Getting Started as a Young Investor

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BetterInvesting™
Silicon Valley Chapter

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Presenters

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Agenda

Personal Finances and You
Goals, Strategies & Compound Returns
Basic Types of Financial Investments
Free, Impartial Education and Research Resources
Questions

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PERSONAL FINANCES AND YOU

Know Yourself

You can start your financial education journey at any time, no matter how young you are, though you must be an adult to invest on your own.

There is something to learn at every age.

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Know Yourself
Where Are You on Your Financial Journey?

If you aren't yet on your own or you are just starting your journey:

Know yourself
Think in terms of matching your spending to your means
Establish a habit of controlling your spending
Think about your goals for saving and investing
Learn which strategies match goals
Learn about basic financial concepts, like compounding

If you are on your own:

Review the goals above
Develop a financial plan
Control credit card debt
Build an emergency fund
As you can, implement your saving and investing goals
Take advantage of IRAs and employer 401Ks
Continue your lifelong financial education

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Does DIY Work for You?

Not necessary to do it yourself, but you can save on expenses

The main thing is to know yourself, now and in the future

- **How do you rate your financial literacy? Beginner? Farther along?**
- **Do you / would you enjoy learning how different kinds of businesses make their money?**
- **Do you / will you have time to learn about investing? It's OK to go slow as long as it's steady.**
- **Do you / will you have time to monitor your investments at least quarterly? It's normal to build an investment portfolio slowly and keep it manageable.**
- **Are you "math phobic." Don't be. The basic math isn't fancy.**
- **Would you sleep at night if/when you lose money?**
- **How impulsive are you?**

If you like DIY generally, just not in the investing arena, there are ways to simplify things. More on this as we go along.

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Emotions? What Emotions?

Many decisions are actually made by the unconscious centers of the brain. You are not even aware of the underlying reasons, which may not be rational.

Everybody says it's a great/lousy company!

The CEO is awesome/a jerk!

What a cool/dumb name for a stock!

I love/hate their products!

CNRI/Phototake

My research says it's a good company, but….

The economy is cratering/unstoppable!

Amazon didn't have any profits in the beginning either.

I'm afraid of losing money

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Behavioral Economics

Humans did not evolve with today's financial markets.

Our brains do not always make rational decisions regarding investing.

Educate yourself about brain shortcuts that may hinder your investing.

Knowledge of these tendencies can help you avoid them.

Realize you will make mistakes occasionally.

Be sure to learn from your mistakes.

Even better – read and learn from others' mistakes.

The Behavior Gap – Simple Ways to Stop Doing Dumb Things with Money by Carol Richards

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A Financial Plan
Whether you're on you own or not

- Review your expenses/spending
  - ✓ Essential vs non-essential items?
  - ✓ Excessive or impulsive spending?
- Compare expenses/spending to your income/means
- Create a Budget to get them in balance

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Plug Spending Leaks

- **What is a spending leak?**
  - Seemingly small amounts of money, spent on nonessentials, that add up over time
- **Examples of spending leaks**
  - Soda, coffee drinks, habits such as cigarettes
- **Wants vs. needs**
  - Deciding if you want it or need it helps with spending leaks

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Impulse Buying

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Control Credit Card Debt

- Keep only one or two cards
- Don't charge big ticket items
- Pay off each month
- Shop for best deal
- Leave cards at home
- Use cash
- Make lists

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Here's Why Credit Card Companies Love You When You Only Make the Minimum Monthly Payment

A REAL EXAMPLE
You buy a mattress for $893.47 on credit*.

Your bill arrives and tells you this:
Minimum payment = $30.00 (This is about 3.3% of the total.)

September payment is due by 9-25-22
If you are late, there's a $41 fee. (There will be a $41 fee every month you pay late. This is more than the $30 minimum monthly payment.)

If you pay only the $30 minimum for 5 years, you will end up paying $1,594. (This is $700 more than the mattress cost, or almost 80% more)

If you pay $37 for 3 years, you will end up paying $1,348 – a savings of $246. (This is $454 more than the mattress cost, or about 50% more. It is NOT a "savings." It's simply $246 less than the larger cost of 5 years at the minimum payment: 1,594-1,348 = 246)

* Annual Percentage Rate (APR) is 28.99%

The credit card company stands to make 50% - 80% profit on your mattress if you stretch payments out for the times they suggest (warn you about). That doesn't include late payment fees.

