it is less than you can earn on a savings account. A minimum balance is sometimes required. Some banks or credit unions charge a monthly fee for checking accounts. Often banks and credit unions offer debit cards that are linked to your checking account.

Savings Accounts

A savings account is a secure place to keep your money for future use. Some people use them to save up for a vacation or to make an expensive purchase. Savings accounts normally pay you a small amount of **interest**. **Interest** is money that you can earn on top of the money you already have in your account.

Debit Cards

A debit card is a plastic card that is connected to your credit union or bank account. When you make purchases using this card, money is immediately taken from your checking or savings account to cover these costs. Debit cards can also be used for the withdrawal of cash. Often you can withdraw cash along with making your purchase.

ATMs (Automated Teller Machines)

Almost every bank has Automated Teller Machines (ATMs) that allow you to skip the teller window and conduct your basic banking tasks at the machine. Your bank will issue a card for use at its ATMs. This card may also serve as a debit card if you give your permission.

Credit Cards

A credit card allows you to purchase items now and pay for them later. Credit cards are an example of revolving credit. When you get a credit card, it will have a limit, also known as a "line of credit." Your first credit card may have a limit. Here are some important things to remember about using a credit card: Every month you get a credit card bill for all the purchases you made that month. On the credit card bill there will be a due date this is the date when your

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payment must be received by the credit card company. The credit card company does not require you to pay your entire balance at the end of each month. You can pay the minimum monthly payment. If you only pay part of the bill, the credit card company will start charging you interest on the amount that you didn't pay. This interest can add up, and what you purchased can end up costing you twice as much.

Credit cards are essentially open lines of credit. Credit cards can be either

1. The single most destructive financial instrument in the history of the world, or
2. A tool to help us reach our personal and family goals. It depends on us! If we use them to borrow money and get further into debt, they are destructive. If we use them to achieve our personal and family goals, they can be helpful.

There are five main benefits for using credit cards:

1. **Emergencies:** Credit cards can be useful when you don't have cash on hand and need to pay for something immediately, such as an auto repair or an insurance co-payment.
2. **Reservations:** Credit cards can be used to guarantee hotel rooms, rental cars, and other rental items. This is an important use, especially if you travel.
3. **Convenience:** With a credit card, you can buy things over the phone or on the Internet. Credit cards make purchasing things very easy. They also provide you with a record of everything you spend, an important bookkeeping benefit.
4. **Cash flow and timing:** If something is on sale, and you know you have the cash coming in a week, you can actually buy the item before you pay for it. In this way, you can take advantage of sales (but remember, you do not save money by spending).
5. **Free services:** Often, credit cards offer rewards, such as extended warranties, travel insurance, airplane miles, gasoline rebates, and cash rebates all of which can reduce the overall cost of some items. While there are benefits to using credit cards, **there are drawbacks as well.** Credit cards must be used wisely to avoid problems. The following is a list of some of the problems associated with using credit cards:

Increased spending: People don't take as much time to think about how much they're spending when they use a credit card. Research has shown that, on average, people spend 30 percent more with a credit card than they do with cash.

Losing track of spending: It's easy to lose track of what you spend with your credit card. It requires discipline to track the charges you make.

The difference between debit and credit cards

Both debit and credit cards allow you to make purchases and cash withdrawals, but there are a few key distinctions. The main difference between debit and credit cards comes down to how each payment method works. When you make a purchase with your debit card, the purchase amount is immediately withdrawn from your checking account. Credit cards work a little differently; instead of immediately withdrawing funds from your checking account, you borrow money from your credit card company whenever you make a purchase.

With debit cards, you don't need to worry about receiving a monthly bill, since your purchases are automatically taken out of your bank account. However, when you use a credit card, you will receive a monthly statement outlining your credit card balance. You have the option to pay the minimum amount, pay your balance in full, or pay anything between the minimum and full amount. But, you'll accrue interest if you carry a balance month to month. If you pay your balance on time and in full, you avoid interest and late fees.

4.3. Discussing different attitudes to savings and investment

Gross domestic savings in Ethiopia are affected by age dependency ratio, real exchange rate, real interest rate, real gross domestic product, foreign capital inflow and money supply both in the short and long run. Elasticity of exchange rate with respect to domestic savings is high and significant in the long run. The level of savings in underdeveloped countries is very small mainly because their level of national income or per capital income is very low. As a result much of the income is consumed and little is left for investment purposes. New investors today choose from a wide selection of investment options through financial institutions and online investment firms. Whether you prefer to make your investment decisions on your own or with the help of a professional, there are several factors to consider when selecting options for your portfolio.

