

Your Financial Foundation

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Since the economy moves through continual periods of ups and downs, it's impossible to avoid economic downturns entirely. However, there are steps you can take to build and protect your finances to help ensure that the next downturn won't throw you off your financial track or lead you into debt.



Introduction

A successful financial future requires a sound structure and a secure foundation, just as a well-made home does. You create this base with a well thought-out budget that fits your personal circumstances, a savings and investing plan that can help you meet your goals, a strategic use of credit and debt and adequate insurance to protect you and your loved ones. The more proactive you

are about implementing these financial building blocks, the easier it will be to meet your goals. And while you can't know for sure what you'll face in the future, you'll be in a better position to overcome financial hurdles when they appear—the loss of a job, unexpected emergency expenses, rising health-care costs or a loss in your investment portfolio—if you have a strong financial foundation upon which you can rely.



Managing Your Income and Expenses

Successful money management requires looking at your finances from short-, medium- and long-term perspectives. While your current expenses need to be a top priority, so does planning for your future, which means next year, five years from now and 30 or more years ahead. That's why, as a first step, you should have a basic financial plan.

Your basic financial plan consists of your road map and directions for all of your financial goals—where you are starting for each, where you want to end up and how you'll get there. It should detail all of your goals and the timeframes in which you'd like to accomplish them—whether that means paying for a child's education,

buying your first home or retiring at the age you'd like.

Understanding Cash Flow

Before you can create a budget, or spending plan, for the future, you need to evaluate how you're living now by analyzing your cash flow.

Cash flow describes the movement of your money—the money coming in and the payments going out. Whether your cash flow is positive or negative has a big impact on your ability to meet your financial goals.

Positive cash flow means that your annual expenses are less than your income. For example, if your salary is \$50,000 and you spend \$45,000 over

Budget Plans

If you want more of your expenses to be predictable, find out if your utility company has a budget plan. If you sign up, your expenses will be the same each month. The company uses your past or current usage to estimate your annual expenses and divides by 12.

the course of the year, you have a positive cash flow of \$5,000. The good news is that you are probably living beneath your means and are already taking steps to save and invest for your future. At a minimum, you're able to pay your bills, cover small unexpected expenses and still have enough money left over to pay for some of the things you enjoy.

On the other hand, if you spend \$55,000, you have a negative cash flow of \$5,000. You may find yourself living paycheck to paycheck, spending money on unplanned purchases and never really being able to get ahead. If you have a negative cash flow, you can't save for the future or pay down any debt you may have. The longer your cash flow is negative, the larger the problem grows. The good news is that if you recognize this situation soon enough, you will be able to take steps to address the way you're managing your finances before it impacts the future you want.

Over the long term, positive cash flow can help improve the likelihood that you will be able to pay for your long-term financial goals, such as buying a house or enjoying a comfortable retirement.

Creating and sticking to a budget is an important and effective first step in gaining control of your finances and staying in control.

Creating a Budget

Budgeting is a useful tool for everyone. It can provide a great next step even for those who have a clear vision of their future and have their finances under control. You use a budget to plan how you'll allocate the money you have coming in to pay and save for the things you need, now and in the future.

Before you can begin making decisions about how much of your income you'll allocate to pay for the various expenses you have, you need to know the details of your current spending.

One approach is to examine your bank statements, receipts and credit card bills from the past year. Another is to keep a written record of everything you spend for a couple of months. Recording every purchase you make (either on a digital assistant or in a small notebook you carry around with you) may make it easier to keep track of where you are spending your money.

Once you have a thorough understanding of your current spending patterns,



you'll be better equipped to make decisions about how you can alter them so that you're on track for meeting your future financial goals. You may find, for example, that you could save more by making coffee at home instead of buying a cup on the way to work or by finding a more economical cell phone or cable TV plan than the one you have now.

Using Financial Filters

Before you start making cuts in your budget, it's helpful to take your financial analysis further by

categorizing your expenses. One way to do this is to run them through two filters. The first separates fixed from variable expenses, and the second separates needs from wants.

Fixed expenses are those that do not change from month to month, such as your mortgage payment or rent, insurance premiums and gym membership. **Variable expenses**, on the other hand, fluctuate from month to month. They include what you spend on food, transportation, medical bills and entertainment.



Learning Lessons

The financial downturn that began in December 2007 came as a surprise to many. If you lost a job or faced steep losses in your investment portfolio as a consequence of the recession, you weren't alone. Like many others, you may have found you needed to make significant sacrifices in order to get back on track toward meeting your goals. While sacrificing may be challenging, it can certainly help you move

forward and make the future a bit easier.

