SAVING AND INVESTING FOR WEALTH

Hard Core Boot Camp
Content Session #1
SAVING AND INVESTING: WHAT’S THE SAME AND WHAT’S DIFFERENT?

Saving

Both

Investing
VIDEO: THE PROS AND CONS OF SAVING AND INVESTING

http://www.youtube.com/watch?v=2DBdWeTxXeU&feature=related (ING Tutorial)
WHY PEOPLE INVEST

- To achieve financial goals, such as purchase of a new car, down payment on a home, or a child’s education
- To increase current income (e.g., retirees)
- To build wealth over time
- For financial security and peace of mind
- To have funds available during retirement years
# INVESTMENT CHARACTERISTICS

<table>
<thead>
<tr>
<th>Type of Investment</th>
<th>Safety</th>
<th>Risk</th>
<th>Income</th>
<th>Growth</th>
<th>Liquidity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Common stock</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
<td>High</td>
<td>Average</td>
</tr>
<tr>
<td>Preferred stock</td>
<td>Average</td>
<td>Average</td>
<td>High</td>
<td>Average</td>
<td>Average</td>
</tr>
<tr>
<td>Corporate bonds</td>
<td>Average</td>
<td>Average</td>
<td>High</td>
<td>Low</td>
<td>Average</td>
</tr>
<tr>
<td>Government bonds</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td>Mutual funds</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
</tr>
<tr>
<td>Real estate</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
<td>Average</td>
<td>Low</td>
</tr>
</tbody>
</table>

*Source: Garman/Forgue, PERSONAL FINANCE, Fifth Edition*
**INVESTMENT RETURNS**

- **Rent** - payment received in return for use of your real estate, such as a building.

- **Interest** - “rent” for the use of your money.

- **Dividend** - portion of a company’s earnings that the firm pays out to its shareholders.

- **Capital Gain** - occurs only when investment is sold; results from increase in value of initial investment.

http://www.aarp.org/money/investing/investment_return_calculator/
TOTAL RETURN

Measure of your profit before taxes and fees

Formula:

Gain or loss in value + investment earnings

Examples:

- $1 per share dividend + $5 increase in share value = $6 per share TR before expenses
- $1 per share dividend + $5 loss in share value = <$4> share TR before expenses

http://www.ehow.com/how_6500173_calculate-total-returns.html
Illustration assumes an 8% average annual return
INVEST FOR LONG-TERM GOALS

http://njaes.rutgers.edu/money/pdfs/goalsettingworksheet.pdf

Source: Garman/Forgue, PERSONAL FINANCE, Fifth Edition
INVESTMENT PRE-REQUISITES

- Adequate emergency fund
- Adequate insurance
- No or low consumer debt balance
- Written financial SMART goals
- An “investor’s mindset”
Even small amounts invested regularly grow impressively over time

- Time + Money = MAGIC!

Volatility “comes with the territory” but not all investments are equally volatile

- Volatility = “peaks and valleys” of investment value

- Need an “investor’s mindset” to handle

The higher the potential rate of return, the greater the investment risk
INVESTMENT RISK PYRAMID

Summit
- Options
- Futures
- Collectibles

Middle
- Real Estate
- Equity Mutual Funds
- Large/Small Cap Stocks
- High Income Bonds/Debt

Base
- Government Bonds / Debt
- Money Market / Bank Accounts
- CDs, Notes, Bills, Bankers Accept.
- Cash and Cash Equivalents

High Risk
Low Risk
Historically, common stocks have out-performed other investments over long time periods **BUT**...it has not been a smooth ride!

<table>
<thead>
<tr>
<th>Year</th>
<th>S&amp;P 500 Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>-11.90%</td>
</tr>
<tr>
<td>2002</td>
<td>-22.1%</td>
</tr>
<tr>
<td>2003</td>
<td>28.7%</td>
</tr>
<tr>
<td>2004</td>
<td>10.9%</td>
</tr>
<tr>
<td>2005</td>
<td>4.9%</td>
</tr>
<tr>
<td>2006</td>
<td>15.9%</td>
</tr>
<tr>
<td>2007</td>
<td>5.5%</td>
</tr>
<tr>
<td>2008</td>
<td>-37.0%</td>
</tr>
<tr>
<td>2009</td>
<td>26.5%</td>
</tr>
<tr>
<td>2010</td>
<td>15.1%</td>
</tr>
</tbody>
</table>
TECHNIQUES TO OFFSET RISK:

- **Diversification**
  - Putting your money, “your eggs,” into several “baskets” (e.g., stocks, bonds, cash, real estate)
  - [http://www.investopedia.com/articles/02/111502.asp#axzz1rH9rDBUo](http://www.investopedia.com/articles/02/111502.asp#axzz1rH9rDBUo)

- **Dollar-Cost Averaging**
  - Investing regular amounts at regular intervals regardless of price
  - Examples: $50 on the 1\(^{st}\) of every month or 6% of your gross income every payday
  - Lowers average share price cost over time
### DOLLAR-COST AVERAGING EXAMPLE