Think about each factor carefully to ensure you make the investment choices that best suit your needs and plans.

Saving

Saving is the portion of income not spent on current expenditures. In other words, it is the money set aside for future use and not spent immediately. Why should we save money? Saving can be used to accomplish objectives in the short-term such as buying a mobile phone, or in the longer run such as continuing to study, or else buying a car or a house. Saving money can also help us cover unexpected expenses, such as an illness, replace an appliance that cannot be repaired or make an emergency trip.

In addition, savings can be invested and, as a result, you get a profit on the money you have set aside. That is to say, not only will you have the funds available to spend later, but you will also earn money in the process. Saving money is a healthy habit that is built on a day-by-day basis. You should start today to get in a lot of practice in saving until it becomes a habit.

Quick summary of factors that influence saving levels

- **Interest rates** – higher interest rates make saving more attractive.
- Rising income enables higher savings. People on very low incomes cannot afford the luxury of saving
- **Economic growth** – high growth and high consumer confidence encourage relatively higher spending and a fall in the savings ratio.
- **The age of individuals** – People in their 40s and 50s tend to save for retirement. Old people run savings down.
- **Cultural trends** – some cultures have a stronger ‘saving culture’ – others pursue higher spending and borrowing.
- **Wealth** – Rising house prices increase household wealth and diminish the need to save in other forms.
- **Inflation** – high inflation may discourage cash saving, but encourage the purchase of fixed assets.

Self-check 4

Part I: short Answer writing

Directions: Answer all the questions listed below.

1. Explain factors that influence saving levels
2. Main benefits for using credit cards
3. Impact of high cost of living

Unit Five Understand risk as it relates to saving and investing

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Explain the concept of risk versus return
- Determine risk profile of an individual's
- Discuss the impact of inflation

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Understand concept of risk and risk versus return
- Determine an individual's risk profile is based on current and
- Identify the impact of inflation on the earnings power of money

5.1. Explaining the concept of risk versus return

To maximize share price, the financial manager must learn to assess two key determinants: risk and return. Each financial decision presents certain risk and return characteristics, and the unique combination of these characteristics has an impact on share price. Risk can be viewed as it is related either to a single asset or to a **portfolio** (a collection, or group, of assets.). In the most basic sense, **risk** is the chance of financial loss. Assets having greater chances of loss are viewed as more risky than those with lesser chances of loss. Some risks directly affect both financial managers and shareholders.

Interest Rates In simple terms, interest rates represent the cost of money. Like everything else, money has a price. The forces of supply and demand influence interest rates. When consumer saving and investing increase the supply of money, interest rates tend to decrease. However, as consumer, business, government, and foreign borrowing increase the demand for money, interest rates tend to rise. Interest rates affect your financial planning. The earnings you receive as a saver or an investor reflect current interest rates as well as a risk premium based on such factors as the length of time your funds will be used by others, expected inflation, and the extent of uncertainty about getting your money back. Risk is also a factor in the interest rate you pay as a borrower. People with poor credit ratings pay a higher interest rate than people with good credit ratings. Interest rates influence many financial decisions. The relationship between risk and return is a fundamental investment concept. The concept states that an increased probability for return is highly correlated with the increase in the level of risk taken. The return is expressed as a percentage and refers to the gains or losses made from an investment, whereas the risk element is associated with the volatility of that return. In theory, an investor could expect higher return on investment only if willing to accept a higher level of risk.

Risk cannot be completely eliminated; it can be managed by holding a diversified portfolio of varying, low correlated asset classes. Investors should be aware that the right mix in the portfolio depends on the individual's risk tolerance level as well as end-goals from the investment. The lower risk assets that usually offer lower but more predictable rate of return include: money

market instruments and fixed income securities. On the other hand, equities, commodities, and derivative securities are considered a higher risk and can offer the potential for higher returns.

Types of investment risk

Market risk

The risk of investments declining in value because of economic developments or other events that affect the entire market. The main types of market risk are equity risk, interest rate risk and currency risk.

