



MODULE
04

INVESTING:

Money Working for You

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NEFE HIGH SCHOOL FINANCIAL PLANNING PROGRAM

About the NEFE High School Financial Planning Program Series

By picking up this booklet, you are on your way to making your dreams come true and headed down the path to financial independence. This program series includes six topic modules to introduce you to the fundamentals of mindful money management behaviors. Use what you learn in each module to develop sensible habits to confidently manage your money and adapt to unexpected events.

Program Modules

- 1. MONEY MANAGEMENT: Control Your Cash Flow:** goal setting – decision making – spending plan & budget – money management tips
- 2. BORROWING: Use—Don't Abuse:** application process – loans – credit cards – costs – credit score – debt – rights & responsibilities
- 3. EARNING POWER: More Than a Paycheck:** earning potential – career plan – life stages – employee benefits – take-home pay – lifestyle
- 4. INVESTING: Money Working for You:** savings – investing – goals – options – risks & rewards – time value of money – diversification – plan
- 5. FINANCIAL SERVICES: Care for Your Cash:** account types – fees – service options – transaction tracking – automation – identity protection
- 6. INSURANCE: Protect What You Have:** risk management – costs – claims – insurance types – coverage decisions – insurability factors

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Use the tips and strategies in this guide to do the following:

- » Summarize how saving and investing can be used to build wealth.
- » Explain how investing works.
- » Evaluate the risks and rewards of investment options.
- » Outline strategies to achieve investing goals.
- » Explore ways to fit saving and investing into your financial planning.

MEET JUSTIN AND WHITNEY

Justin is an eighth grader who's already worried about paying for college. His older sister, Shelby, won a big basketball scholarship to a state university but lost it after a career-ending knee injury last year.

Their dad isn't working right now because of a job layoff, so Shelby couldn't afford to go back this fall. Justin sees how unhappy she is taking a detour to earn her four-year degree, and he decides to start saving his own money for college.

Whitney is a senior who spends most of the money she earns on clothes, shoes, and going out with her friends. For the past two years, she was supposed to be saving at least 10 percent of her paychecks. One day during an argument over Whitney's spending, her mom asks to see her savings account balance.

Both are shocked to see that there's only a couple hundred dollars in the account. Whitney admits that she skipped saving and withdrew money a couple of times. Her mom shakes her head and walks off in disappointment.



“ Poor people see a dollar as a dollar to trade for something they want right now. Rich people see every dollar as a ‘seed’ that can be planted to earn a hundred more dollars ... then replanted to earn a thousand more dollars. ”

~ T. Harv Eker, author of Secrets of the Millionaire Mind

Do you want to be rich? Who doesn't! But remember: Being wealthy isn't about how much you earn—it's about how much you keep. You can find plenty of stories about superstar athletes and big-name singers who were earning millions but went broke shortly after their careers ended.

You can have the freedom of being financially set for life one day. Anyone can. You do NOT have to be born rich, get straight A's, have talent worthy of a superstar, or make a huge salary. You just need to start thinking about and treating money differently. And the sooner you start, the sooner you may get there.



The wealthy think of money as a 24–7 “employee”—expecting it to make more money for them while they work, play, and go about their daily lives. They do that through saving and investing.

Justin and Whitney will help you get started with saving and investing. In fact, you'll learn that you already have some of the tools and knowledge to get started now.



Activity 4.1: What is Wealthy?

In 25 words or less, define what it means to you to be wealthy.

UNRAVELING THE ‘MYSTERY’ OF SAVING AND INVESTING

“The shortest period of time lies between the minute you put some money away for a rainy day and the unexpected arrival of rain.”

~ Jane Bryant Quinn, author of *Smart and Simple Financial Strategies for Busy People*

When you receive money, the first thing you should do is to set aside a specific amount for financial goals that you can't afford on short notice—like prom, buying a car, or going to college. This “pay yourself first” (PYF) strategy is a way for you to plan ahead to regularly save portions of money over time. Eventually, your PYF fund will grow so you have enough money to later pay for a big-ticket item. (You can learn more about planning for a PYF fund in *Module 1: Money Management*.)

Use some of your PYF money to build an emergency fund so you'll have a financial cushion to fall back on when unexpected things happen. A cushion is especially important because no one is immune from a sudden loss of income due to a job layoff or unplanned expenses such as car repair or replacing a lost cellphone.

An emergency fund also is important if you choose to work in an industry or profession where the amount you earn each month may vary *a lot*—like seasonal work, farming, selling on commission, or running your own business. Not having cash on hand when there are shortfalls can add unwanted stress to your life.

