Investing 101: The Basics

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What is investing?

Investing is the act of allocating resources, usually money, with the expectation of generating an income or profit. It’s different from saving because it involves more risk, but can also help you earn a greater return than keeping your money in a savings account. As you prepare to invest, understand that there will be gains AND losses. If your assets are diversified, your overall gains over time will outweigh your losses.

Key Terms:
Risk: The chance that the outcome of an investment will differ from the expected outcome or return. Any uncertainty with respect to investment.
Return: The money made or lost on an investment over some period of time.
Inflation: The decline of purchasing power of a currency over time. (i.e. you can buy less with $1 today than you could have in the past)
Volatility: A measure for the dispersion of returns for a given security. (i.e. how much/often the price changes) More volatile = more risky.
Broker: An individual or firm who acts as an intermediary between an investor (you) and a securities exchange (stock market, bond market, etc.)

Why invest?
- You might outpace inflation, meaning the rate of your return is higher than the rate of inflation.
- You might earn and accumulate more with compounding interest. If you reinvest your returns, your value will grow exponentially. For example, if you invest $10 now and earn $1 in returns, your next return will be on $11, and your return will grow more quickly.
- Saving alone might not be enough for your future goals.

Types of Investments

Traditional Cash Investments

Savings Account: avg. return of 0.05%
  - Very common. Many of you already have one!
  - Your bank will give you a very small return as an incentive for you to keep your money with them.

Money Market Account: avg return of 0.08%-0.11%
  - A hybrid of a checking and savings account that offers slightly higher interest rates.

Certificate of Deposit (CD): avg. return of 0.5%-1%
  - Similar to a savings account, but holds a fixed amount of money for a fixed amount of time
  - Ex: You will not be able to access $500 for 6 months, but you will earn significantly higher interest on that $500.
  - The longer the time period, the higher the interest rate.
  - These are very safe, but interest often does not outpace inflation.

Bond (debt) Investments
  - Bonds are issued to investors from companies, governments, and other organizations to raise money.
  - When you purchase a bond, you are lending the issuer money that they will then pay back with interest. Your payments will come regularly and will be outlined in the bond agreement.
  - Bonds can add stability to a diversified portfolio.
  - You can purchase them from the federal government, corporations, or your local city (called municipal bonds).
  - Average return of ~6.34%

Equity Investments (Stocks)
  - A security that represents a share or partial ownership (equity) of a company.
  - Shareholders profit as the company does well, and lose money when the company does poorly.
  - Returns vary with size, industry, and maturity of companies.

Mutual Fund
  - A type of financial vehicle made up of a pool of money collected from many investors to invest in securities like stocks, bonds, and other assets.
  - Operated by professional money managers, who charge a fee for managing the fund.
  - Attempts to “outperform” the market by conducting research and hand picking investments.

Exchange Traded Funds (ETF)
  - A security that involves a collection of securities—such as stocks—that often tracks an underlying index.
  - Similar in nature to mutual funds; however, they are listed on exchanges and ETF shares trade throughout the day just like ordinary stock.
  - Often have lower fees than a mutual fund, making them potentially more appealing to novice investors.
  - Example: SP500 index ETF (ticker: SPY)
Mitigate Risk with Diversification
Don’t put all of your eggs in one basket! A good portfolio has money in several different places. This spreads out the risk that you will lose a large share of your funds if one company does poorly.

Mitigate Risk with Dollar Cost Averaging
Dollar Cost Averaging is an investment strategy in which an investor divides up the total amount to be invested across periodic purchases of a target asset in an effort to reduce the impact of volatility on the overall purchase. With this strategy, purchases occur at regular intervals (regardless of the asset’s price). For example, you might invest $10 in your chosen asset every week for 10 weeks instead of investing all $100 at one time. This strategy is a good alternative to “timing the market,” which can be especially difficult for people who are new to investing, and can reduce volatility.
Resources

Yahoo Finance
- Provides financial news, data & commentary including stock quotes and press releases.

Investopedia
- Good for looking up a term you’re unfamiliar with.
- Provides financial and investment dictionaries, detailed explanations and more.

SEC Edgar
- Provides access to public companies’ financial statements. Be warned, these statements are long and dry. Don’t worry if you aren’t using this tool right away.

Picking a Broker

As you go about choosing a broker, consider:
- Is there a deposit minimum?
- Are there annual or monthly account maintenance fees?
- Does the broker offer access to a trading platform as part of their free membership?
- If you’re interested in mutual funds or ETFs, are there fee-free options?

Some Common Brokers:

Robinhood
- No fees, but no access to mutual funds.
- Little to no professional guidance.

TD Ameritrade
- No fees for stocks/ETFs.
- Access to mutual funds.
- Extensive educational offerings.

Fidelity
- No fees for stocks/ETFs.
- Access to mutual funds.

Charles Schwab
- No fees for stocks/ETFs.
- Access to mutual funds.

Remember
- Investing is a marathon, not a sprint. Think long term!
- Do extensive research before making any financial decision. Don’t just follow trends. An informed decision is always better than an impulsive one.
- Become familiar with different investment vehicles and different industries within the market.
- Don’t swing for the fences. Don’t put a large sum of money in one place.
- You can start investing in your future even if you have limited money to invest at the moment!

5 Steps to Get Started
1. Research and decide on a broker
2. Determine your risk tolerance and comfortability
3. Do more research on the investments you are interested in
4. Diversify your knowledge and your portfolio
5. Be patient