

FINANCIAL LITERACY

for Teens

BY ROCHELLE L. MOORE, CFP®, CDFA®, CPA/PFS



Financial literacy, knowing the components of personal finance and having the ability to make intelligent financial decisions, is an important life skill to have. Although educational curriculums are improving, many students graduate high school without any exposure to formal learning regarding financial matters.

Often times, a child's first experience with money comes in the form of receiving birthday or holiday gifts, but they rarely understand the value or the role of money in our economic society. As children grow older, they may have chores to do which earns them an allowance. With this they learn the concept of effort for compensation.

Older still and teens are now able to be hired for their first "real job." They may want to earn and save money for a certain goal such as a new computer game, event tickets or their first car.

The main principals of financial literacy include:

- Earning - understanding the effort, knowledge and experience involved in earning income, how income taxes and other deductions impact "gross income" and managing "net income."
- Spending - including budgeting effectively to manage one's spending, recognizing the difference between needs and wants, especially when funds are limited, and the ability to make informed spending decisions.
- Saving - from awareness of the importance of maintaining a sufficient emergency fund for unforeseen events as well as working toward short-term goals (purchasing a new game or gadget) and longer-term goals (buying a home, paying college tuition or funding retirement).
- Borrowing - recognizing favorable and unfavorable loan terms by understanding how interest rates work, repayment terms and the impact one's credit scores can on those terms. Knowing the importance of paying monthly bills on time, including credit cards in full each month, to avoid unnecessary interest charges. A good guideline to remember is to charge only what you can afford to pay off at the end of the month.
- Investing - protecting and growing your money by understanding terms such as "inflation," "compounding," "time value of money," "time horizon," "asset allocation" and "risk tolerance" to build long-term wealth. Learning strong money habits early enables teens to grow into financially responsible and confident adults. They will be better prepared to handle college costs, lease a car or housing and much more with the ability to also avoid common financial pitfalls, reduce future debt obligations, and improve long-term financial independence.

Budgeting is the foundation of personal finance. Teens should be taught how to track income and expenses as the first step toward building a budget. That monthly budget should be broken down into the following four categories:

- Income - funds received from paychecks and investment earnings
- Fixed expenses - school, rent, utilities, insurance, loan and other necessary payments
- Discretionary expenses - eating out, shopping, hobbies, travel and entertainment



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- A savings component - ideally 10% to 20% toward an emergency fund and future goals. Children often copy adults, so you can help your teen by being a good role model. Engage in age-appropriate discussions about money and encourage questions. Include them in budgeting exercises, perhaps planning the family vacation within a set budget. Use everyday events like grocery shopping or buying a car to create teachable moments on budgeting, comparison shopping, and evaluating funding options.

The next step would be to set short-term, mid-term, and long-term financial spending goals. Work with your teen by starting small with a specific goal and by breaking down larger goals into more easily achievable steps. It's important to also keep in mind that budgets are not a set in stone and may be adjusted based on changes in income or spending needs.

Explain economic concepts like inflation and how when inflation rates fluctuate it affects purchasing power. Demonstrate inflation by comparing the cost of items today, such as a gallon of milk or gasoline, with their cost five, ten and twenty years ago. Compounding can become an enticing exercise by showing how money can grow exponentially, especially the longer it is left to grow as with a child's longer time horizon. Risk tolerance is another important concept so that the chance of losing hard-earned money is minimized, typically through diverse investment selections or asset allocations.

The opposite is also important to mention because poor money management can have long-lasting negative consequences. Examples include incurring bank overdraft fees by not accurately tracking spending, falling for "buy now, pay later" offers, or seeing balances skyrocket by not paying off credit cards in full each month. Teens often get excited about those first paychecks or money received as a gift and might want to spend it all right away. Waiting and saving for something you really want can feel like forever, but it may be more beneficial to save up ahead of the purchase rather than using credit cards with the potential for incurring interest and fees.

Enlist the assistance of one or more of the many financial tools available including books, games, apps, podcasts, and online courses to help demonstrate concepts and track funds. Raising financially literate children is more than just teaching them about adding and subtracting numbers in an app or on a spreadsheet. It's about helping the next generation become capable and self-sufficient individuals when it comes to making money decisions. One of the most rewarding benefits is the feeling of pride knowing that you've earned what you have.

We are happy to answer your financial questions, to walk through the financial and non-financial decisions surrounding your stage of life and help you to achieve your goals. Give us a call at (217) 441-2200 or visit us online and check out the free resources available at www.MySoundPlan.com.