Since the economy moves through continual periods of ups and downs, it's impossible to avoid economic downturns entirely. However, maintaining a positive cash flow, saving for emergencies and spending within a budget that will help you meet your financial goals can help ensure that the next downturn won't throw you off your financial track or lead you into debt.



The second filter distinguishes essential from discretionary, or non-essential, expenses. More informally, it distinguishes needs from wants.

Essential expenses are those you literally could not do without, such as food, clothing and housing. While you can make choices to keep spending in these areas under control—for instance, not eating out regularly and choosing a smaller house or apartment than you'd like—you can't cut out these expenses entirely.

Discretionary expenses, on the other hand, are more often than not "nice to haves," such as a new cell phone or pair of shoes, but aren't necessary. While this category is probably the easiest place to make cuts in your budget, you don't need to do away with everything in this group to make a positive difference in your spending habits.

By categorizing your expenses, it will become clear where you spend the least and where you spend the most. You can also use your **spending ratio** as a guide to further clarify the areas that could use some trimming. A spending ratio identifies how much of your total income is going toward paying for a particular expense.

For example, if your income is \$60,000 and you spent \$20,000 on housing last year, divide what you spend on housing by your income to find the spending ratio. In this example it would be 33%. Since a standard guideline for housing expenses is 28% of income, you may want to reduce your housing costs and free up money to put toward other goals, such as your retirement. If this isn't possible, either because you aren't able or don't want to move, you'll have to find other areas in which to cut expenses.



Saving

As you know, saving money (or investing it) is an essential component of an effective budget. Not only may you eventually use these funds for the goals you've established for yourself, but they can also serve as an important safety net if you face unexpected financial challenges. Whether it's saving for that dream home in three years, or using your emergency funds to see you through an unanticipated downsizing, having adequate savings allows you to realize dreams and offers peace of mind.

Identifying Your Goals

The amount you should be setting aside in savings every month is directly linked to your financial goals and where you want to be in the future. While everyone's situation is different, many people share similar objectives. Supporting a family, buying a house, sending children to college and

enjoying a secure retirement are a few examples.

You probably also have some goals that are unique to you and your family. Perhaps you'd like to start a small business, be able to provide for an aging relative or plan an expensive vacation overseas. Whatever your goals are—no matter how large or small, near- or far-term—they all require planning, and have a price tag. Saving and investing can help you achieve those goals.

When you are formulating your goals, it is important to be as precise as you can be. For example, housing expenses can differ significantly based on where you want to live and the size of the apartment or house you want to live in. College tuition will vary based on whether your children go to a private or a public institution and whether they pursue a two-year or a four-year degree.

Bigger Ways to Save

While it's easy to focus on looking for small ways to reduce expenses, don't forget about two larger expenses that have a significant impact on your finances—housing and transportation. People who buy the largest or most expensive homes or cars over their lifetimes can really strain their ability to save money for their goals. Before purchasing a new home or car, be sure you analyze how the new debt may impact your ability to save, including how much interest you will be paying over the life of your loan.

The Importance of Saving

Once you've outlined your goals and the timelines within which you want or need to reach them, you can figure out how much you'll need to save to attain them. In addition to your earnings, savings and investments are essential to increasing your wealth.

In order to confidently reach your goals, especially longer-term ones, you should aim to save at least 10% of your pretax income. And while that's a good start, aiming to save 15% or 20% is even better. That means, for example, that if you have a salary of \$60,000, you'd save \$6,000 a year, or \$500 a month. If that's more than you can afford right now, you can still make progress toward your goals by saving as much as you can, even if it's as little as \$100 a month. What's most important is to begin saving as much as you can, as soon as you can.

Where to Put Your Money

In addition to basic savings accounts, money market accounts and certificates of deposit (CDs) are other popular savings options that are available. One advantage of keeping your savings in one of these accounts is that bank deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to the limit Congress sets. Credit union deposits are also insured.

The interest you'll receive depends on the type of account you use, and each variety carries its own benefits and drawbacks. CDs generally pay higher rates of interest than savings or money market accounts do. But these vehicles require your money to be tied up for a period of time, so be sure the CD you choose fits into your financial plan before you invest.

Strategies to Increase Your Savings

While you may be confident in your ability to save money, you probably also recognize that it can be challenging at times since it reduces the amount of money you have available to pay for other expenses. Bills can eat into your paycheck, leaving you with little to contribute to your savings account each month. The key is thinking of saving as a necessary expense that's just as important as your rent, utility or other obligations you have.

