Budgeting

Like the federal government, individual consumers must manage their money. In this section, you will learn about budgeting and saving money.

Vocabulary

discretionary expense: an expense a person can choose to have

fixed expense: an expense that does not change from month to month

gross income: the total amount of money that is earned

mortgage: a loan to buy a house

net income: the amount of money a person actually takes home after taxes and other expenses are subtracted from gross income

variable expense: an expense a person must pay each month, but its amount might change

When a person has a job, he or she receives wages in exchange for labor. In other words, the person gets paid for the work he or she does. A person's paycheck shows **gross income** and **net income**. Gross income is the total amount of money that is earned. Net income is the amount of money left after taxes and other expenses are subtracted from gross income. This amount is what the person actually takes home. For example, FICA taxes, income taxes, and payments for medical insurance are things that might be subtracted from a person's gross income.

A person must use his or her net income to pay for all the things he or she needs and wants. These things can include rent for a place to live, food, electricity, and transportation. In addition, most people want to do fun things, like go to the movies or have dinner at a restaurant with friends. A person must pay for all these things without spending more money than he or she earns. It can be difficult and complicated to manage money.

People often use a budget to help them manage their money wisely. Remember, a budget is a plan for saving and spending money. To create a personal budget, you should spend two months keeping track of everything you spend money on. Once you know how you are spending your money, you can create a realistic budget. The goal is to have a balanced budget. To have a balanced budget, your income must be equal to the amount of money you spend and save. When you create a budget, you write down the estimated amounts you plan to spend on expenses. You can write your budget on a sheet of paper or use a computer program to help you organize your budget.

Each month, you will have three types of expenses: **fixed**, **variable**, and **discretionary expenses**. Fixed expenses do not change from month to month. These expenses include your rent or **mortgage** payment, car payment, and car insurance payment. Since these expenses do not change, you must plan on paying the same amount every month.

Variable expenses can change from month to month. These expenses include payments for utilities, like electricity, and money spent on gasoline and groceries.

Budgeting

These expenses will probably vary each month. For example, if gasoline prices go up, you will have to spend more money on gasoline for your car.

Discretionary expenses are things you can choose to spend money on, like going to the movies, eating at a restaurant, or buying a new pair of jeans. It is up to you whether you spend money on these things or not.

Experts say that it is smart to save at least 10 percent of your income. You will have to set aside money in your budget for savings. This way, if there is an emergency, you will have money in your savings account to pay for it. You also might want to save your money for things like buying a car or taking a vacation.

Once you have created a budget, you can look at it and find ways to change it if you need to. For example, you might think you are not saving enough money. Or maybe you would like to spend more money on entertainment. You might choose to save more money by not eating at restaurants as often. You may decide that you do not make enough money to do the things you want to do, so you might choose to work more hours to make more money.

Look at the sample budget below. Is it a balanced budget?

Sample Budget

Income

Wages	$1,484.00

Fixed Expenses

Rent	$425.00
Car Payment	$255.00
Car Insurance	$66.80
Telephone	$42.57
Total	**$789.37**

Variable Expenses

Electricity	$35.00
Water	$10.00
Groceries	$200.00
Gasoline	$50.00
Total	**$295.00**

Discretionary Expenses

Entertainment	$100.00
Savings	$148.40

Total Expenses	**$1,332.77**

Section Review

1. How do you know if a budget is balanced?

____

____

2. Give an example of a variable expense.

____

____

Borrowing Money

Section • 2

Even when a person has a balanced budget, it is sometimes necessary to borrow money. In this section, you will learn about loans and credit cards.

Vocabulary

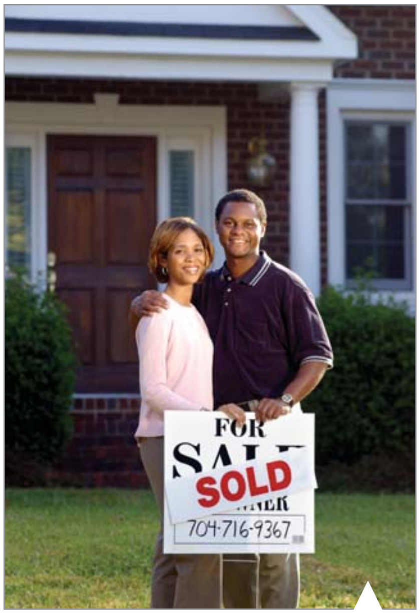
loan: money borrowed from a bank

principal: the amount of money borrowed when someone takes out a loan

Have you ever borrowed something from a friend? Imagine that you are sitting in class one day, and you realize that you have run out of notebook paper. You borrow five sheets of paper from a friend and promise to replace them. The next day, you bring your friend five sheets of notebook paper to replace the paper you borrowed.

