

“Financial literacy is wonderful if you have it and expensive if you don’t”



“A Tale of Two Brothers”

Adapted from the New York Times Best-Seller, *The New Rules of Money*, by Ric Edelman

Our story begins with two brothers, each earning \$70,000 a year. They each have \$40,000 in savings and both are buying \$200,000 homes.



Brother “A”

Believes in “The Old Way” — paying off the mortgage as soon as possible

• 15-year mortgage at 5.12% (5.44% APR)
• \$40,000 big down payment
• \$0 left to invest
• \$1,275 monthly payment (56% is tax deductible first year/28% average)
• \$1,153 average monthly net after-tax cost ²
• Sends \$100 monthly to lender in effort to eliminate mortgage sooner

Brother “B”

Believes in “The New Way” — carrying a big, long mortgage and never paying it off

• 30-year interest-only loan at 6.11% (6.29% APR ¹)
• \$10,000 small down payment
• \$30,000 remaining to invest
• \$967 monthly payment (100% is tax-deductible first 15 years/59% average)
• \$657 monthly net after-tax cost ³
• Adds \$100 monthly to investments, plus \$496 saved from lower mortgage payment, where account earns 8% rate of return ⁴

Who made the right decision? Results After Just 5 Years

• Received \$11,286 in tax savings ²	• Received \$18,574 in tax savings ²
• Has \$0 in savings and investments	• Has \$88,428 in savings and investments ⁴

What if both brothers suddenly lose their jobs?

• Has no savings to get through the crisis	• Has \$88,428 in savings to tide him over ⁴
• Can’t get a loan — even though he has \$87,247 more in equity than his brother — because he has no job	• Doesn’t need a loan
• Must sell his home or face foreclosure because he can’t make payments	• Can easily make his mortgage payment even if he’s unemployed for years
• At this point, it’s a fire sale, so he must sell at a discount, then pay real estate commissions (6-7%)	• Has no reason to panic since he’s still in control — remember ... Cash is King!

Results After 30 Years

• Received \$19,702 in tax savings ²	• Received \$87,927 in tax savings ²
• Has \$567,148 in savings and investments ⁴	• Has \$1,215,069 in savings and investments ⁴
• Owns home outright	• Owns home outright — so starts fresh and enjoys the same benefits once again

Remember ... Cash is King — and Brother “B” now has more than \$1.2 million in savings and investments! People who understand how money works choose to carry a big, long mortgage and never pay it off.

The above hypothetical examples are for illustrative purposes only. Plans vary based on the needs and wants of the customer. Illustrated interest rates are based upon the monthly average interest rates compiled by Freddie Mac for April 2003.

¹ This example is based on a Fannie Mae Interest First loan fixed at 6.11% APR. Interest only for 15 years, then the first loan converts to a 15-year amortizing loan on the 15th anniversary with a mo. payment of \$1,753.

² Assumes combined federal/state income tax rate of 32%.

³ Assumes combined federal/state income tax rate of 32%. Net after-tax cost shown is for years 1-15; average for years 16-30 is \$1,470.

⁴ Assumes 8% rate of return. Rate of return may vary based on type of investment.