Tip

Virtual banks and online versions of conventional banks generally pay slightly higher interest rates than those that are offered at bricks and mortar bank and credit union branches.

Keeping It Interesting

Putting your money in an account that accrues interest means you can take advantage of compounding. Compounding occurs when the interest you earn is added to the balance in your account, creating a larger base upon which future contributions and interest can grow. So it can be a powerful force, especially over long periods of time. It's probably why Albert Einstein once said, "Compounding is the most powerful force in the universe."

One strategy that helps make saving easier and keeps you moving toward your goals is to pay yourself first. Instead of contributing to your savings after you've paid your other bills and expenses, you add to your savings account before you spend any of your income. You may be able to do this automatically through direct deposit with the help of your employer so you never even have the money in hand—some employers allow you to have a portion of your paycheck deposited directly in your savings account, with the remainder put into your checking account.

Alternatively, you could have your bank automatically move a certain amount from your checking account on a regular basis and deposit it in the savings account you select. The transfer could be on certain days of the month, every two weeks or once a month.

Investing

Investing is another powerful tool that can help you take that next step to increasing your wealth over the long term. When you invest, you put money in stocks, bonds, mutual funds or other securities because you expect them to:

- Increase in value over time
- Provide current income
- Offer a combination of both

Before you invest, though, it's important to learn as much as you can about how any investment you're considering works so you fully understand its potential risks and rewards.

When you buy **stock**, you are part owner of the company that issues it. You generally buy stock because you expect it to grow in value over time, so that you can realize a profit when you sell, or because you expect the company to issue dividends, or a portion of their profits, to their shareholders on a consistent basis.

When you buy a **bond**, you are essentially loaning money to a corporation, municipality or to the government. You earn interest during the bond's term and, when the term ends, you are repaid your principal, or the amount you invested. While there are categories of bonds that can be very risky, generally speaking, bonds tend to be less risky than stocks are. However, they also tend to offer less return than stocks do.

Another way to invest is by purchasing mutual funds. Mutual funds invest in a variety of stock, bonds or **cash equivalents**—the other major asset class—or sometimes in a combination of two or more of these classes. Many

people choose mutual funds because they find the process of selecting stocks or bonds too time-consuming, intimidating or both. Investing in a mutual fund can also help you **diversify**, or spread your investment dollars across a group of different investments, rather than concentrating your money in just a few.

You'll probably be able to earn more on the money you put into an investment than you would in a savings account because the return you'll receive is generally higher. **Return** is the change in the value of your principal plus any earnings on that principal. It can be positive or negative, just as cash flow can be. However, with the possibility of higher return comes a greater degree of risk.

In this case, risk means that when you invest, there's no guarantee you'll make money on your principal, and you may even lose it all. As a result, it's important you understand and are

comfortable with all of the risks of a particular investment before you make a financial commitment.

However, avoiding investing altogether may carry an even higher risk due to the impact of inflation, or the continual rise in the cost of goods and services over time. Historically, inflation has averaged 3%, which means that, over the long term, your assets will be worth less than they are now unless you select investments that provide a long-term return that is greater than the rate of inflation.

Investing for Your Goals

The investments you choose will depend on a number of factors, including your goals, your tolerance for risk and your investment timeframe.

While some of your goals will have more flexible timeframes, such as when you buy a house or retire, others, such as sending your child to college, won't. The key is choosing



investments that will offer you the potential for the return you're seeking and allow you to access your money when you need it.

For instance, you wouldn't want to tie up all of your money in a 30-year bond if you need to pay for your child's college tuition in 15 years. On the other hand, investing in a bond whose term is up soon before you need the money can help ensure you'll have the money when you need it.

While the number of investment options available may seem overwhelming, there are some investment vehicles designed to help you save for certain expenses, such as education and retirement, that you can investigate.

Paying for College

While the value of an education may be priceless, it is far from free. Whether you want to pay for graduate school for yourself or would like to start saving for your child's education, there are tax-advantaged plans in which you can invest that make paying for school more manageable.

Though the cost of room, board and books might be comparable wherever you or your child wants to go to school, tuition differs significantly depending on whether you choose a public or private education. For example, for the 2009-2010 school year, average tuition at a four-year

public college was \$7,020 in-state and \$18,548 out-of-state, while tuition at a four-year private institution averaged \$26,273.

While this means that you can plan on attending a college that fits a particular budget, it also means that the sooner you begin saving, the more options you'll have available to choose from.