This is probably just one item on your credit card bill.

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DEBT

- **Try these steps:**
  - Prioritize
  - Pay at least the minimum
  - Eliminate debts with highest interest rates
- **Consider debt consolidation**
  - www.consumerfinance.gov
  - www.nfcc.org
  - www.afcp.org

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Pay Yourself First
Build Your Emergency Fund

Build a Financial Safety Net for emergencies

- Loss of Job
- Medical Emergency
- Car repair
- Household repairs
- Family Emergency

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GOALS AND STRATEGIES

Saving versus Investing
Short-Term versus Long-Term
Simple versus Compound Return

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SAVING versus INVESTING

Saving

Short term goals 1-5 years

- Don't risk losing money
  - Insured bank account
  - Insured CDs (certificates of deposit)
  - US Treasury Bills
- Little to no compounding

Investing

Long term goals 5+ years

- Weigh potential risks and gains carefully
  - Stocks
  - Mutual funds or ETFs
  - Bonds
  - Other
- Take advantage of compounding
- Never invest if you cannot fund your basic needs (food, rent, etc.)

More about types of savings and investing later

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Short-Term versus Long-Term Goals

Short-Term: Save

- Holiday/graduation/wedding gifts/expenses
- Vacation
- Car
- Emergency fund
- Bridge between dips in seasonal or irregular income
- Down payment on home

Long-Term: Invest

- Maintain purchasing power
- Kids' college fund
- Retirement
- Expensive hobbies
- Others

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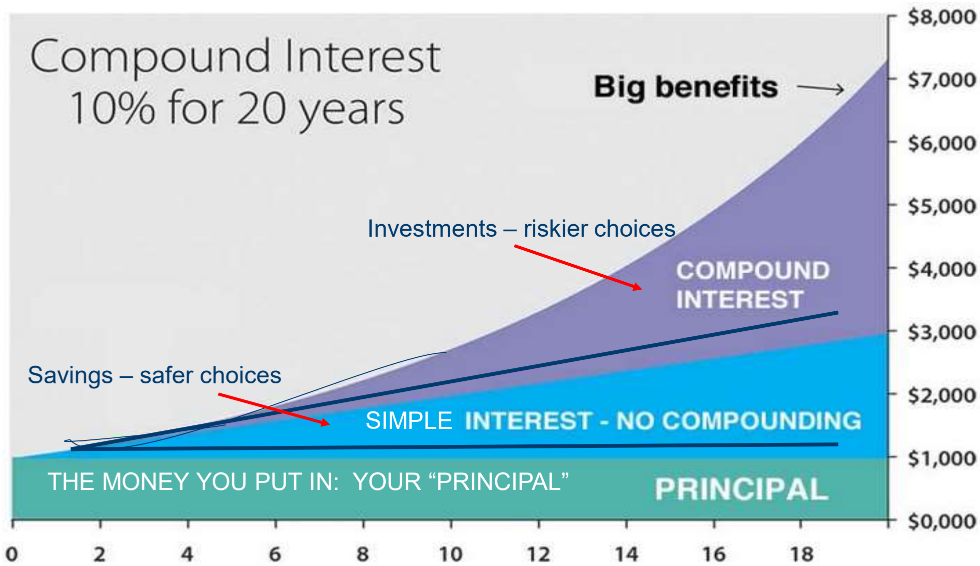
Simple vs. Compound Return



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Simple Annual Return vs. Compound Annual Return (CAR)

Simple Annual Return
$1,000 invested for 20 years @10%

Your principal ($1,000) does not grow. Every year you earn 10% of $1,000, or $100.

In year 1, you earn 10% of $1,000 = 100 earned
In year 2, you earn 10% of $1,000 = 100 earned
In year 3, you earn 10% of $1,000 = 100 earned
In year 4, you earn 10% of $1,000 = 100 earned

20 years x $100/year = $2,000

1,000 Your principal (investment)
+2,000 earned at 10% simple rate
=3,000 at end of year 20

Simple rate OK for safe, short-term saving. You probably will get 1-3% per year, not 10%.

Compound Annual Return (CAR)
$1,000 invested for 20 years @10%

Your principal ($1,000) does not grow, but every year, your earnings are added to it before the rate of return (10%) is applied

In year 1, you earn 10% of $1,000 =100 earned
In year 2, you earn 10% of $1,100. =110
In year 3, you earn 10% of $1,210 =121
In year 4, you earn 10% of $1,331 =133
Etc.