- **Equity risk** – applies to an investment in shares. The market price of shares varies all the time depending on demand and supply. Equity risk is the risk of loss because of a drop in the market price of shares.
- **Interest rate risk** – applies to debt investments such as bonds. It is the risk of losing money because of a change in the interest rate. For example, if the interest rate goes up, the market value of bonds will drop.
- **Currency risk** – applies when you own foreign investments. It is the risk of losing money because of a movement in the exchange rate.

Liquidity risk

The risk of being unable to sell your investment at fair price and get your money out when you want to. To sell the investment, may need to accept a lower price. In some cases, such as exempt market investments, it may not be possible to sell the investment at all.

Credit risk

The risk that the government entity or company that issued the bond will run into financial difficulties and won't be able to pay the interest or repay the principal at maturity. Credit risk applies to debt investments such as bonds. You can evaluate credit risk by looking at the credit rating of the bond. For example, long-term Canadian government bonds have a credit rating, which indicates the lowest possible credit risk.

Reinvestment risk

The risk of loss from reinvesting principal or income at a lower interest rate. Suppose you buy a bond paying 5%. Reinvestment risk will affect you if interest rates drop and you have to reinvest the regular interest payments at 4%. Reinvestment risk will also apply if the bond matures and you have to reinvest the principal at less than 5%. Reinvestment risk will not apply if you intend to spend the regular interest payments or the principal at maturity.

Inflation risk

The risk of a loss in the purchasing power because the value of your investments does not keep up with inflation. Inflation erodes the purchasing power of money over time – the same amount of money will buy fewer goods and services. Inflation risk is particularly relevant if you own cash or debt investments like bonds. Shares offer some protection against inflation because most companies can increase the prices they charge to their customers. Share prices should therefore rise in line with inflation. Real estate also offers some protection because landlords can increase rents over time.

Horizon risk

The risk that the investment horizon may be shortened because of an unforeseen event, for example, the loss of your job. This may force you to sell investments that you were expecting to hold for the long term. If you must sell at a time when the markets are down, you may lose money.

5.2. Determining risk profile of an individual's

A risk profile is an evaluation of an individual's willingness and ability to take risks. It can also refer to the threats to which an organization is exposed. A risk profile is important for determining a proper investment asset allocation for a portfolio. Organizations use a risk profile as a way to mitigate potential risks and threats.

- A risk profile is an evaluation of an individual's willingness and ability to take risks.
- A risk profile is important for determining a proper investment asset allocation for a portfolio.
- Organizations use a risk profile as a way to mitigate potential risks and threats.

Understanding Risk Profile

A risk profile identifies the acceptable level of risk an individual is prepared and able to accept. A corporation's risk profile attempts to determine how a willingness to take on risk (or an aversion to risk) will affect an overall decision-making strategy. The risk profile for an individual should determine that person's willingness and ability to take on risk. Risk in this sense refers to portfolio risk. Risk can be thought of as the trade-off between risk and return, which is to say the tradeoff between earning a higher return and having a lower chance of losing money in a portfolio.

Influences risk profile

Risk profile is something we mention a lot when looking at investments and other key financial decisions. But what has an impact on your risk profile?

Investing naturally comes with some level of risk and values will rise and fall over time. However, the amount of volatility experienced varies hugely. Typically, the greater the level of risk and volatility you take on, the higher the potential returns, but there is a greater chance that values will fall. For some, the potential returns of a higher risk profile will outweigh the drawbacks, whilst others will prefer the relative stability of lower risk investments, even if potential returns are reduced.

It's important to keep in mind that all investments involve some risk. But you also need to look at the long-term picture where volatility is considered. Over the years, stock markets have experienced significant dips, which can be a cause for concern for investors. However, historically, markets have recovered to deliver returns over the long term.

There are five key factors to consider when weighing up the risk profile:

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1. Goals

The first area to think about is what you're investing for. Having a clear goal in mind, allows you to build an investment portfolio that suits you. Investing for is likely to have a significant impact on how you feel about risk. Let's say you're investing to pay for a child's education, security may be a priority for you and investments with a relatively low risk may be more attractive because of this.