Popular tax-advantaged vehicles, including 529 college savings plans, Coverdell education savings accounts (ESAs), 529 prepaid tuition plans and US savings bonds, can help reduce the burden of saving for an education. The rules are different for each plan, so research your options carefully to determine what will work best for your situation.

In addition to tax-advantaged plans, you can invest in a taxable account, apply for scholarships or financial aid, qualify for tax credits and apply to work-study programs.



Paying for Retirement

At some point, you have likely thought of, perhaps even dreamt about, how and where you would like to spend your retirement. For retirement, as for education, there are tax-advantaged approaches you can use to your benefit, including individual retirement accounts (IRAs) and plans that may be offered through your employer.

Individual retirement accounts (IRAs)

are tax-deferred accounts to which you can contribute as long as you're earning income. You don't pay taxes on earnings in the account as they accumulate. There are limits on how much you can contribute in a year, but you decide where to open your IRA and how to invest the assets in the account.

If you choose a traditional IRA, you may be able to deduct your contributions when you file your tax return. You pay tax on your earnings and any contributions you deducted when you withdraw, and you must start taking money out after you turn 70½.

If you choose a Roth IRA, there are no required withdrawals and any money you take out is tax free if you're at least 59½ and your account has been open at least five years. But there are income limits on who qualifies to contribute.



Employer-sponsored retirement plans

, such as the 401(k) or 403(b), are also tax-deferred plans. You may roll what you've contributed to the account and your earnings over to an IRA when you retire or leave your job. You typically have a number of investment options from which to choose, and, similar to a traditional IRA, there are rules about when you must begin making withdrawals.

Whatever the specific goals you're investing for, the more you can set aside, and the sooner you can do so, the better. That's especially true of investing for retirement, as you're likely to encounter competing demands, such as paying for a child's education, along the way. The bottom line is that nothing is more important to your long-term financial security than providing for yourself in retirement.



Credit and Debt

As you may have learned, credit can be a positive component of your spending and saving plan, providing convenience and allowing you to avoid having to carry large amounts of cash to pay for your purchases. You can also use credit, which allows you to borrow money you agree to pay back within a certain timeframe, to help build your credit history or to pay for things you may not otherwise be able to pay for in full at the time. The tradeoff is that you have to use credit wisely. If you don't pay back what you owe on time and in full, you can end up paying a lot more for something than it originally cost. At worst, it could lead you into debt.

While you must make borrowing decisions carefully, it's helpful to know that not all debt is bad debt.

Credit can help you achieve important financial goals more quickly. For instance, you may need to take a student loan to pay for education expenses, a mortgage to be able to afford a home or a car loan to pay for a car you need to drive to and from work. Saving all the money you need for any of these goals can be unrealistic.

Keys for successfully using credit are to budget for the payments on the credit you use, make sure you don't owe more than you can afford to pay back and be sure to keep your borrowing costs to a minimum.

The more you understand about how credit works, the better you'll be able to make credit work for you. The two most common types of credit are credit cards and loans.

Using a Credit Card

When you use a credit card to pay for things you want or need, you borrow against a **credit limit**, which is the maximum amount you're entitled to borrow. When you pay back what you owe, you're able to borrow an amount up to the credit limit again. This is an arrangement known as **revolving credit**.

For example, if your credit limit is \$1,500 and you charge \$500 on your card to pay for an emergency car repair, you now have \$1,000 available from which you can borrow. Once you pay back the \$500, your full credit limit is available and you can borrow up to \$1,500 again.

Though this arrangement is convenient, there are costs associated with it. One example is the **interest charge**, which is a percentage of your unpaid balance that is added to your bill every month for as long as you take to pay back what you borrowed. For example, if you have a balance of \$500 on a card with an annual interest rate of 18%, your monthly interest charge will be \$7.50. To calculate your monthly interest charge, multiply the interest rate that applies for one month, 1.5% in this example, times your unpaid balance.

The rates lenders charge on their credit cards differ, so it's important to look at a number of cards before settling on one. The easiest way to compare cards is to compare their **annual percentage rates (APRs)**, which is the actual annual rate you'll be charged. All card issuers are required by law to disclose this figure.

The APR, however, isn't the only charge for which you may be responsible. There may also be an annual



How Credit Works

When you use credit, you're borrowing money from a bank or other financial institution, known in this context as the **creditor**, and agree to pay back the amount by a certain date or on a particular schedule.

In exchange for the privilege of borrowing, the creditor charges you a percentage of what you borrow, called **interest**. The amount of interest typically accrues over the time you take to pay back what you owe. So, the more you borrow and the longer you take to pay the balance back, the more you'll pay in interest. And, if you miss payment deadlines you may also owe a penalty or late fee on top of the interest you owe.

fee, though it depends on the card you choose. To ensure you choose the card that will cost you the least, be sure to research all the fees fully before making a selection.