Over 20 years, compounding makes a huge difference.

1,000 Your original principal
+6,000 earned at 10% compound rate
=7,000 at end of year 20

CAR better for long-term investing, which involves risk. 10% CAR is possible.

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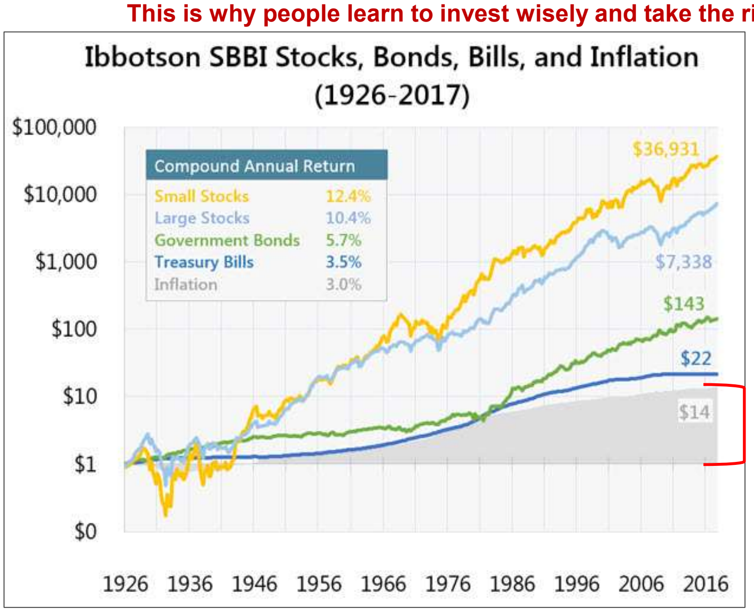
Despite ups and downs, over the long-term stocks have beaten inflation and more
This is why people learn to invest wisely and take the risk



Small stocks – large return but risky

Large stocks – large return but risky

Govt. bonds – small return less risky

Treasury bills – small return less risky

Inflation – eats into returns

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Inflation Eats Into Purchasing Power

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BASIC FINANCIAL INVESTMENTS

Stocks
Funds: Mutual Funds, Exchange Traded Funds
Bonds

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Types of Basic Financial Assets

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Stock Shareholder - OWNER

- You have BOUGHT shares of a company
- Your shares become more valuable if the company prospers
- The company may use some of its profits to pay you cash (dividends) periodically

Fund Shareholder - OWNER

- You have BOUGHT shares of a mutual fund or ETF (exchange traded fund)
- Funds are collections "baskets" of stocks and/or other assets chosen by a manager
- You buy shares of the fund, not its individual stocks or other assets
- Your shares become more valuable if the fund prospers
- Some of the fund profits may be used to pay you dividends

Bondholder - LENDER

- You have LOANED money to a company or a "Muni" – a government entity
- You receive periodic cash (interest) payments from the company or muni for a set period of time until your loan is paid back

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Pros and Cons of Investment Types

Individual Stocks

- DIY is for you:
  - Time
  - Temperament
  - Skill
  - Interest
- Historically best long-term returns
- You are OK with slowly diversifying

Funds (Mixtures)

- Often less $ needed to start
- Don't have time, etc. DIY not right for you now
- Funds provide a measure of instant diversification
- No-load Index funds often have very low fees

Individual Bonds

- You know exactly what your returns will be
- You are OK with historically low returns
- DIY is for you

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If DIY Investing Is Not for You…

You can still be a saver and investor.

Index, no-load mutual funds might be easier to use than stocks or bonds.

You can “hire” certified financial managers to advise you and make investment choices for you. You will need to “manage your manager.” Knowing something about investments makes that easier.

There will be more fees than if you DIY.

For more information about financial managers and their specialties:
FINRA.org > Education

Financial managers will want to know about your financial goals and objectives so they can best help you.

If you do retain a manager, be sure to keep track of what they do on your behalf.
The tips in this presentation will help you understand their recommendations and evaluate their performance.

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What is a Stock?

- Corporations issue (sell) stock to raise funds to operate their businesses. They sell a chunk of the business.
- Investors who buy stock become shareholders in the company … they own part of the company.
- If the company’s business succeeds, shareholders’ stock usually becomes more valuable.