2. Investment time frame

This one links directly to what the goals are; when do you plan to access your initial investment and the returns it's hopefully generated. As a general rule of thumb, you shouldn't invest if your time frame is less than five years. This gives you an opportunity to ride out dips in the market and recover from potential downturns. In turn, if the time frame is longer in a better position to take on more risk when you take a long-term view. Investing for retirement is a good example of when a long time frame may mean a higher risk profile is appropriate. When first start saving for retirement, it's likely to be a milestone that's decades away. As a result, short-term volatility should have little impact when you focus on the end goal.

3. Other assets

Financial decisions shouldn't be made in isolation. They should look at your overall financial plan and the other assets you have. This will influence your risk profile too. For example, if hold a significant amount in cash and other low-risk assets, you may decide to take a higher risk with new investments. It's important to keep in mind here that not all your investments should be the same in terms of risk. Diversifying and holding a range of investment assets, with various risk profiles, can help smooth out market volatility and limit potential losses.

4. Capacity for loss

No one wants to think about losing money when they invest. However, it's an important consideration to make. If your investments were to perform poorly and decrease in value, how would this impact your lifestyle. Shouldn't invest capital that you can't afford to lose. However,

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there's more to it than that. If your investments were to fall, would it devastate your future plans. Or would it simply mean that some small adjustments would need to be made to ensure your lifestyle was sustainable over the long term.

5. Overall attitude to risk

Whilst the above four factors are influential, your overall feelings about risk are too. You should feel comfortable with all the financial decisions you make, including the level of risk taken when investing. It's natural to worry about potential losses when investing and if you think you're being too conservative, taking some time to understand how investment markets operate over the long term can help. On the flip side, an aggressive approach to investing isn't always appropriate even if you're comfortable with it. Working with a financial adviser can help you reconcile your feelings on investment risk with your financial position.

5.3. Discussing the impact of inflation

Inflation affects all aspects of the economy, from consumer spending, business investment and employment rates to government programs, tax policies, and interest rates. Understanding inflation is crucial to investing because inflation can reduce the value of investment returns. **Inflation**

Inflation is a sustained rise in overall price levels. Moderate inflation is associated with economic growth, while high inflation can signal an overheated economy. As an economy grows, businesses and consumers spend more money on goods and services. In the growth stage of an economic cycle, demand typically outstrips the supply of goods, and producers can raise their prices. As a result, the rate of inflation increases. If economic growth accelerates very rapidly, demand grows even faster and producers raise prices continually. An upward price spiral, sometimes called “runaway inflation” or “hyperinflation,” can result. In general, when economic growth begins to slow, demand eases and the supply of goods increases relative to demand. At this point, the rate of inflation usually drops. Such a period of falling inflation is known as disinflation.

Inflation is the rate of change in prices. Rising inflation means you have to pay more for the same goods and services. This can help you in the form of income inflation or asset inflation, such as in housing or stocks, if you own the assets before prices rise, but if your income doesn't keep pace

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with inflation, the buying power declines. Over time, inflation increases your cost of living. If the inflation rate is high enough, it hurts the economy.

Inflation is defined as sustained increase in the general price level in the economy over a period of time. It has overwhelmingly more negative effects for decision making in the economy and reduces purchasing power. However, **one positive effect is that it prevents deflation.** The effect depends on the type of inflation. For example, walking inflation is 3% to 10% per year. Creeping inflation is milder than walking inflation while running inflation implies a more aggressive rise in prices that could be a prelude. Rising prices may be an indication of an economy growing very fast. People buy more than they need to avoid tomorrow's higher prices fuels demand for goods and services. Suppliers can't keep up. More importantly, neither can wages. As a result, everyday goods and services are priced out of most people's reach.

- Inflation raises prices, lowering your purchasing power.
- Inflation also lowers the values of pensions, savings, and treasury notes.
- Assets such as real estate and collectibles usually keep up with inflation.
- Variable interest rates on loans increase during inflation.

Inflation occurs when there is a sustained increase in the general price level. Traditionally high inflation rates are considered to be damaging to an economy. High inflation creates uncertainty and can wipe away the value of savings. Some economists even argue we should target a higher inflation rate during periods of economic stagnation

Self-check 5

Part I: short Answer writing

Directions: Answer all the questions listed below.

