

Common Sense Economics:

What Everyone Should Know About Wealth and Prosperity
(Gwartney, Stroup, Lee, and Ferrarini ~ St. Martin's Press, © 2010)

Small Group Discussion Questions

Part IV. Twelve Key Elements of Practical Personal Finance



Element 1. Discover Your Comparative Advantage.

1. The authors state, "...financial insecurity is primarily the result of the choices we make rather than the incomes we earn." Do you agree or disagree? Explain, using examples from your personal life.
2. Why is it important for you to specialize in areas where you have a comparative advantage? How can you discover key areas where you have a comparative advantage?
3. Explain the meaning of the following quote: "The worst thing you can do is convince yourself, or be convinced by others, that you are somehow a victim and therefore unable to become wealthy through your own effort and initiative." Do you agree or disagree? Give some examples to support your view.

Element 2. Be Entrepreneurial. In a Market Economy, People Get Ahead by Helping Others and Discovering Better Ways of Doing Things.

4. How can you "be entrepreneurial" without ever becoming an entrepreneur in the traditional sense (i.e., opening up your own business)? Give an example of a time when you have been entrepreneurial, or an opportunity where you could be entrepreneurial in the near future.
5. Do successful entrepreneurs share common characteristics? If so, what are they? What role do formal education and wealth play in entrepreneurship? Is either a necessity for successful entrepreneurship?
6. Is it important for employees, as well as business decision-makers, to "think entrepreneurially"? Why or why not?

Element 3. Use Budgeting to Help You Save Regularly and Spend Your Money More Effectively.

7. Do you currently have a budget? What is the purpose of a budget?
8. Do you agree or disagree with the following statement: "...almost all of our spending decisions are discretionary, rather than based on true need."
9. *Can* everyone spend less than they earn? *Can you?* Do you think it would be possible for you to save 10 percent of your income? What are some examples of expenses you might be able to eliminate?

Element 4. Don't Finance Anything for Longer Than Its Useful Life.

10. What does it mean to finance something for longer than its useful life? How does doing so force you to "pay in the future both for your past pleasure *and* your current desires"? Have you ever done this? How can you avoid doing so in the future?

Element 5. Two Ways to Get More Out of Your Money: Avoid Credit-Card Debt and Consider Purchasing Used Items.

11. What does an unused balance (a balance that is less than your credit limit on the card) represent? Is it like money in your bank account? Why or why not?
12. Explain the following statement: "...those who try to increase their consumption using credit-card debt end up having less consumption and less money than those who avoid credit-card debt and save instead."
13. Why is the interest rate on credit cards so high? Is it unfair for banks to charge, for example, a 7 percent prime interest rate to some customers and at the same time charge others 15 percent to 18 percent on outstanding credit card balances? Why or why not?
14. What types of items will generally result in substantial savings when purchased "used"? Give examples.

Element 6. Begin Paying Into a "Real-World" Savings Account Every Month.

15. What are some synonyms for what the authors call a "real-world" savings account?

16. Consider the following statement: “The surprising element relates to the nature and timing of the events, not to their occurrence.” Why does it make sense to save for such “surprises”? Provide some examples from your own life in which a “real-world” savings account would have (or did!) come in handy.
17. Do you think most Americans save for the expenses of unexpected, but nonetheless, predictable events?

Element 7. Put the Power of Compound Interest to Work for You.

18. Can people with average incomes become quite wealthy? Do they have to be lucky in order to do so?
19. What is your reaction to the example of Roger, who is deciding whether to start smoking? Is there a message about the costliness of seemingly small expenditures? Does the example reflect the power of compound interest?
20. Albert Einstein is purported to have stated, “The most difficult thing in the world to understand is the power of compound interest.” What do you think he meant by this statement?

Element 8. Diversify – Don’t Put All Your Eggs in One Basket.

21. What is the difference between a stock (equity) and a bond? Is it risky for the ordinary investor to undertake stock market investments? Are equity investments more risky than bonds?
22. What do the authors mean when they refer to “double jeopardy”? How does their advice differ from what you might expect to receive from your employer? Would this advice have made any difference to employees of companies like Enron and Bear Stearns, who lost both their jobs and a substantial value of their retirement assets when their employers ran into difficulties? Does this segment in any way alter your feelings about these employees’ misfortunes? Explain.

Element 9. Indexed Equity Funds Can Help You Beat the Experts Without Taking Excessive Risk.

23. How difficult is it to tell whether a specific business will do well in the future? Are “experts” able to determine whether the price of a stock will rise or fall in the future? Why or why not?
24. How does the “random walk theory” help to explain the authors’ enthusiasm for (indexed) equity mutual funds?

25. Can an ordinary person who does not want to spend a lot of time studying the stock market or analyzing specific businesses expect to earn an attractive return in the stock market? If so, how?

Element 10. Invest in Stocks for Long-Run Objectives, but As the Need for Money Approaches, Increase the Proportion of Bonds.

26. If an investor pays a fixed amount each month or quarter into an indexed equity mutual fund, what generally happens to the variability in the average annual rate of return as the investor pays into the fund over a longer and longer period of time?
27. How do the investment goals of people generally change over the course of their life? How do these changes influence the attractiveness of investment alternatives (for example, stocks relative to bonds)? Use examples of real-world investments as you discuss how individuals might alter their investment portfolio as they age.
28. Will people moving into the retirement phase of their life often find TIPS to be an attractive investment alternative? Why?

Element 11. Beware of Investment Schemes Promising High Returns with Little or No Risk.

29. Why is investment characterized by a principal-agent problem? Can it ever be eliminated? Explain.
30. It is usually costly for a firm to obtain its financing from small investors rather than from a bank or investment company. Why? Why should you be wary of such investments?
31. If someone offers you an unbelievable investment option that promises to make you wealthy in a relatively short period of time, what should you do?

Element 12. Teach Your Children How to Earn Money and Spend It Wisely.

32. When parents provide their children with most everything they want, what message is this sending? Is this a good way to help them learn sound personal finance?
33. "People spend money they earn more wisely than funds that are given to them." Indicate why you either agree or disagree with this statement. Use some examples to make your case.