Interest is an amount paid to use someone's money, usually a percentage of the amount deposited (aka **principal**). The bank or credit union will not actually keep all of your money in the vault. Some of it will be loaned to other people or businesses. Because the financial institution receives interest from the borrower, it is able to pay out interest to you for using your deposited money.

Everyone needs to have some money set aside. But if you stash that money in your room, you (or someone else) may be tempted to “borrow” from it. For that reason, keeping your PYF funds “out of sight, out of mind” is a wise route. If you save or invest it, your money can do a lot more for you than take up space in your dresser drawer.

Many people often use the words “saving” and “investing” interchangeably, but technically they're not the same thing.

Saving is setting aside money you don't spend now so it can be used later.

Investing is buying something with the expectation that it will make money for you.

The right choice—saving or investing—depends on your situation. Let's take a closer look at some of the most popular options.

THE BIG SCORE

Savvy people have a strategy in place for **windfalls** such as work bonuses, inheritances, tax refunds, or other unexpected chunks of money. They use them to bump up the amount they're saving and investing. Funneling a windfall in that direction means you get the added boost, with no effect on your day-to-day living expenses.



Activity 4.2: My Windfalls

Have you received any unexpected increases in cash during the past year? Circle any of the examples below that were windfalls for you:

Gift money

Increase in pay

Scholarship or grant

Found money

Tip money

Inheritance

Increase in allowance

Bonus

Other: _____

The next time you have a windfall, decide how much you'll sock away before indulging yourself. You also may need to set aside enough money to pay income taxes on your windfall.

SAVE FOR FUN (AND A RAINY DAY)

The first stop for your PYF money probably will be some type of savings option. When you put money into a savings account at a financial institution, you're basically lending that bank or credit union your money. Your money is used to make loans to other customers and businesses. Also, credit unions and banks are required to keep some money on hand so that customers can take out their money whenever they want to.

Savings options at banks or credit unions offer these features:

- » **Safety.** No need to worry about impulsive spending or theft. Plus your money is insured, so it will be returned if anything happens to the bank or credit union.
- » **Ease of Access.** If you put in \$100, you can take out \$100.
- » **Interest.** The bank or credit union gives you a percentage of the amount that you save. The more money in your account, the more interest you receive.
- » **Easy Tracking.** You can check your balance online anytime.

Popular Savings Options			
Type	Where	Pros	Cons
Savings Account	Any bank or credit union	<ul style="list-style-type: none"> » Low minimum balance requirement » Able to remove or add money to the account » Interest is applied to the account, usually each month or quarter » Insured 	<ul style="list-style-type: none"> » Low interest rates, which may change over time
Money Market Deposit Account (MMDA)	Any bank or credit union	<ul style="list-style-type: none"> » Higher interest rates than with regular savings accounts » Able to remove or add money to the account » Interest is applied to the account, usually each month » Insured 	<ul style="list-style-type: none"> » May limit how many times money can be removed each month » Required first deposits are higher than for regular savings accounts » May require a minimum balance to avoid fees
Certificate of Deposit (CD)	Any bank or credit union	<ul style="list-style-type: none"> » Higher interest rates than for regular savings accounts and MMDAs » Interest rate stays the same for specific length of time » Interest might be applied more often than with savings accounts or MMDAs » Insured 	<ul style="list-style-type: none"> » Low interest rates » Money isn't available until a specific date » Penalties for cashing in CD early
U.S. Savings Bond	Bonds are sold online by the U.S. Treasury at www.treasurydirect.gov	<ul style="list-style-type: none"> » Buy in amounts of as little as \$25 » Fixed interest rate for up to 30 years 	<ul style="list-style-type: none"> » Interest adds up but isn't paid until you cash in the bond » Low interest rate » Penalty if cashed in within the first five years

THE 8TH WONDER OF THE WORLD

Whitney's surprised to hear that her 45-year-old uncle is leaving his job to backpack around the world for a year. He never really seemed like he was rich, so she asks her mom how he can afford to do it.

Her mom says that he has a lot more money than people think. It's not because he earns a lot—he really doesn't. It's because he started saving and investing everything he could when he was a teen. Instead of spending money on big houses, fancy cars, or expensive clothes, he continued to save it for things that are more important to him—like this trip he's been dreaming about for years.

Whitney questions how he could have put that much money away when he was her age. It must have been mostly later, once he was climbing the career ladder. Her mom says no, for years it was just \$25 here and \$10 there. But all the while, his investments and earnings were compounding over time—trickling a little more money into his account at first and then building to a waterfall the longer he left it untouched.