A card's **grace period** also has a big impact on the amount you pay. The grace period is the number of days the creditor allows before it starts charging interest on the amount of any purchases you've made in the billing period. Often you must pay the previous statement balance in full to get a grace period, but if you have, and you pay your new balance in full before the grace period ends, you won't owe any interest. On the other hand, some cards don't have a grace period at all, which means you'll begin to accrue interest as soon as you buy something.

If you're just beginning to use credit, or are trying to improve your credit history, you might consider a secured credit card. This type of card is linked to a savings account that acts as collateral if you don't pay your bill. If you miss a payment, your creditor can take what you owe from the savings account. Be sure to understand the details before you commit yourself, however, as some secured cards charge very high fees and may cost you more than you expect.

Your Credit History

Just as you would want to know all you could about someone before lending them your money, prospective lenders considering extending credit to you will look at several factors. One of these is your credit history, or the record of how you've used credit in the past. The better you are about paying in full and on time and keeping your debt at a reasonable level, the better your credit history will be.

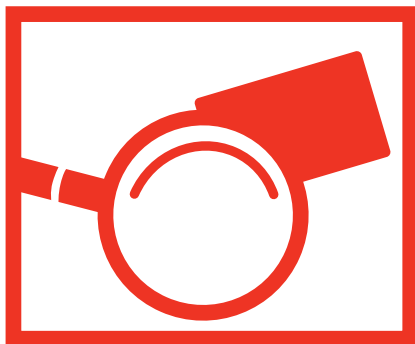
Potential lenders review your credit history by reading a summarized

Tip

Keep in mind there may be various APRs for each card—one that applies to balances you transferred from other credit cards, one that applies to purchases, one that applies during an introductory period and so on. Be sure you understand all the APRs associated with any cards you are comparing, and especially the one you select.

version of it called a **credit report**, or by looking at your **credit score**, which translates your creditworthiness into a number—the higher the score, the better. For example, a FICO® credit score can be between 300 and 850.

By law, you can obtain a free copy of your credit report from each of the three national credit reporting agencies, Equifax, Experian and TransUnion, once every 12 months by going to www.annualcreditreport.com or calling 877-322-8228. If you request them at staggered times throughout the year, you can help ensure that you'll see and be able to correct any

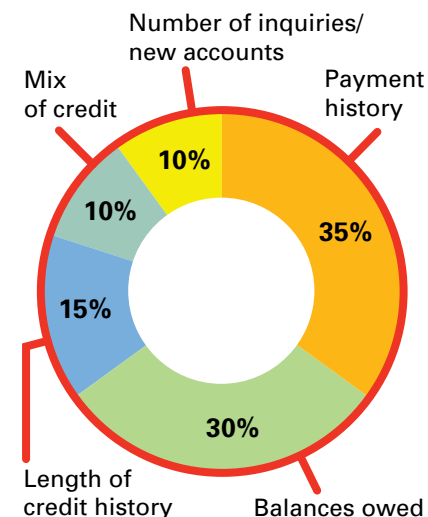


mistakes about your personal information or credit history as quickly as possible. While the FACT Act mandates that your credit report is free, if you want your credit score, you'll have to pay a fee.

If you find a mistake, report it immediately. If the information is accurate but may be damaging, you have the right to submit a brief explanation of what happened so that potential lenders can see your side of the story. While you can't change the past, you can help rebuild your credit history by making future payments on time and in full, gradually reducing the amount you owe. This will also help to raise your credit score.

Managing Your Credit Score

In general, the exact calculations for determining a credit score are proprietary to the companies that create them. However, according to myfico.com, there are five factors that help determine your FICO® score. These factors, along with the percent they impact your score, are as follows:



Keeping Score

While there are many different types of credit scores, the FICO® score, named for its developer Fair Isaac Corporation, is the most common.

As you can see, paying your bills on time and in full is the best way to maintain a good credit score or to improve it. However, there are other strategies you can employ to help boost your score:

- Aim to keep the balance on your cards below 30% of your credit limit. The higher the balance you carry, the more creditors may worry that you won't be able to repay what you've borrowed.
- Apply for only those loans or credit cards you need. The number of times you request additional credit will be reflected on your credit history as inquiries. A high number may give prospective creditors pause. Further, the more access to credit you have, the easier it will be to lose track of what you're spending—as well as what you owe.

