Funding For Gap Year

Introduction

A friend has approached me wanting some advice on comparing the total cost and time required to save or take out a loan for funding their GAP Year overseas trip. My friend will need to save up to $15,000.00 for her trip, so I will be investigating and exploring the best way for them to save up and be able to afford a GAP Year overseas. For this task I will be urged to use various resources like graphic calculators and laptops in order to find the best result for my friend. With the details I will gain from this assignment, I will then apply this in future anytime I want to borrow a lot of money on something and investigate whether a savings account or a loan is going to be the right option for me.

Part 1: Important terms summary

A fixed rate payment is an instalment loan with an interest rate which can't be changed during the lifetime of the loan. The amount of payment will remain the same, however, the proportion that will go to pay off the interest rate and pay off the principal may alter (CommBank, 2020). A variable interest rate is when the interest rate fluctuates on a loan or security (Investopedia, 2020).

An unsecured loan means you don't have assets to pay off your debt. For a number of reasons, you may use an unsecured loan like taking a holiday or make any renovations to your home. While the interest rate on an unsecured personal loan is usually higher than a secured loan, it also allows much more stability and a smoother and easier way of applying for and repaying (CommBank, 2020). A secured personal loan, such as a car, is a debt backed by an estate. The asset is used as collateral by the lender, which ensures that should you refuse to make the negotiated repayments, the lender can assume ownership of the asset and auction it to fund the expense of the debt. This protection means the lender will give the borrower a lower interest rate (CommBank, 2020).

In a fixed-rate fee, the total amount remains the same throughout the time of the loan, even though the proportion that goes to interest and principal differs. The fixed-rate payment mostly refers to mortgage loans. The borrower must decide between a fixed-rate payment and an adjustable-rate payment. The repayments stay the same each month, which then gives you more certainty throughout your loan and makes it easier to budget (Investopedia, 2020). Further repayments are made after the establishment of the loan and are made at the same time as you continue to pay the regular monthly repayments that you need. A personal fixed rate loan has an interest rate that remains identical for the entire credit term (CommBank, 2020).

A term deposit is money savings held at a financial institution where your money is lent over a fixed period of time, or term, for a discussed interest rate. Term deposits may be deposited into a bank, a building society, or a credit union (Investopedia, 2020). A savings account is an interest-bearing deposit account kept at a bank. While typically these accounts pay a moderate interest rate, their stability and reliability make them a great choice for putting the cash that you want to be available for short-term needs (Investopedia, 2020).

Part 2: Make a prediction about which may be better: to save or take a loan

Using the knowledge that I have gained I predict that a savings account for my friend will be the best option. This is because it's easier to manage the money that is required for their gap year instead of taking out a loan. Instead of having a personal loan and being at risk of additional fees, it's better to have insurance coverage, no lock in contract and being able to have easy access which makes it more beneficial for my friends future GAP year.

Part 3: Select the amount of money they require and period of time

My friend is required to save up to $15,000 within the next four years. Fortunate for my friend who has already saved 2,000 leaving them with $13,000 left. My friend has a part-time job with a regular salary and has no current expenses that needs to be paid therefore between $200 - $300 is a reasonable amount that my friend can deposit, leaving them still with some extra cash. My friend would like to use a savings account, however, I will be comparing loans as well to see which is best for them.

Conclusion

According to the information and mathematical calculations from this investigation I would have to recommend that my friend should apply for a savings account as it's a more suitable outcome. It can be noticed that my prediction in part two which was a savings account to manage their money that is required for their GAP year instead of a loan.

By choosing a savings account with Bank SA this will enable them to afford to deposit $263.21 a month for 4 years to reach their goal of $15,000 while still having extra $2,000 which they had already saved from their part time job. This makes their total $17,000 which gives them extra money for other expenses. $263.21 a month is a reasonable amount of money for my friend to be able to deposit as it leaves them still with extra cash for other expenses like shopping, etc. Instead of having a personal loan and being at risk of additional fees, it's better to have insurance coverage, no lock in contract and being able to have easy access which makes it more beneficial for my friends future GAP year.

Bibliography

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