“Compound interest is the eighth wonder of the world. He who understands it, earns it ... [and] he who doesn't ... pays it.”

~ Physicist and theorist Albert Einstein



Investment gurus may have lots of expertise, but you have one HUGE advantage they can only wish for: more time. That's because when it comes to building wealth, **time is much more powerful than the amount you invest and even the return you earn.**



The more often your money is earning interest, the faster and bigger your account will grow—thanks to the mighty power of **compounding**.

Simply leave your savings in your account. As interest is added to the account balance, you earn interest on the original balance plus the previously earned interest. The more frequently interest is compounded, the more the balance increases.

Justin has been saving up his birthday money and some cash he's earned from odd jobs in his neighborhood. He now has \$500 in his savings account with an annual interest rate of 0.55 percent.

He crunches some numbers to see how much his account will grow in a year. Using the simple interest formula, Justin calculates that he will have \$502.75 (\$500 + \$2.75 interest) at the end of a year.

Simple Interest Rate Formula:

$$I = P \times R \times T \text{ where}$$

I = interest

P = principal (the original invested amount)

R = interest rate (decimal number)

T = time (number of years)

Example:

$$\begin{array}{rcccl} \$2.75 & = & \$500 & \times & .0055 & \times & 1 \\ \text{interest} & & \text{principal} & & \text{rate} & & \text{time} \end{array}$$

When interest is compounded, the amount paid in a year is actually more than when the simple interest formula is used to calculate the interest. That's why financial institutions show the return as the **annual percentage yield** (APY), the actual return on an investment when compound interest is taken into account.

Justin's dad suggests putting the \$500 into a CD that earns more interest, more frequently. Their credit union currently offers 2.5 percent APY on a 12-month CD and interest is compounded daily.

Justin uses the compound interest formula to see the difference it makes to have his money earn interest at a higher rate every day rather than just once a year. He discovers that he will have almost \$513 after one year if he goes with the CD option.

Compound Interest Formula:

$$A = P (1 + r/n)^{nt}$$

A = final amount including interest after t years

P = principal (original invested amount)

r = annual interest rate (decimal number)

n = number of times interest is compounded each year

t = number of years the amount is invested

Example:

$$\underset{\text{final amount}}{\$512.66} = \underset{\text{principal}}{\$500} \left(1 + \underset{\text{rate}}{.025} / \underset{\substack{\text{how often} \\ \text{compounded}}}{365} \right)^{\underset{\text{year}}{365} \times \underset{\text{year}}{1}}$$



Activity 4.3: More Money

Justin can increase his savings by compounding interest more often. What are at least two other ways he can grow his savings?



Before you decide where to stash your cash, **always shop around for the best interest rates.** Every little bit of added interest can make a big difference over time. Comparison shop to compare rates at local and national banks and credit unions.

Challenge 4-A: It Pays to Shop Around

Go online to compare options for saving your money. Find out the following about savings accounts, money market accounts, and CDs at one or two banks or credit unions:

- » any minimum balance requirements
- » current APY
- » compounding
- » interest frequency

Use the DECIDE steps to assess the saving option(s) that might be best for your current situation. (You can learn more about the DECIDE Steps in *Module 1: Money Management*. The steps are also listed in the Appendix.)

BEWARE SAVINGS ENEMY NO. 1

Everyone should have savings for short-term and unexpected needs. For long-term goals, however, you need to amp up your earnings because of the inflation bandit.

The **inflation** bandit silently steals your spending power by driving up prices of food, gas, clothes—everything—over time. As it costs more to provide goods and services, those costs are often passed on to consumers. If you use the inflation calculator provided on the U.S. Bureau of Labor Statistics website (www.bls.gov/bls/inflation.htm), you will see that the same items you bought for \$20 in 2005 would cost you \$23.95 to buy in 2013.



The increase in the cost for the same items is expressed as a percentage (aka inflation rate). The historical long-term annual average for inflation is about 3 percent. Even at that growth rate, inflation would **slash the value of your dollar nearly in half every 20 years**. If you stashed \$1,000 in your drawer today, in 20 years it would buy only \$554 worth of stuff (at today's prices)!

When the rate of inflation is greater than the interest rate on your savings, your money may be growing, but it's losing spending power. That means you cannot buy as much with the same dollar later. That's not good over a long period of time.



Is the historical annual average for inflation more or less than the savings APYs you found for Challenge 4-A?

WHEN A DOLLAR IS NOT A DOLLAR

Would you rather get \$100 today or a month from now? Today, of course! For two reasons:

- » You'll save money buying an item now, in case inflation drives up the price over the next month.
- » Waiting a month to save or invest deprives you of a month's worth of returns—which has the potential to help your money grow faster than the rate of inflation over time.