Other Types of Cards

Charge cards are another type of card. A charge card doesn't typically have a set credit or spending limit, but you must pay your balance in full by the end of each billing period, so they aren't for everyone. Examples include certain American Express and Diners Club cards.

- Be cautious when closing older accounts, as closing your oldest credit card may shorten the amount of time it appears you have used credit.
- Correct any problems you find with the three national credit reporting agencies as well as your lender as soon as you're aware of them.

Taking Loans

Credit cards can be useful for paying for relatively minor expenses. But, for larger, one-time expenses such as buying a house or car, starting a small business or paying for college tuition,



you might need a loan. In general, the better your credit score, the easier it will be to be approved for a loan and the lower the interest rate you'll have to pay.

With a loan, you borrow a specific amount of money called **principal**, which you must repay, plus interest, by a specific date in the future. You'll receive a bill each month and you must pay the balance in full.

Loan Basics

Loans, like credit cards, have different costs, the most important of which is the APR. The others include application fees, credit check fees and sometimes closing costs.

Each loan has distinctive characteristics, including its term, or amount of time you have to pay back what you borrowed, and whether the interest rate is fixed or variable, which means it will change over the term of the loan.

In addition, loans can either be secured or unsecured. A secured loan is one that's guaranteed by collateral, or

property, that the lender can repossess if you **default** by not making the required payments. In the case of a mortgage, the collateral is your house, and for a car loan, it's your car. An unsecured loan isn't backed by collateral and may have a higher interest rate than a secured loan since the lender is assuming greater risk by lending to you.

Managing Debt

As you've learned, planning for a successful future means living within your means, saving and investing as much as you can as soon as you can and keeping debt to a minimum. While it's essential to make sure any debt fits within your budget, keeping track of your total debt is also important. Not only will it be easier to control, but you need to know what you owe overall to figure your **debt-to-income (DTI) ratio**, a number that's especially important if you're shopping for a mortgage.

Your DTI ratio is the amount of debt you have compared to your total income. Most mortgage lenders require that your DTI be no greater than 36%. This means, for example, that if you have a monthly income of \$3,600, your debt, including mortgage payments, should not exceed \$1,296, or 36% of \$3,600. Housing-related obligations (principal, interest, taxes and insurance, or PITI for short) shouldn't exceed 28% of your income.

If your debt-to-income ratios are on the higher side, it may be a good idea

Finding Money to Save

Paying off debt has many advantages, including one you may not have considered. Once your debt payments have been eliminated, deposit the same amount you had been paying for this expense into your savings or investment accounts. You'll be compounding your ability to meet your financial goals as you're increasing your net worth by building assets with money that was being used to pay down debt. Better yet, you don't have to carve money out of your budget to increase your savings.

to pay off debt before applying for a mortgage or taking on any additional debt. In general, the lower your DTI, the easier it will be for you to achieve your long-term financial goals.

Debt-to-Income Guidelines

All debt	No more than 36% of gross income
Housing related debt	No more than 28% of gross income



Being Prepared

Life is unpredictable—there may be times when a downturn in the economy, the loss of a job, a health emergency or other setback takes you by surprise. But, while you may never know exactly what's just around the bend, there are strategies you can use to prepare yourself for many of life's challenges. In fact, a large part of smart financial planning is anticipating the problems you may encounter and being prepared to deal with them.

Saving for Emergencies

Financial experts recommend that you have sufficient cash reserves to provide a cushion if emergencies or setbacks strike—which at some point, they usually do. In fact, having reserves is so important to your financial security that it should be a priority when you're setting your goals and allocating money to meet them.

Think of these cash reserves in two distinct categories. The first is a **rainy day fund**, containing perhaps \$1,000 or \$1,500 that you can use to pay for smaller, unexpected expenses that can set you back, such as car repairs, a household appliance that breaks down or a leaky faucet that requires a plumber. Certainly these expenses can be put on a credit card, but having the cash on hand in an easily accessible account can make paying off that credit card bill immediately when it comes due much easier.

The second account is more substantial and may take a bit more time to establish. This is your **emergency fund**. It's designed to cover more severe situations, such as losing a job, a divorce, an illness or injury requiring an extended hospital stay or a short-term disability. When situations such



as these occur, having at least three to six months' worth of living expenses (or more, if possible) can mean the difference between recovering from a temporary financial setback or the beginning of a financial disaster.

Being Insured

While having ample cash reserves can help in the event of unforeseen circumstances, insurance is another important way to make sure that the future you have envisioned for yourself and your loved ones is protected in case something goes wrong.