<table>
<thead>
<tr>
<th></th>
<th>January (Market High)</th>
<th>February</th>
<th>March</th>
<th>April (Market Low)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount Invested</td>
<td>$200</td>
<td>$200</td>
<td>$200</td>
<td>$200</td>
</tr>
<tr>
<td>Share Price</td>
<td>$35</td>
<td>$28</td>
<td>$24</td>
<td>$20</td>
</tr>
<tr>
<td>Number of Shares Purchased</td>
<td>5.7</td>
<td>7.15</td>
<td>8.3</td>
<td>10</td>
</tr>
</tbody>
</table>

**Total Number of Shares:** 31.15 shares

**Average Share Cost:** $25.68/share ($800 \div 31.15)
Percentage of portfolio in different asset classes
Important factor in overall investment success
The more stock in portfolio, the more aggressive the asset allocation

- One guideline: 110 - age = % of portfolio in stock
- Conservative portfolio: less stock in portfolio

Conservative          Moderate          Aggressive
PORTFOLIO REBALANCING

- Get back to original asset class weights (percentages) to maintain same risk level
- Asset classes grow at different rates
- Two ways to do:
  - Sell assets in over-weighted asset class
  - Put new money in under-weighted asset class
- Forces you to “buy low, sell high”
INVESTMENT FRAUDS
The difference between a pyramid scheme and a Ponzi scheme is that a Ponzi schemer will only ask you to invest in something. You won't be asked to take any action other than handing over money.

On the other hand, a pyramid schemer will offer you an opportunity to make money yourself by recruiting new “investors” into the “franchise” similar to a multi-level marketing firm.
## Pyramid Schemes

<table>
<thead>
<tr>
<th>Levels</th>
<th>Number of Participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>2</td>
<td>36</td>
</tr>
<tr>
<td>3</td>
<td>216</td>
</tr>
<tr>
<td>4</td>
<td>1,296</td>
</tr>
<tr>
<td>5</td>
<td>7,776</td>
</tr>
<tr>
<td>6</td>
<td>46,656</td>
</tr>
<tr>
<td>7</td>
<td>279,936</td>
</tr>
<tr>
<td>8</td>
<td>1,679,616</td>
</tr>
<tr>
<td>9</td>
<td>10,077,696</td>
</tr>
<tr>
<td>10</td>
<td>60,466,176</td>
</tr>
<tr>
<td>11</td>
<td>362,797,056 - more than U.S. Population</td>
</tr>
<tr>
<td>12</td>
<td>2,176,782,336</td>
</tr>
<tr>
<td>13</td>
<td>13,060,694,016 - more than double World Population</td>
</tr>
</tbody>
</table>
“PUMP AND DUMP” SCAMS

- Promoter urges you to “buy now or lose out”
- Price rises sharply
- Fraudsters sell at peak
- Price drops when the hype stops
- Investors lose money

http://www.sec.gov/answers/pumpdump.htm
AFFINITY FRAUDS

- Target members of a group
  - Race
  - Profession
  - Religion
  - Age
- Recruit group leader to spread the word
- Key to scheme: trust

How to avoid: Ask questions!
High yield often means high risk

Watch out for “guaranteed” returns

“Red Flag” words: “limited time offer,” “safe as a CD,” “risk-free”

Beware of exotic, unusual products

- Don’t invest in anything you don’t understand or feel comfortable with

Warning:

If it sounds too good to be true, it probably is!
INVESTMENT RESOURCES
INVESTING FOR YOUR FUTURE
HOME STUDY COURSE
(COOPERATIVE EXTENSION)

- Free of charge and downloadable
- 11 units; do at your own pace
- Designed for beginning investors
- Monthly investment messages

www.investing.rutgers.edu
FINRA INVESTOR EDUCATION FOUNDATION CONTENT MODULES

- Free of charge and downloadable
- 11 content modules
- Designed for beginning investors
- Used for library investor education programs

http://www.finrafoundation.org/resources/education/modules/
INVESTMENT RISK TOLERANCE QUIZ

Rutgers Cooperative Extension

http://njaes.rutgers.edu/money/riskquiz/
TWENTY STEPS TO SEVEN FIGURES

- Set measurable (SMART) financial goals
- PYF starting today
- Diversify portfolio
- Invest regularly (DCA)
- Buy and hold stocks for the long term
- Take prudent investment risks
- Choose quality stocks
- Minimize investment expenses
- Take advantage of tax breaks
- Invest cash windfalls
- Live below your means
- Develop a spending plan
- Work hard
- Increase your “human capital”
- Grow your net worth
- Practice stability
- Take care of yourself (good health habits)
- Believe in yourself
- Pass the “Wealth Test”
  - Age x Income ÷ 10 = Adequate Net Worth
- Be patient

Slides: http://rci.rutgers.edu/~boneill/presentations/index.html
CONTENT SESSION 1
ACTIVITIES
BREAK TIME!