In the old days, companies gave investors paper certificates to document how much they owned. Today, this is handled electronically.

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How to Buy / Sell Stocks

- Stocks are bought and sold predominantly on exchanges, such as:
  - New York Stock Exchange (NYSE)
  - NASDAQ
- Investors set up accounts with brokerages to buy and sell their shares. Brokerages you've probably heard of:
  - Fidelity Schwab Roundtable Many Others
- Minors must use a custodial account
  - CUTMA or CUGMA in California (more later)

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Rights of Stock & Fund Shareholders

- Attend and vote in annual shareholders' meetings.
- Receive dividends if companies pay them. Not all do.
  - Dividends are cash payouts, often made on a quarterly basis.
- Sell shares to reap profits of shares that have gone up in value or to cut losses from shares that go down in value.

A Shareholder's Total Return =

1. Rising (declining) value of shares +
2. Dividends, if any

Do NOT spend dividends or profits/losses from sales. Treat them as money to invest.

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Mutual Funds vs. Exchange Traded Funds (ETFs)
May be easier for beginning investors

Mutual Funds

- Purchased and sold (traded) at end of trading day
- Funds charge annual fees
- Some also charge "loads," or one-time fees
- More often are actively managed

Exchange Traded Funds

- Purchased and sold (traded) throughout the trading day
- May be more tax efficient with smaller fees
- Transaction fees may be charged when buying or selling.
- Many passively match an index

Both are baskets of stocks, bonds or other assets.

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Actively Managed Mutual Funds & ETFs

- The fund managers pick stocks (and/or other assets) which they believe will outperform the market
  - Most fund managers trade too much. (They buy and sell too often.)
  - Most are not tax-efficient.

- Fund holders pay for this asset-picking "expertise"
  - Expense ratios (range from 0.5% up to 2% or more)
  - Transaction costs (buying and selling) are an additional expense

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Passively Managed Funds/ETFs

Often good for beginning investors

These funds often match holdings in an index. Funds based on well known indexes, such as the "Dow" or the S&P 500 Stock Index, usually have very low fees.

- Very low expense ratios (0.1% to 0.2%)
- Offer tax-efficiency due to low turnover

- Indexes are lists of stock, bonds or other assets.
  They are intended to represent the market or part of the market.
- Index fund managers don't spend time picking stocks.

Over the long-term (10 years), 85-90% of active managers fail to beat the S&P 500 index

- Source: Morningstar.com

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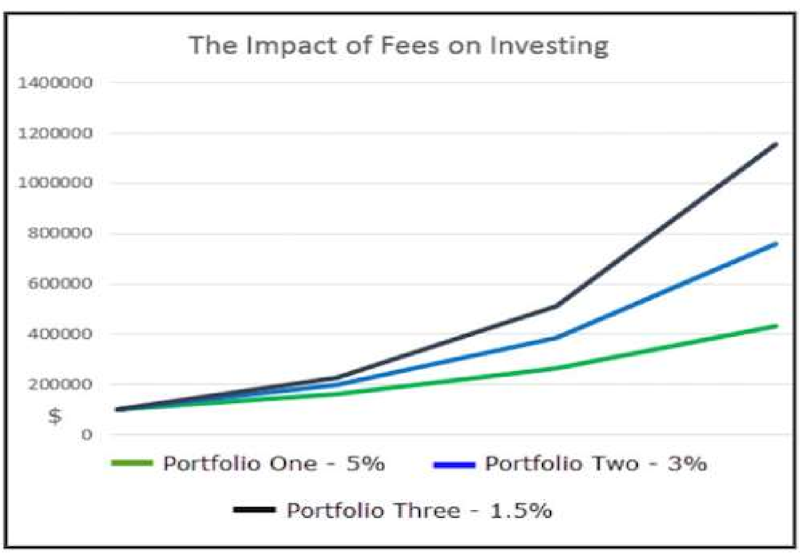
Impact of Fees



Growth of Your Investment over the long-term

1.5% fee

3% fee

5% fee

The larger the fee, the lower your return

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Bonds – Different from Stocks & Funds

- Bondholders are creditors (lenders) to a corporation or government agency. They are entitled to interest payments and repayment of principal
- Creditors in a bankruptcy have legal priority over stock holders and are made whole first
- Bonds have a fixed duration; they expire on the date specified in the bond
- After the original issuance, bonds are often resold on the secondary market
- Bondholder's Return =
  YTM, or Yield to Maturity (interest payments until bond expiration) + Repayment of principle when bond was issued

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Other Kinds of Investments

Each kind of investment has its own knowledge base

Real estate
Commodities (wheat, cattle, etc.)
Metals (gold, silver, aluminum, etc.)
Collectibles (Art, coins, etc.)