People borrow things when they need items that they do not have. In the same way, people borrow money to buy the things that they want. They borrow money because they do not have enough money saved to pay for the items. People often borrow money from banks to pay for college tuition or to buy large items like houses and cars.

When a person borrows money from a bank, he or she takes out a **loan**. Borrowing money from a bank always works the same way. The amount of money borrowed is called the **principal**. The bank charges a fee for borrowing the money. This fee is called interest. When the person repays the loan, he or she pays the bank the principal plus interest. A person has a specific amount of time to pay the loan back. For example, a person might take five years to pay back the money borrowed to buy a car.



Jupiter Images

These people borrowed money to buy a house. A loan to buy a house is called a mortgage.

Using a credit card is a type of borrowing. When a credit card company issues someone a credit card, the company agrees to loan that person money. With a credit card, a person can buy the things he or she wants. Then, the person must pay the credit card company back. A credit card usually has a limit on the amount of money that can be spent using the card. For example, if the limit on your credit card is $2,000, the credit card company has agreed to lend you no more than $2,000 at a time. If you reach the limit, you will have to pay money back to the company before you can use the credit card again.

Borrowing Money

Section • 2

Each month, you will get a credit card statement in the mail. The statement will list the items you have purchased that month and will tell you how much money you owe. The credit card company will let you pay back the money you have borrowed over time. But, if you do not pay the total amount due, the company will charge you interest. The longer you take to pay back the money, the more money you will have to pay in interest and other fees.

Did You Know?

The word "credit" comes from the Latin word *creditus*, which means entrusted. Lenders trust borrowers to pay them back.

If you do not have enough money in the bank to make a large purchase, you might use a credit card. For example, if you needed a new computer, you would have to save your money for months to be able to pay cash for it. If you needed the computer right away, you might decide to use your credit card instead.

Jupiter Images

There are many different credit card companies.

Also, credit cards can be helpful if there is an emergency and you do not have enough money to pay for it. For example, if your car had a flat tire, you would need to replace it immediately. Since you could not plan for a flat tire in your budget, you would probably need to use your credit card to buy a new tire.

Credit cards are useful and convenient. However, they can easily lead to serious financial trouble. It is easy to use credit cards too often. When this happens, a person ends up owing a lot of money. Sometimes, it can take years to pay back money borrowed from a credit card company. If you have a credit card, use it wisely and never borrow more money than you can pay back.

Section Review

1. What is principal?

____

____

2. How can a credit card lead to serious financial trouble?

____

____

Chapter Checkup

Matching

Match each word to its definition, and write the letter in the blank.

_____ **1.** an expense a person can choose to have

_____ **2.** an expense a person must pay each month, but its amount might change

_____ **3.** an expense that does not change from month to month

_____ **4.** the amount of money borrowed when someone takes out a loan

_____ **5.** money borrowed from a bank

A. discretionary expense

B. fixed expense

C. loan

D. principal

E. variable expense

Choose the Answer

Circle the answer that correctly completes each sentence.

6. A person must use his or her (**gross** / **net**) income to pay for all the things he or she needs and wants.

7. When you create a budget, you write down the (**exact** / **estimated**) amounts you plan to spend on expenses.

8. Money spent on rent is a (**fixed** / **variable**) expense.

9. Money spent on electricity is a (**variable** / **discretionary**) expense.

10. Experts say that it is smart to save at least (**half** / **ten percent**) of your income.

Chapter Checkup

Fill in the Blank

Use the words in the word bank to complete the sentences.

Word Bank

budget	credit card	principal
fee	years	

11. A bank charges a ___________________ when a person borrows money.

12. When a person repays a loan, he or she pays the bank the ___________________ plus interest.

13. Using a ___________________ is a type of borrowing.

14. A person might take five ___________________ to pay back the money borrowed to buy a car.

15. Sometimes, there is an emergency that could not be planned for in your ___________________.

True / False

Decide if each statement is true or false, and write "true" or "false" in the blank.

__________ **16.** A person's goal should be to have a balanced budget.

__________ **17.** People borrow money when they do not have enough money to buy the things that they want.

__________ **18.** If you have a credit card, you should use it wisely.

__________ **19.** You should always borrow more than you can pay back.

__________ **20.** Concert tickets are an example of a fixed expense.