Both reasons reflect the **time value of money (TVM)**, which basically means that a dollar today is worth more than a dollar tomorrow. The shrinking dollar is why investing is a possible way to help you reach your long-term goals. It makes sense to start sooner rather than later to save and invest, so your money can potentially earn more than the rate of inflation.

THE POWER OF NOW

Whitney's intrigued by the fact that her uncle got rich—thanks primarily to compounding interest. She finds a compound interest calculator online and starts playing around with it.

She decides to see what would happen if she invested \$2,000 a year starting now, at age 18, then stopped after 10 years. Using the calculator's suggested annual return of 7 percent, she tells it to calculate what the total would be when she is age 65.



She's shocked at the results, which she shares with her mom. Her mom chuckles and says, "I know. That's why I keep trying to get you to save more money now." Her mom tells Whitney to see what the total would be if Whitney invests the same amount—\$2,000 a year—but doesn't start until she's 31 years old. How much money will she have 35 years later?

Again, Whitney is blown away. Although she contributed 30 percent less money in the first scenario, she ended up having a much higher total amount, thanks to the magic of compounding.



Activity 4.4: Getting a Late Start

As you can see in the chart, after a late start you have to invest more to catch up to the amount in an account started earlier. In Whitney's scenario, what is the cost of starting later to invest at age 31 rather than earlier at age 18?

The Advantage of Starting Early: The Impact of Time on the Value of Money

Whitney Starting to Invest at Age 18 Total Amount Whitney Invested: \$20,000			Whitney Starting to Invest at Age 31 Total Amount Whitney Invested: \$70,000	
7% APR	Year-End Balance	AGE	7% APR	Year-End Balance
\$2,000	\$2,140	18	Starting later to invest \$2,000 annually for 35 years.	\$0
\$2,000	\$4,430	19		\$0
\$2,000	\$6,880	20		\$0
\$2,000	\$9,502	21		\$0
\$2,000	\$12,307	22		\$0
\$2,000	\$15,308	23		\$0
\$2,000	\$18,520	24		\$0
\$2,000	\$21,956	25		\$0
\$2,000	\$25,633	26		\$0
\$2,000	\$29,567	27		\$0
Stopping early after investing \$2,000 annually for 10 years.	\$31,637	28		\$0
	\$33,852	29		\$0
	\$36,221	30		\$0
	\$38,757	31	\$2,000	\$2,140
	\$41,470	32	\$2,000	\$4,430
	\$44,372	33	\$2,000	\$6,880
	\$47,479	34	\$2,000	\$9,502
	\$50,802	35	\$2,000	\$12,307
	\$54,358	36	\$2,000	\$15,308
	\$58,163	37	\$2,000	\$18,520
	\$62,235	38	\$2,000	\$21,956
	\$66,591	39	\$2,000	\$25,623
	\$71,252	40	\$2,000	\$29,567
	\$76,240	41	\$2,000	\$33,777
	\$81,577	42	\$2,000	\$38,281
	\$87,287	43	\$2,000	\$43,101
	\$93,397	44	\$2,000	\$48,258
	\$99,935	45	\$2,000	\$53,776
	\$106,931	46	\$2,000	\$59,680
	\$114,416	47	\$2,000	\$65,998
	\$122,425	48	\$2,000	\$72,758
	\$130,995	49	\$2,000	\$79,991
	\$140,164	50	\$2,000	\$87,730
	\$149,976	51	\$2,000	\$96,012
	\$160,474	52	\$2,000	\$104,872
	\$171,707	53	\$2,000	\$114,353
	\$183,727	54	\$2,000	\$124,498
	\$196,588	55	\$2,000	\$135,353
\$210,349	56	\$2,000	\$146,968	
\$225,073	57	\$2,000	\$159,395	
\$240,828	58	\$2,000	\$172,693	
\$257,686	59	\$2,000	\$186,922	
\$275,724	60	\$2,000	\$202,146	
\$295,025	61	\$2,000	\$218,436	
\$315,677	62	\$2,000	\$235,867	
\$337,774	63	\$2,000	\$254,518	
\$361,418	64	\$2,000	\$274,474	
\$386,718	65	\$2,000	\$295,827	

Investments are assumed to be made annually and at the beginning of the investment period.
Balance amounts are rounded to the nearest dollar and are not adjusted for inflation.

