



Personal Finance Turning Money Into Wealth

Desmond Chong Kok Fei

Title : Personal Finance
Turning Money Into Wealth
Author : Arthur J. Keown
Publisher : Pearson
No. pages : 607
Price : RM100
ISBN : 0132719169
Publication: 2013, Sixth Edition, United States

INTRODUCTION

Arthur J. Keown's book titled is divided into five parts and comes with a total of 607 pages. The book covers an individual's life stage planning with many real life examples and graphs and charts. The book helps an individual to think of their goals (financial planning) until the wealth distribution process (estate planning) when faced with different life cycle scenarios.

The book explains credit as receiving cash, goods or services with an obligation to pay later. The shopper's language is, "Just charge it". The credit card is the easiest way to obtain credit and once credit is easily obtained in this way, many people become addicted to it. Therefore, as the book claims, the most dangerous debt is right in your pocket - your credit card. But there is another group of people who disagree

credit is "dangerous" as they see it as very convenient when you wish to make hotel reservations, buy airline tickets, make online purchases, etc. There are numerous arguments regarding the advantages and disadvantages of credit cards. Let us gain an explanation of credit cards by understanding their important elements.

For those who have yet to read the book, the most recent edition (7th) is updated with recent changes in personal finance. Most importantly, the preceding editions and the latest one have one thing in common, the fundamental principles of personal finance are given serious emphasis so that readers may take control of their financial future by incorporating the necessary changes in their lives that could help them cope with their financial future.

Correspondence: desmond@akpk.org.my

THE 10 PRINCIPLES OF FINANCE

The author illustrates the 10 principles of finance in Chapter 1 of his book briefly before going into these in a more in-depth manner in subsequent chapters. The “10 Principles of Finance” provides the framework for the major concept of the book. The principles ensure a reader can make and carry out a financial plan.

- **Principle 1:** The Best Protection is Knowledge
- **Principle 2:** Nothing Happens Without a Plan
- **Principle 3:** The Time Value of Money
- **Principle 4:** Taxes Affect Personal Finance Decisions
- **Principle 5:** Stuff Happens, or the Importance of Liquidity
- **Principle 6:** Waste Not, Want Not—Smart Spending Matters
- **Principle 7:** Protect Yourself against Major Catastrophes
- **Principle 8:** Risk and Return Go Hand in Hand
- **Principle 9:** Mind Games, Your Financial Personality, and Your Money
- **Principle 10:** Just Do It!

PART 1 TO PART 5 OF THE BOOK

In Part 1 of the book the author writes on financial planning. He explains the financial planning process and the importance for every individual to have a plan, including having tax planning and the appropriate strategies.

In Part 2, the author draws everyday examples of money management, defining among others, the differences between cash and liquid assets and the role of borrowings. He provides a significant amount of information on the role of open credit.

Part 3 of the book covers protection with Insurance and in Part 4 the author explains the basics of investments including the ways of diversifying and obtaining mutual funds. While some examples may not be relevant to the Malaysian scenario, the basic elements, as discussed in the book are indeed those that are propagated by many financial experts.

In the final part of the book, the author illustrates life cycle issues. In the reviewer's experience, this is an important element in financial planning that throughout one's life, there are bound to be different scenarios that one has to deal with.

The author also provides appendices where he illustrates the concepts of finance, compounding, present value, future value and monthly instalment loan tables.

For the purpose of writing this review, I would like focus on one element in Part 2 where the author writes about Managing Your Money and thoroughly explains the role of Open Credit and the characteristics of Credit Cards. The books also explains individual creditworthiness which is



determined by “The Five Cs of Credit”. The Five Cs include Character, Capacity, Capital, Collateral and Condition to determine for credit evaluation of an individual.

HOW CREDIT CARDS WORK

A credit card is an electronic payment tool which allows you to purchase products and services without the exchange of cash. Credit cards involve receiving cash, goods or services with an obligation to pay later with interest. Before you make a purchase, there is a line of consumer credit extended to the consumer and once you open credit, then you can pay back the debt at whatever pace you like as long as you pay a specified amount or minimum payment each month. Additionally, you are given an interest-free period of between 20 to 50 days from the date of purchase to settle the outstanding amount.

BENEFITS OF CREDIT CARDS

Below are the benefits of owning a credit card provided you use it smartly:

- They are a convenient and efficient mode of cashless payment.
- They facilitates online purchase of products and services.
- They assist in tracking spending for budgeting purposes based on the statements.
- Some credit cards provide free personal accident and travel insurance coverage.
- They offer attractive schemes such as zero-interest instalment plan, flexi-payment scheme and balance transfer.
- They earn loyalty points to redeem goods and services.