1. Explain types of investment risk
2. Explain the risk and return

Unit six . Develop your own savings plan

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Identifying and quantifying personal savings goals
- Developing personal budget
- Investigating financial product options

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Identify personal savings goals
- Develop a personal budget to contribute towards savings goals
- Investigate and select the range of financial product options available to maximize earnings on savings

6.1. Identifying and quantifying personal savings goals

Understanding a Savings Plan

A savings plan is a method for amassing money in order to reach specific financial goals. It enumerates the goals in question and the steps needed to reach them. Such goals you want to save and invest for:-

- Emergency savings
- Vacation plans
- Wedding arrangements
- Buying a home
- Home repairs or improvements
- Purchasing a vehicle
- College planning
- Retirement savings



Make your own list and then think about which goals are the most important to you. List your most important goals first. The types of financial goals you include in a savings plan depend on your individual financial situation.

Types of financial goals

Two factors commonly influence your financial aspirations for the future. The first is the time frame in which you would like to achieve your goals. The second is the type of financial need that drives your goals.

Timing of goals What would you like to do tomorrow? Believe it or not, that question involves goal setting, which may be viewed in three time frames.

- **Short-term goals**, such as saving for a vacation or paying off small debts, will be achieved within the next year.
- **Intermediate goals** have a time frame from one to five years.
- **Long-term goals** involve financial plans that are more than five years off, such as retirement, money for children's college education, or the purchase of a home.

Develop Your Financial Goals

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Once you have evaluated your current financial situation, you are ready to move forward in the financial planning process. The second step is developing your financial goals. Setting goals will give you a direction for your plan and a destination toward which you want to head. When creating financial goals, you want to consider obvious objectives such as monthly savings or retirement investments. As you develop your financial goals, recall the first tip from Chapter One which discussed setting your goals. Your goals should be **SMART**, that is specific, measurable, attainable, realistic, and time-based. You should also develop short-term, intermediate, and long-term goals. Developing each of these types of goals allow you to achieve successes early in the plan while also keeping your eye toward the future. Short-term or intermediate goals may also serve as stepping stones to reach long-term goals.

If you want to save birr 24000 within six months to start min business in the seventh month, you set goal.

Look the following set specific, measurable, Attainable, realistic, and timely financial goals

Saving goal	specific	measurable,	Attainable	realistic,	Timely
24000	2000	Monthly 2000	Started mini business	Six months	Monthly and in seventh month

6.2. Developing personal budget

Use the following guidelines for personal Budget

Housing & Utilities	30%	Monthly budget		
Food & Household	20%	Total monthly income		10000
Clothing & Personal	10%	Housing & Utilities	30%	3000
Transportation	10%	Food & Household	20%	2000
Saving & Investing	10%	Clothing & Personal	10%	1000
Miscellaneous	20%	Transportation	10%	1000
		Saving & Investing	20%	2000
		% Miscellaneous	10%	1000

6.3. Investigating financial product options

Financial products are investments and securities that are created to provide buyers and sellers with a long term or short term financial gain. Financial products enable risks to be spread, and liquidity to circulate around an economy.

Financial "products" or "**instruments**" are contracts that can be negotiated on capital markets. There are several ways to classify such products. The approach taken in this website is to focus on the technical characteristics of such instruments. However, we also present an alternative classification based on market segment which more closely reflects economic realities.

Options are financial derivatives that give buyers the right, but not the obligation, to buy or sell an underlying asset at an agreed-upon price and date. Call options and put options form the basis for a wide range of option strategies designed for hedging, income, or speculation.

Securities

Securities cover all direct financing instruments of companies, banks, states or public entities. A security represents a share of a medium or short-term (Medium term note, commercial paper) claim or long term claim (bonds), or a share in the capital of a company (equities or shares). For the issuer of the security, it is a financing instrument and for the buyer an investment instrument. Securities are negotiable instruments, in other words they can change hand after they have been issued on what is called the secondary market, provided of course that a counter party exists for the exchange. In this section we deal with related subjects such as securitization and corporate actions.

Self-check 6

Part I: short Answer writing

Directions: Answer all the questions listed below.