BetterInvesting can help you get started with financial investments, particularly stocks

For other investments, search for impartial sources of information in those areas, and give yourself time to learn and explore thoroughly, just as you should for financial investments.

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FREE, IMPARTIAL FINANCIAL INFORMATION RESOURCES

Library – Value Line Investment Survey
Websites

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Value Line

- The San Jose Public Library subscribes to the Value Line Investment Survey
- You can access it with your SJPL card online 24/7
- VL is a well known, independent source of information about companies
- VL has an online users' guide to help you understand their reports

VL Reports are crammed with information.

What does the company do? (What products/services to they sell?)

- Are their sales (revenue) growing steadily?
- Are their profits (earnings per share) growing steadily?
- Do they have a lot of debt?
- How has the company done lately?
- What does the Value Line analyst think about the company?

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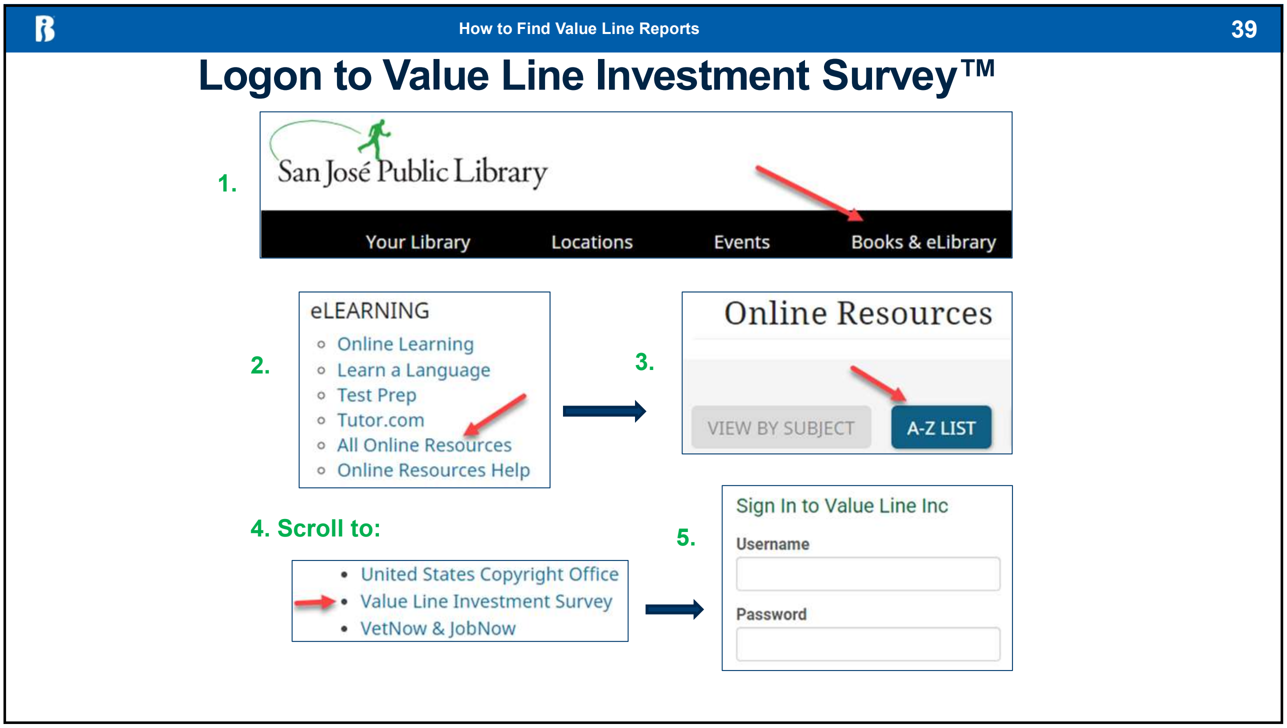
How to Find Value Line Reports
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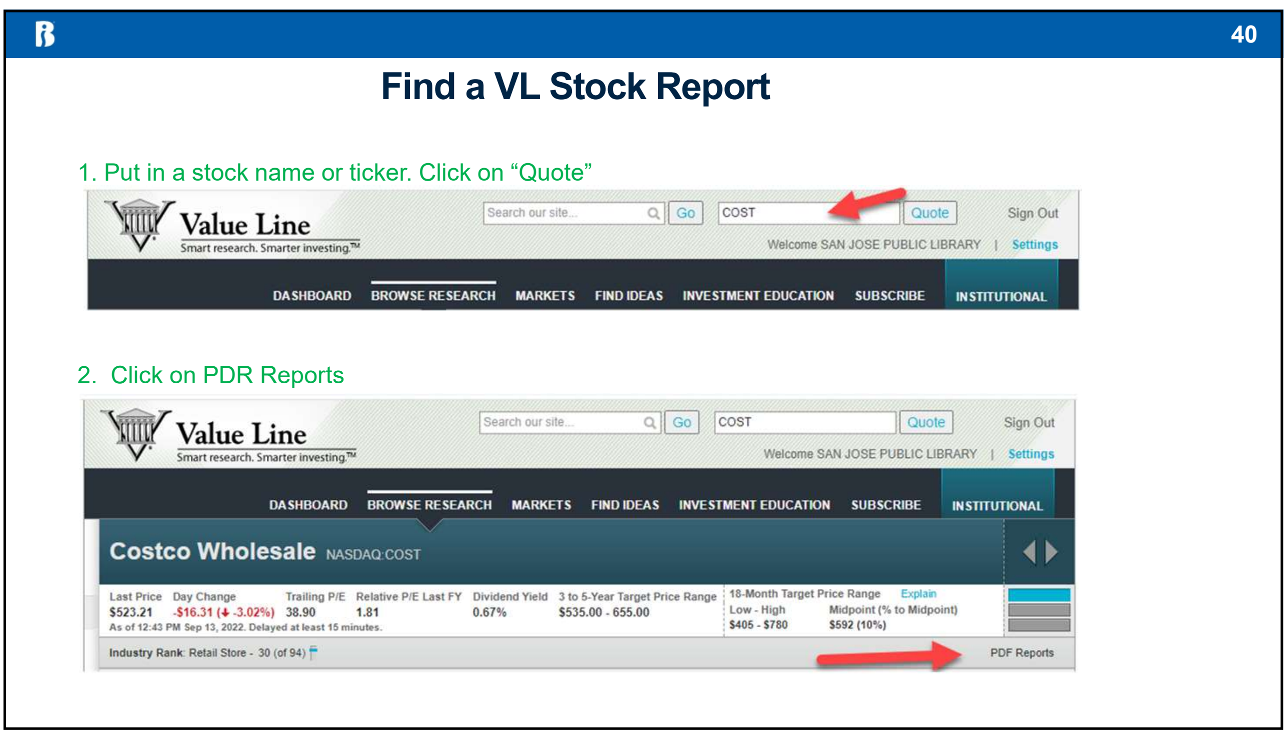
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Costco Wholesale NASDAQ:COST
Last Price $523.21
Day Change -$16.31 (-3.02%)
Trailing P/E 38.90
Relative P/E Last FY 1.81
Dividend Yield 0.67%
3 to 5-Year Target Price Range $535.00 - 655.00
As of 12:43 PM Sep 13, 2022. Delayed at least 15 minutes.
18-Month Target Price Range Explain
Low - High $405 - $780
Midpoint (% to Midpoint) $592 (10%)
Industry Rank: Retail Store - 30 (of 94)
PDF Reports

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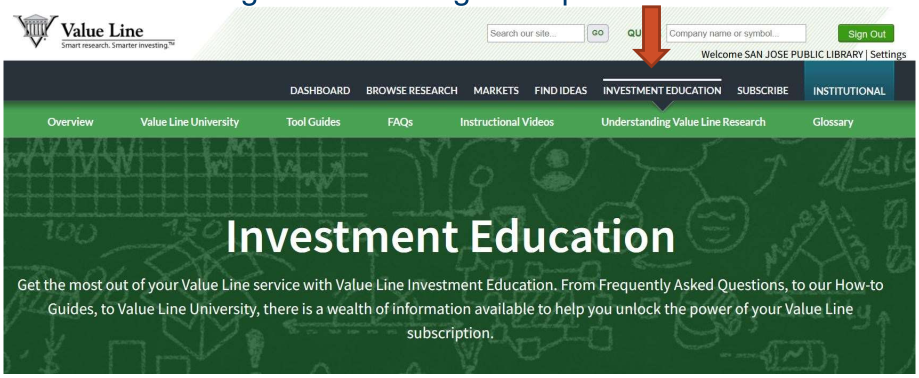
Learning to Use Value Line

