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Assignment 4 FN281

1. Explain what amortization is and how a down payment and loan duration impact it.

Amortization is to pay off an amount of debt over time by making planned, and It also refers to the spreading out of capital expenses for intangible assets over a specific duration. Down payment impact the amortization inversely. For example, if the down payment is higher, the amortization will lower. In the same way, if the loan duration is higher, the amortization is lower.

2. What is the importance of health insurance and disability insurance in personal financial planning?

Health insurance is fundamental to create financial planning. It alleviates the financial burden individuals suffer from illness and injury, while the disability insurance offers income protection to individuals who become disabled for a long period of time, and as a result can no longer work during that time period.

3. What is life insurance? What is its purpose and principle?

Life insurance is Insurance that provides compensation to your beneficiaries should you die prematurely. Life insurance replaces income that would be lost if the policyholder died. The purpose for having life insurance is that It transfers the economic loss of death from an individual to an insurance company by way of a life insurance contract. It can help us take care of our own and extended families should we die. The principle of life insurance consists of law of large numbers, insurable interest, transfer of risk, and perfected savings.

4. Joe and Jane are both 35 years old. Although they graduated from college almost 15 years ago, they have never developed a diversified investment program. What extra money they had was invested in high-tech stocks that did quite well. Then, with the economic downturn, they encountered major losses. How could asset allocation have reduced the dollar amounts of the Joe's and Jane's losses?

The asset allocation can help us diversify the idiosyncratic risk that make our investment become highly volatile to the market risk. Diversification can be done by invested more assets in several of correlation to the market. If we have a good asset allocation, we can maximize returns while minimizing risk. In order to reduce the dollar amounts of Joe’s and Jane’s losses, they should invest in asset that have negative correlation to the market, which will gain the benefit from the economic downturn and help to compensate the losses that occur from positive correlated assets.