3. Explain financial product options
4. Discuss the purpose of saving
5. Discuss financial products (instrument)

Operation sheet 6.1: saving plan and setting goal

- **Operation title:** Preparing six months your own saving budget
- **Purpose:** To evaluate personal budget preparation.
- **Instruction:** Using the following information prepare your own budget
 - a. Quantifying personal savings goals
 - b. Show the steps of personal budget
 - c. Identify fixed expenses and variable expenses
 - d. Use budget spreadsheet

Unit Seven: Implement your own savings plan

This learning guide is developed to provide you the necessary information regarding the following content coverage and topics:

- Identifying requirements to open an account
- opening relevant savings accounts or other investigated financial products
- Adjusting savings goal

This guide will also assist you to attain the learning outcomes stated in the cover page.

Specifically, upon completion of this learning guide, you will be able to:

- Understand requirements to open an account and provide evidence of personal identity
- Investigate relevant financial products, savings accounts and implement savings plan a short period of time
- Adjust unattainable goal and realize savings goal

7.1. Identifying requirements to open an account

Bank

Opening an account is a fairly simple process, but you need to make sure you bring the right documentation with you. Checking accounts are deposit accounts that allow you to store your cash, make withdrawals and transfers, write checks, and pay your bills.

Your bank or financial institution will also provide you with a debit card so you can do your banking at automated teller machines (ATM). If you want to do routine financial transactions, you can choose from a variety of checking account options. Once you choose a bank and fill out some paperwork, you can leave with a functioning account. But the process can get a little more complicated because you usually have to provide documentation to prove your identity. It can get frustrating and delay your ability to use the account if you don't provide the right paperwork.

- Checking accounts generally come with very few eligibility requirements.
- When you open your account, make sure you have a government-issued ID to prove your identity.
- You'll also need your Social Security number or individual taxpayer identification number, along with something that has your address on it, such as a utility.

Ethiopian national/foreigners of Ethiopian origin residing abroad can open the account in person & by post in his/her home.

- Application forms properly filled and signed by the applicant and specimen signature.
- For Ethiopians or foreign nationals of Ethiopian origin individuals, valid passport and/or identification card.

Therefore documents required to open current account: -

- Trade license

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- Tin (tax identification number)
- Memorandum of association
- Minute of meeting of board of director
- Held to discuss opening account
- Initial amount of deposit
- Resident ID and Passport (for Ethiopian national living abroad)

7.2. Open relevant savings accounts or other investigated financial products

Banks

A bank is also a place where you can deposit your money to keep it safe. Banks are interested in earning a profit from customers so you may find that the fees with a bank are higher. Banks typically have multiple branches across a large region. **Checking accounts** is a service that gives customers a way to pay bills by check, and to deposit money. Checking accounts don't often pay interest, or if they do, it is less than you can earn on a savings account.

Savings account is an interest-bearing deposit account held at a bank or other financial institution. Though these accounts typically pay a modest interest rate, their safety and reliability make them a great option for parking cash you want available for short-term needs. Because savings accounts pay interest while keep your funds easily accessible, they're a good option for emergency or short-term cash. In exchange for the ease and liquidity that savings accounts offer, you'll earn a lower rate than that paid by more restrictive savings instruments and investments.

Savings accounts have some limitations on how often you can withdraw funds, but generally offer exceptional flexibility that's ideal for building an emergency fund, saving for a short-term goal like buying a car or going on vacation, or simply sweeping surplus cash you don't need in your checking account so it can earn more interest.

How Savings Accounts Work

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Savings and other deposit accounts are important sources of funds that financial institutions use for loans. For that reason, you can find savings accounts at virtually every bank or credit union, whether they are traditional brick and mortar institutions or operate exclusively online. In addition, you can find savings accounts at some investment and brokerage firms.

Savings account interest rates vary. With the exception of promotions promising a fixed rate until a certain date, banks and credit unions might change their rates at any time. Typically, the more competitive the rate, the more likely it is to fluctuate. Changes in the federal funds rate can trigger institutions to adjust their deposit rates. Some institutions offer high-yield savings accounts, which may be worth investigating.

Savings Account

Some savings accounts require a minimum balance in order to avoid monthly fees or earn the highest published rate, while others have no balance requirement. Know the rules of your particular account to ensure you avoid diluting your earnings with fees. Money can be transferred in or out of your savings account online, at a branch or ATM, by electronic transfer, or direct deposit. Transfers can usually be arranged by phone, as well.

Some banks limit withdrawals to six per month, after the Federal Reserve set that limit only to withdraw it in April, 2020. Exceed six withdrawals, and a bank might impose a fee, close your account, or convert it to a checking account. The amount that can be withdrawn is limited only to how much is in the account.