UNDERSTANDING THE COST OF CREDIT

The main factor that determines the cost of a line of credit is the annual percentage rate (APR) which is the true simple interest rate paid over the life of the loan. It takes most of the costs into account, including interest on the balance, the loan processing fee, and document preparation fee. In Malaysia, the annual percentage rate for credit cards is 18% and the breakdown of the cost is given below.

Type of fees/charges	Explanation
Joining fee	Credit card issuers may impose a one-time joining fee. This fee varies depending on the card issuers.
Annual fee	This is a fee to be paid annually once is accepted the credit card.
Finance charges	These are charges imposed on the outstanding balance after the payment due date.
Cash advance fee	The fee varies from 3% to 5% of the amount withdrawn.
Late payment charge	This charge is imposed when you fail to pay the minimum monthly payment.
Administrative cost for overseas transactions	It varies from 1% to 5% of the transaction amount.

GRACE PERIOD

You will enjoy an interest-free period on the purchases made using your credit card if you do not have unpaid payments due from the previous billing cycle. This interest-free period is usually 20 to 50 days from the posting date of the transaction. Please take note that there is no interest-free period for cash advances.

This means that if you do not pay your credit card bill in full but carry forward the balance to the following month, the interest-free period would not be applicable. Interest charges will be imposed on each transaction from the posting date to the statement date. Further interest will be charged on the outstanding balance from the statement date to the payment due date. All the interest charges will be computed on a daily basis.

BALANCE TRANSFER FACILITY

A balance transfer enables credit cardholders to transfer their credit card balance (or part of) from one card issuer to another to save on interest charges. Usually, card issuers offer this facility at 'promotional' rates to encourage cardholders to transfer their balance. This may not be a bad idea as it helps save on interest charges.

While a balance transfer may be a good strategy to reduce interest charges on your credit card outstanding balance,

you have to be aware of the terms and conditions of such facilities.

For example, some of these conditions may state that you can only make the minimum payment of 5% of the amount transferred during the promotion period and that you cannot pay more or settle the amount earlier. In addition, there would be a 'lock-in' period barring you from transferring your balance to another card issuer without first paying a penalty. Moreover, if you opt for a balance transfer and use the credit card from which you have transferred the balance, you could incur more expenses than you can manage if you are not prudent with your spending.

You also have to make sure that you keep to the repayment amount and agreed schedule. If you are unable to do so, then the promotional rates will revert to the normal rate, say, 18% p.a., along with other late payment charges and penalties.

FLEXIBLE PAYMENT / ZERO-PERCENT INTEREST SCHEME

This is a facility arranged between card issuers and selected merchants where cardholders can pay for purchases made with the merchants at no interest by instalment ranging from three to 24 months. This is subject to the cardholder's available credit limit at the time of purchase.



MANAGE YOUR CREDIT CARDS AND OPEN CREDIT WITH 5Cs

Using credit wisely will ensure you to maintain a good record of individual credit worthiness which is measured as credit scoring. Credit scoring involves the numerical evaluation and your score is evaluated according to predetermined standard. If your score is up to the acceptance standard, then you will get approval for credit. The book proposes the 5Cs to help individuals to manage a good credit scoring.

1. **Character** - Have you established a record of timely repayment of past debt? Keep in mind that exhibiting good character involves not overextending yourself with respect to credit- not taking on too much debt given your income level.
2. **Capacity** - Determine your ability to repay any credit card charges. Lenders will look to both your current income and level of borrowing in determining your capability to service the loan.
3. **Capital** - The size of your financial holding or investment portfolio which refers to the more your savings, the more creditworthy you are. The lenders want to know whether your income is sufficient to provide for the debt you have already incurred
4. **Collateral** - This refers to assets or property offered as security to obtain credit. If you were to default

on a loan, the collateral would be sold and the proceeds from the sales would go to repay the debt.

5. **Conditions** - The impact the current economic environment may have on your ability to repay any borrowing. You may appear to be strong in all the other “Cs” but if you are affected by an economic downturn, you might not be able to meet your obligations.

CONCLUSION

We have become a society of “no secret” can be kept thanks to advancements in technology. Therefore it is essential we keep a good track record and maintain a good credit scoring to ensure our future financial security. The book gives an insight into how credit cards work and an understanding of the costs of credit to alert us into not falling into financial traps with this easy credit. Most importantly, the book provides ways to keep a good credit scoring by learning the 5Cs principles. The real life examples and simple language used makes the book interesting and it is easy to understand the concepts shared. More importantly, as the book focusses on the logic of financial planning instead of terminologies. I chose to focus in-depth on a single aspect of the book as this is one of the most important elements that continue to contribute to the consumption patterns of Malaysians, which have led many to fall into debt. ■