When you buy an insurance policy, you make regular premium payments in exchange for protection against certain risks. You can buy insurance to protect against almost any risk you face—from your death or disability to damaged property. To determine which policies are right for you and your family, you need to weigh how much coverage you might need against how much you can afford to spend in premiums.

Life Insurance

When you buy life insurance, you're protecting the people you love, who depend on your income for living expenses now and on your potential future earnings to meet their

long-term goals. If you die, the beneficiary of your policy receives a lump sum payment, known as a death benefit. That benefit can help your family pay for immediate expenses after your death, including the cost of a funeral. The money can also be used to help pay for much larger expenses, such as a college education or another significant financial goal—ones that may otherwise be in jeopardy if your income would have provided for them.

The two most basic types of life insurance are **term** and **permanent**, and there are varieties of each. With a term policy, you are covered—and pay premiums—for a certain period of time, while a permanent policy stays in effect for your lifetime, provided you pay the premiums. For example, you might buy term insurance for a specific period to make sure your family would have enough money to cover the mortgage or college tuition and choose not to renew when those bills are paid.

Permanent policies also enable you to build savings in a cash value account as you make payments. You can borrow against the account and will

Liquid Accounts

To ensure you'll be able to access the money in your rainy day or emergency funds fairly quickly with little to no loss in value, you might consider having this money in safe and liquid accounts that offer some return, such as a money market account or certificate of deposit (CD).

receive the cash surrender value—minus charges and fees—should you surrender or cancel the policy.

Term policies do not have this savings feature, so the same amount of coverage is likely to cost less initially. However, if you renew your coverage at the end of your policy's term, which could be anywhere from 1 year to 20 years, the premiums for the new policy will be higher because you are older.

Disability Insurance

While life insurance provides income to your family if you die, disability insurance provides financial protection to you and your family if you become sick or injured and cannot work. Most policies replace a percentage—usually between 50% and 70%—of your pretax income, up to a limit, or cap.

You might consider buying a policy through your employer, but remember that if you leave your job it's unlikely you'll be able to keep the same coverage. Other affordable options are policies available through organizations



Working on Your Own

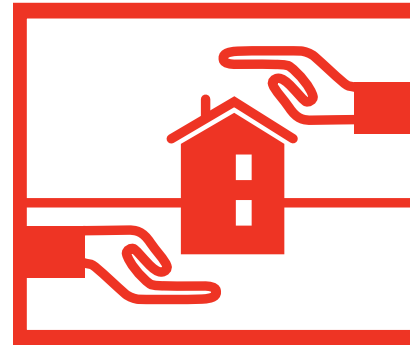
If you want to handle your finances on your own, computer software, such as Quicken® or Microsoft Money®, can be powerful tools to help you develop and revise a budget and track your spending. There are also many free services and websites available that you may find useful.

to which you belong. Before you buy a policy, though, take a close look at what the plan does and does not cover, including the plan's definition of what it means to be disabled. In some cases, you may find that it's more difficult to qualify to receive income payments than you thought it would be. (Social Security also provides disability coverage, but it can be difficult to qualify for payments.)

Other Types of Insurance

Depending on your circumstances, you may be interested in exploring additional insurance plans. In some instances, you may be required to purchase policies.

For instance, if you own a home, most mortgage lenders require that you buy homeowner's insurance, which protects against financial loss if you experience damage or loss to your property. In addition, most states require that car owners purchase automobile liability insurance to ensure



that there will be money available in case of an accident.

Other types of insurance, such as long-term care insurance and health insurance, may or may not be required, but offer you protection against long-term or unexpected, and otherwise uncovered, medical expenses.

Keeping Your Records Safe

In addition to adequate insurance coverage and access to emergency savings, keeping your financial records secure and organized is another way you can make sure you'll be prepared in the event of a financial emergency. You should choose a safe place to keep your records—to protect them from theft—but also one that is easily accessible to you and anyone in your family who may need to access them. Keeping a record of your accounts and the transactions you make will not only be helpful for long-term financial planning, but can serve as an important resource should you ever become a victim of identity theft.

Protecting Against Identity Theft

Here are some tips for protecting yourself against identity theft:

- Always keep your personal identification numbers (PINs) separate from your bank and credit cards. Better yet, memorize them.
- Never give out personal information, online or in person, to any individual or institution you're not confident is legitimate. When making a purchase online, check for a padlock or key icon in the bottom right hand of the screen that tells you you're on a secure webpage. Also be sure there is an "s" in the URL address when you are typing in sensitive information. The "s" in <https://...> stands for "secure." You should, however, still be sure the website is an authentic one.
- Monitor your accounts closely for any sign of fraudulent activity. Keep your receipts so you can check them against your statements.
- Shred all financial documents, including receipts, before you throw them away.

