Chapter 14: Managing Your Personal Finances

Questions — Let's Explore

Q1 Why is managing money wisely important for all individuals irrespective of their income?

Managing money wisely is important because money is a limited resource that must be used efficiently to meet both present needs and future goals. Regardless of income level, individuals face choices about spending, saving, and investing. Without proper management, even a high income can run out, while careful planning can help those with lower incomes build security over time. Personal finance helps people prepare for emergencies, achieve goals such as buying a house or funding education, protect assets through insurance, and avoid the burden of unnecessary debt. It also ensures that people live within their means and build long-term financial stability.

Q2 How can budgeting help people balance their present needs with their future financial goals? Give examples.

Budgeting is a written plan that balances income and expenses. It helps people allocate money deliberately — covering present necessities while setting aside amounts for future goals. By listing all expenses and setting a savings target, a person can avoid overspending and redirect money toward what matters most. For example, a family budgeting monthly can decide how much to spend on food, rent, and transport while saving a fixed amount each month toward children's education. A student could save 500 a month toward a new bicycle worth 3,000 in six months. Regular review and adjustment keep the budget realistic as circumstances change.

Q3 School Reopening Budget Activity: Your parents have given you 3,000 to prepare for the new school year. Make a list of the items you need, find out their prices (by visiting local stores, or asking a parent or teacher), and prepare a budget. Calculate the total cost and check whether it stays within 3,000. If your total is less than 3,000, you may add one additional item of your choice. If your total exceeds 3,000, decide which item(s) you can postpone or avoid buying to stay within your budget.

List all the school items you need (school bag, books, uniform, shoes, notebooks, pens, pencils, art supplies, etc.) and find out the price of each from a nearby store or by asking a parent. Enter each item and its price in the budget template. Add all amounts to get the total. If the total is under 3,000, add one optional item of your choice and check the new total. If it exceeds 3,000, identify which items are wants rather than needs and postpone or remove them until the total stays within 3,000. Record the final total expenses and the remaining savings in the template.

Q4 Why is saving alone often not enough to build wealth in the long run? How do investments help increase the value of money over time?

Saving means setting aside money for future use, but money kept at home or in a non-interest-bearing account does not grow. Over time, inflation reduces purchasing power — for example, if a school bag costs 1,000 today and inflation is 6% per year, the same bag may cost 1,060 next year. If savings do not grow at least as fast as inflation, the saver can afford less over time. Investing puts savings into assets such as fixed deposits, stocks, or mutual funds that generate returns. Through the power of compounding — where returns themselves earn further returns — investments grow significantly over the long term, helping individuals build wealth and protect the real value of their money.

Q5 Investment Planning Activity: Suppose you received cash gifts worth 3,000 on your last birthday and decided to save 1,500. With the help of your teacher, calculate the returns you might have earned if you had invested this amount in different combinations of investments. For example, what returns would you have received if you had invested 500 in a fixed deposit, 800 in the stock market, and 200 in gold? Try other combinations and find information on the returns from different investment options using reliable sources. Based on your findings, prepare an investment plan explaining why you think each investment option is suitable or unsuitable.

Look up current interest rates for a fixed deposit at a bank's website, and recent return data for the stock market and gold from a newspaper or reliable financial website. Using the 1,500 saved, try different splits — for instance 500 in an FD, 800 in stocks, 200 in gold. Calculate the expected returns for each portion after one year using the rates you found, then add them up. Try at least two more combinations (e.g., 1,000 in FD + 500 in a mutual fund). In your investment plan, explain that FDs offer low risk and assured returns, stocks carry higher risk but higher potential returns, and mutual funds spread risk through diversification. State which combination suits a student's goal of safety with some growth, and why.

Q6 How does inflation affect the value of money over time? Why should people consider inflation while making financial decisions?

Inflation is the rise in the prices of goods and services over time, which reduces the purchasing power of money — the same amount of money buys fewer goods as prices increase. For example, if a school bag costs 1,000 today and inflation runs at 6% per year, it will cost about 1,060 next year. Money kept at home without growing will buy less and less over time. People must consider inflation when making financial decisions because savings that earn less than the inflation rate effectively lose value. By investing in assets that generate returns higher than inflation — such as fixed deposits, mutual funds, or stocks — individuals protect and grow the real value of their money.

Q7 Different investment options involve different levels of risk and return. Do you think taking higher risks is always the best way to earn higher returns? How should a person decide which investment option is most suitable for them?

Taking higher risks is not always the best strategy, because higher-risk investments such as shares can also result in significant losses if markets fall. While the risk-return trade-off means higher-risk options have the potential for higher returns, this potential is not guaranteed. A person should choose an investment based on their financial goal (what they are saving for), time horizon (how long they can keep the money invested), risk tolerance (how much loss they can absorb), and liquidity needs (how quickly they might need the money). For example, someone saving for retirement over 30 years may afford more risk than someone saving for a goal three years away. Fixed deposits suit those who prefer safety, while stocks suit investors with a long horizon and tolerance for short-term fluctuations.

Q8 Why do people buy insurance policies even though they may never face a major loss? How does insurance provide financial security?

People buy insurance because life is uncertain — illness, accidents, property damage, or the death of a breadwinner can happen to anyone and cause severe financial hardship. Insurance works on the principle of risk sharing: many people pay regular premiums into a common pool, and those who suffer a loss receive financial compensation from that pool. Even if a person never makes a large claim, the premium buys peace of mind and ensures that a sudden crisis will not wipe out their savings. Without health insurance, for example, a serious illness could force a family to spend a large portion of its savings on hospital bills. Insurance provides financial security by reducing the impact of emergencies, helping families recover, and encouraging disciplined saving through regular premium payments.

Q9 Imagine your family receives 1,00,000 from farming, a small business, livestock sales, and savings. Help your family decide how to use the money wisely. (Step 1: Prepare a Budget allocating among Savings, Education, Household expenses, Health and emergency fund, Farm or business investment, Home improvement, Festivals and recreation, Other. Step 2: Classify each expense as a need or a want. Step 3: Suppose your family saves 30,000 at 8% compound interest per year — using $A = P(1 + r)^n$, calculate the amount after 5 years and the interest earned. Step 4: Apply the Save-First principle — if 20,000 is saved first, only 80,000 is available for spending. Step 5: Reflect on savings percentage, needs vs wants, how savings improve financial security, and how compound interest helps money grow.)

Step 1 — Model budget for 1,00,000: Savings 20,000 (20%), Education 15,000 (15%), Household expenses 25,000 (25%), Health and emergency fund 10,000 (10%), Farm or business investment 15,000 (15%), Home improvement 8,000 (8%), Festivals and recreation 5,000 (5%), Other 2,000 (2%). Total = 1,00,000. Step 2 — Needs vs Wants: school fees = need (essential for education); new mobile phone = want (not essential for survival); better seeds or livestock feed = need (productive asset for livelihood); festival celebrations = want (desirable but can be reduced); water storage tank = need (essential for daily life). Step 3 — Compound interest on 30,000 at 8% for 5 years: $A = 30,000 \times (1.08)^5 = 30,000 \times 1.4693 \approx 44,080$. Interest earned ≈ 14,080. Step 4 — Save-First: saving 20,000 first leaves only 80,000 for spending, ensuring future needs and emergencies are covered. Step 5 — Savings percentage = 20%; saving improves financial security by providing a buffer against emergencies and future needs; compound interest helps money grow because returns are reinvested and themselves earn returns, accelerating wealth over time.