Savings Account Advantages

Savings accounts offer you a place to put your money that is separate from your everyday banking needs, allowing you to stash money for a rainy day or earmark funds to achieve a big savings goal. What's more, the bank's security measures, along with federal protection against bank failures provided by the Federal Deposit Insurance Corporation (FDIC), will keep your money safer than it would be under your mattress or in your sock drawer.

Beyond keeping your funds safe, savings accounts also earn interest, so it pays to keep any unneeded funds in a savings account instead of accumulating cash in your checking account, where it will likely earn little or nothing. At the same time, your access to funds in a savings account will remain extremely liquid, unlike certificates of deposit, which impose a hefty penalty if you withdraw your funds too soon. Holding a savings account at the same institution as your primary checking account can offer several convenience and efficiency benefits. Since transfers between accounts at the same institution are usually instantaneous, deposits or withdrawals to your savings account from your checking account will take effect right away. This makes it easy to transfer excess cash from your checking account and have it immediately earn interest or transfer money the other way if you need to cover a large checking transaction.

Many institutions allow you to open more than one savings account, which can be handy if you want to keep track of your savings progress on multiple goals. For instance, you could have one savings account to save for a big trip while a separate one holds surplus cash from your checking account.

Savings Account Disadvantages

The trade-off for a savings account's easy access and reliable safety is that it won't pay as much as other savings instruments. For instance, you can earn a higher return with certificates of deposit or Treasury bills, or by investing in stocks and bonds if your time horizon is long enough. As a result, savings accounts present an opportunity cost if used for long-term savings. Also, while the liquidity of a savings account is one of its key benefits, it can also be a downside, as the ready availability of funds may tempt you to spend what you've saved. In contrast, it is much more difficult to cash in a bond, withdraw funds from a retirement account, or sell a stock than it is to take money out of your savings account, especially if that account is linked to your checking account.

Savings accounts are also a poor choice for funds you need to access frequently. Because rules previously restricted withdrawal transactions to six times per month—whether those were

transfers or outright withdrawals at a branch or ATM—a savings account was not always an appropriate vehicle for these funds. The lifting of these restrictions has made the funds more accessible

7.3. Adjusting savings goal

Setting specific savings goals will help you to begin saving money. When you are just putting money into the bank on a regular basis, it can be easier to withdraw it for various reasons. You can easily overspend and use some of the money you had earmarked for savings. For these reasons, it is important to save for a specific target or goal. You may be working toward several objectives at once, or you may be focused on one specific goal that you want to meet.

Choose a Specific Savings Goal

You need to determine what you are saving money for. Your savings goal may be for a down payment on your home. You may be saving for a dream vacation or to pay for your next car. You may be saving for retirement or for an emergency fund. You may be saving for all of these reasons.

- Choose a specific savings goal- First, define your goal. Whether it's a vacation, a college education for your kids, a down payment on a house or retirement, decide what you're working toward rather than choosing a nebulous number, or a vague idea of "saving more." "Have the emotional conversation with yourself about your money and what you hope it accomplishes."
- Set a savings deadline- Next, set a timeline for accomplishing your goal. Some goals, like buying a car next year, might be shorter term. Other goals, like reaching your retirement number, might take longer and require more ongoing planning. "Setting yourself up for success means a plan and a schedule. Figure out your monthly or weekly contributions to reach your goals."
- Create a different account for each. Setting aside different financial accounts for each goal, especially since it's likely that you're saving for more than one goal at the same time. "Saving for multiple goals can make things tricky. Break down each savings goal

into an account, whether it's for a car, house, vacation or anything else. In some cases, you might have to prioritize some goals over others. Think critically about where your money needs to go first and work from there.

- Track your goals- Keep track of your progress so that you can see where you stand and celebrate your progress. As you see your success, you're more likely to feel good about continuing. And, of course, once you reach your goal, that feeling can encourage you to keep working toward your other goals and setting new goals

Self-check 7

Part I: short Answer writing

Directions: Answer all the questions listed below.

1. Explain documents required to open account
2. Type accounts
3. Discuss adjusting savings goal

THE ONLY BUDGETING BOOK TERE STOUFFER

YOU'LL EVER NEED: How to Save Money and Manage Your Finances with a Personal Budget Plan

That Works for You

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