A Practical Approach to Personal Finance & Investment Fundamentals

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About this presentation:

- Part I – definitions, concepts, terms relevant to Finance & Investment
- Part II – why should we invest?
- Part III – where should we invest?
- Part IV – a few important advise

Definition of Investment

- It is the commitment of money to the purchase of financial instruments (stocks, bonds, checking accounts, certificate of deposits, commodity, currency, real estate, etc.) so as to gain profitable returns in the forms of interest (bonds), dividends (stocks), or price appreciation.
- Most of these activities are taxable.

Diversification

- The reduction of portfolio risk by holding a variety of financial assets.
- In other words, ***<u>DO NOT PUT ALL YOUR EGGS IN ONE BASKET.</u>***

Risk and Reward (Return)

- The lower the risk, the lower the return (Treasury bonds issued by the government).
- The higher the risk, the higher the return (stocks and commodity).
- No risk, no (very low) return (savings).
- 1928-2018: average yearly for stocks – 11%, for bonds – 6%, for certificate of deposits – 3%.

Time Factor

- The sooner you start investing, the better you will be financially in the long run.
- PV = $5,000 @ 8% for n=30, FV = $50,313 ; for n=40, FV = $108,622 ; for n = 45, FV = $159,602
- Annuity: $500 yearly for n = 30 @8%, FV = $56,641 ; for n = 40, FV = $129,528 ; for n = 45, FV = $193,252.
- The sooner, the more frequent, the better.

Inflation & Taxes

- Do not neglect the importance of inflation and taxes to overall portfolio return.
- Real return = nominal return – inflation
- Real return = 10% - 3% = 7%

Let's add taxes

- Real return = nominal return – Inflation – Taxes
- Real return = 10% - 3% - 3% = 4%

- THIS IS THE REALITY.

And don’t forget

- To be always on the lookout for opportunities – remember to buy low and sell high – but not the other way around.
- Stocks, bonds, foreclosed homes, a business, etc…….

Why Should We Invest?

- Financial freedom and security
- Pay for things we want / need, child's education, buy a house, car, etc…
- Plan for retirement – long term objective.
- Average life-span beyond age 65 is 25 for females and 23 for males.
- Do you have enough to live for 20+ more years?

More Reasons to Invest

- Do not rely on social security to pay for your retirement expenses or your lifestyle will be severely reduced.
- Treat social security as a supplemental income to help pay for minor expenses, like food, entertainment, gasoline, etc…

Facts About Social Security

- Social security will be here for you when you need it, but it will not be enough to pay for the lifestyle you desire.
- You will need about 90% of pre-retirement income to maintain current lifestyle.
- Amount received might be reduced due to budget shortfalls or other unpredictable political / economic events the time you are ready to receive it.
- Budget deficits 2018 = $780B ($780,000,000,000) and National Debts as of the end of 2018 = $22T ($22,000,000,000,000).
- Budget deficits 2020 = $3.1T
- National debt as of October 2020 = $27T

Take Care of Yourself

- Invest wisely – start EARLY – and as OFTEN as you possibly can.
- Make social security only as a supplemental income but not as a major source of monthly income.

Where Should You Invest?

- Individual company stocks

- Pros: high return in the long run, good for retirement, control your own taxes. Returns: dividends (not guarantee) and capital appreciation (not guarantee).
- Cons: high risk, lack of diversification (unless you own 35-50 different stocks – where is the money?)

Where else?

- Individual bonds (Treasury and corporate)
- Pros: Regular interest income and potential appreciation
- Cons: Lack of diversification (unless you own a variety of bonds to minimize risk)

- TOTAL LOSS FOR STOCKS / BONDS IF FILED FOR BANKRUPTCY!

Mutual Funds

- A professionally-managed type of collective investment scheme that pools money from many investors to buy securities.
- Has a fund manager or group of managers that (buy / sell) overseeing fund's investment objectives.
- Pros: diversification without sacrificing much risk

Where else?

- For most major corporations – 401(k)
- For public / non-profit corporations – 403(b)
- Individual retirement account (IRA)
- Roth individual retirement account (Roth IRA)

A few investment advise

- Save, save, and then save some more – If you don't put money aside now, you don't have money to invest and you won't have money later on.
- Limit your debts to only two (good) types: mortgages and education. Stay away from credit card debts, auto loans, etc….

More advise

- Invest in age-appropriately manner: age 35 (65% stocks, 25% bonds, 10% cash), age 55 (45% stocks, 35% bonds, 20% cash)
- Maintain a cushion (of cash) – holding cash earns “a pittance,” but you sleep well.
- Use credit card wisely – pay entire balance off each month – use someone else’s money for FREE while building up your own credit history.

Just a few more

- It is ok to live Below your means and be frugal. It is a question of Want vs. Need.
- Do the homework before investing – stocks, bonds, real estate, etc….
- Finally, stick with what you know but not what you are recommended