If Identity Theft Strikes

No matter how carefully you protect your passwords and account numbers, it is still possible you may find yourself a victim of fraud or identity theft. If someone steals your identity and commits fraud against you, there are four important steps you should take:

1. Notify the major credit reporting agencies and have them put a fraud alert on your credit report.
2. Close any accounts which have been compromised.
3. File a complaint with the Federal Trade Commission (FTC).
4. File a police report.

If you keep all of the contact information you'll need with the rest of your financial information, you'll be prepared to act quickly.

For detailed information about identity theft and what to do if it happens, visit

the FTC's homepage at www.ftc.gov and search for "identity theft."

Fine-Tuning Your Finances

While you have been planning confidently for your future, taking all the steps necessary to meet your financial goals, there are times when circumstances beyond your control get in the way of those plans and dreams. Perhaps there's an economic downturn and investments you've made do not provide the returns you anticipated. Perhaps your employer is impacted and you lose your job. Maybe you or a loved one is confronted with an unexpected illness. During these times, you may need to reevaluate your budget or realign your goals to fit your current financial reality.

In some cases, this may mean saving more than you originally budgeted for, or scaling back some of your goals. For instance, if you were planning on your

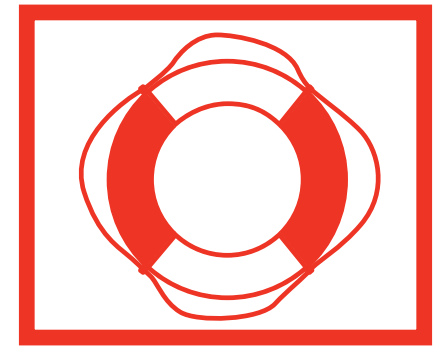
child attending a private university, you might consider having him or her start at a public school or community college and then transfer after a year or two. If you can spend less on tuition, you'll be able to either contribute more to your retirement or other savings accounts or pay down any debt you may have. Alternatives include working more years before retiring or postponing other goals, such as taking an expensive vacation.

Where to Go for Help

Despite your knowledge and confidence in your planning abilities, sometimes having some specific, professional guidance can help confirm that you are on track or can help get you back on a path toward meeting your goals. Whatever your needs—whether you're just creating a financial plan, need to readjust your goals and timeframes after a big life event or are seeking help in reducing or eliminating debt—assistance is available. You may decide to enlist someone to help you through all parts of the process or to bring someone in to help with a particular problem or situation, such as your investments, taxes or debt consolidation.

Here are some examples of where you can go for help with your personal finances:

- **Representatives from your bank or other financial institution**
- **Accountants**, who may have a Certified Public Accountant (CPA) or Personal Financial Specialist (PFS) credential. You can find an accredited CPA or PFS near you by visiting



the American Institute of Certified Public Accountants website at <http://www.aicpa.org>.

- **Financial planners**, who may have a Certified Financial Planner (CFP) or other credential. To find a CFP near you, visit the Certified Financial Planner Board of Standards website at www.cfp.net/search.
- **Nonprofit credit counselors** will evaluate your overall financial situation—your income and assets in addition to your debt—and help you create a new spending plan to help fine-tune your finances. A credit counselor can also work with your creditors to try to extend the amount of time you have to pay back your loans to lower your monthly payment obligations.

To find a reputable counselor in your area, check:

- The National Foundation for Credit Counseling at www.nfcc.org or 800-388-2227
- The Association of Independent Consumer Credit Counseling Agencies at www.aiccca.org or 866-703-8787



Conclusion

Having dreams, setting financial goals and achieving those goals are all possible and probably a part of the future you envision for yourself and loved ones. Making them a reality requires a commitment to maintaining control over your spending, using credit responsibly and making sacrifices when you need to. Though you may face financial challenges from time to time, the more you understand about the tools and products that are available to you, the easier you'll be able to make it through any challenge you face.

Keep in mind these strategies as you work toward your goals:

- **Create a budget** that will help you control your cash flow and save for the future
- **Save** and invest—as soon as you can and as much as you can—for the goals you'd like to achieve in your lifetime
- **Establish and maintain good credit**
- **Be prepared** for both predictable and unpredictable financial challenges by being properly insured and keeping your records complete and secure

Followed consistently, these guidelines can form the financial foundation you need to build a secure future.

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