The Value Line website has an Education section.
This section includes a guide to reading the reports.



BetterInvesting local chapters also give presentations on using Value Line.

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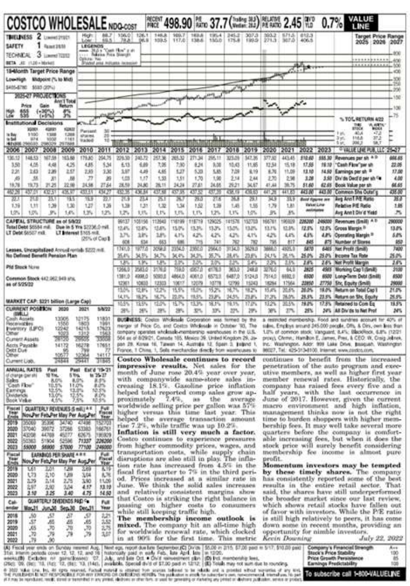
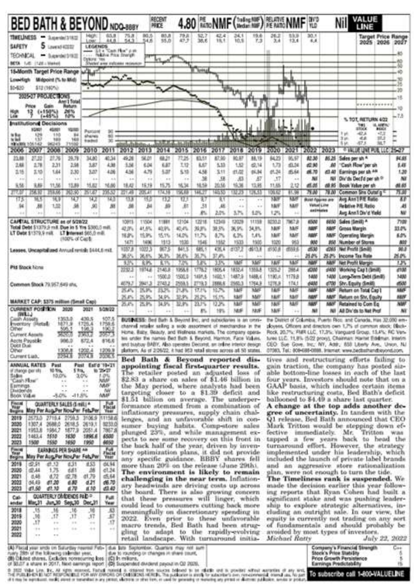
VALUE LINE INVESTMENT SURVEY REPORTS: COST vs BBBY on 7-22-22

Suggestion: Use the Value Line Guide to compare these two companies
One is doing well. One isn't.





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Other Sites for Investor Education and Information

U.S. Securities and Exchange Commission (SEC)

https://www.Investor.gov
Introduction to Investing
Financial Tools & Calculators
Compound Interest Calculator
Information for students, teachers, parents

FINRA

https://www.FINRA.org/investors#/
Financial education, includes section for military members

Other Local Libraries:

Stock and Fund Reports
Morningstar and CFRA Reports
Education

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Advantages of Starting Young

Time is on your side !

Compound interest works longer.
More time to recover from mistakes
Time for investment education while consequences small
Risk is decreased with longer time horizons

Large resources not needed

Small amounts grow with time
At 10% annual compound growth
$25 per month for 40 years = $159,419.51
$25 per month for 10 years then wait 30 years = $90,105.23

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Disadvantages of Starting Young

Limited resources

Less available to invest

long time horizon helps negate this disadvantage

Minors cannot open brokerage accounts

More work to open an account

Adult custodian needed

CUTMA accounts

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CUTMA

California Uniform Transfer to Minors Act

Update to the California Uniform Gift to Minors Act

Became effective in 1985

Adult custodian needed

Income from CUTMA accounts taxable to minor not parents

if minor age > 13 years

At 18 years old CUTMA account belongs to minor

custodian has no legal account control

CUTMA can be used for multiple asset types

stocks and bonds

bank accounts

real estate (unusual, advise consulting an attorney)

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Summary

- Know yourself and your financial goals
- Match short-term and long-term goals to appropriate financial assets
- Compounding works best over many years.
- No need to learn everything at once
- Let information, not emotion, be your guide
- As a start, practice reading company reports such as Value Line Reports
- Fees eat into your CAR
- It's OK to hire financial advisors if they can do a better job
- Use free, impartial investing resources whenever possible

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Question and Comments

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