Difference due to starting early: \$ _____



You may not have much money to invest right now. But get it started working for you now and time will more than make up for that amount. The sooner you start adding to an account, the less money you'll need to put into it over time to have it grow into a hefty amount.



How wealthy are you? If you make \$1 million a year and spend it all, you may feel rich. But you're not getting any wealthier—your money is gone. Wealth is what you accumulate—not what you make.

Here's an easy way to measure it: If you stopped working tomorrow, how long could you keep on living your normal life, relying only on what you already have? That's how wealthy you are.

JUMP-START YOUR FINANCIAL QUEST WITH INVESTING

“ You must know the difference between an asset and a liability, and buy assets. If you want to be rich, this is all you need to know. ”

~ Robert Kiyosaki, author of Rich Dad, Poor Dad: What the Rich Teach Their Kids about Money—That the Poor and Middle Class Do Not!

Justin and his 18-year-old brother, Derrick, stop by a movie rental store that's going out of business. They're surprised by how many great movies are priced at next to nothing. Justin gets the idea to buy the clearance-sale movies and sell them at a higher price online.

Derrick asks how he'll pay for them. Justin says he'll use the "just for emergencies" credit card their dad gave him before a class trip last week. Derrick points out that legally Justin's not old enough to sell through online auction sites, so he offers to help him out with the selling part for a "piece of the action." They quickly agree that Justin will give Derrick 15 percent of net profits.

Justin uses the credit card to buy \$200 worth of movies and they head home. Their mom is furious that Justin charged \$200 without even asking. But their dad is impressed with Justin's plan. He says that just as with a real business, Justin must write out an IOU promising to repay the \$200 to his dad in six months plus 3 percent interest. He also says that Justin has to put his agreement with Derrick in writing, giving him 15 percent ownership in the new company.

Basically, Justin's dad and brother just invested in his new business.

ASSETS VS. LIABILITIES

An **asset** is an item of value that can be converted into cash. An asset can put money in your pocket. A **liability** is something owed to another person. Liabilities take money out of your pocket.

A car is an asset. You can sell it for money later. A car loan is a liability—each loan payment is money out of your pocket until the loan is repaid.

When you invest, you buy an asset that you believe will increase in value or earn more money for you, such as a rental property, a business, or stock in a company. Investments are riskier than savings because there's no guarantee that you will earn more than you paid for the assets.

You can lose money with investments if you end up selling the asset at a price that's less than what you paid. On the flip side, however, there is the potential to be rewarded with a hefty increase in asset value. The degree to which an asset gains (or loses) value over a given period of time is called the **rate of return**.

THE INVESTING SEESAW

The higher the rate of return you earn, the less time and money you may need to invest to reach your goals—and vice versa.

For the most part, investments fall into two distinct buckets:

- » **Income investments** provide regular earnings, such as monthly interest, quarterly dividends, or, in the case of real estate, rent payments. They may increase or decrease in value, but overall they tend to provide a steady income. Steady, mostly predictable earnings are the main goal of income investments.
- » **Growth investments** are about delayed gratification. The goal is to buy an asset that you believe has the potential to increase in value over time. You don't receive a dime of any growth in value that may have occurred until you sell the investment. When compared with income investments, growth investments have greater potential to produce bigger gains—and losses.

As you'll see, though, some investments feature both growth and income.

BE THE LENDER

With a **bond**, you lend money to a government or company. In return, the borrower promises to repay you in full on a specific date, called the **maturity date**. The borrower also pays you interest for using your money.

Types of Bonds

Government Bonds

(Issued by U.S. Treasury and other federal agencies)

Municipal Bonds

(Issued by state and local governments)

Corporate Bonds

(Issued by companies)

Let's say you buy a \$10,000 corporate bond with a 5 percent annual interest rate and a maturity date 10 years away. Twice a year for 10 years, you'll receive interest payments of \$250. And on the maturity date, you'll get your \$10,000 back. In the scenario about Justin's DVD resale company, Justin's dad basically bought a corporate bond. It pays 3 percent interest and will mature in six months.

Here's what you should know about bonds:

- » Bonds typically are sold for \$1,000 each, which is called the **face value**.
- » The interest rate you receive is fixed (doesn't change) and depends on the overall rate that's current when you buy the bond.
- » You can sell a bond to someone else before its maturity date.
- » Bondholders are much less likely than stockholders to lose money.
- » Even if a company goes bankrupt, investors holding its bonds are considered creditors, who by law must be repaid first through the bankruptcy settlement. The company's stockholders may get only a fraction of their investment back, if anything.

How to Buy Bonds: You can buy bonds from investment brokers. You'll probably have to pay the broker a fee for each transaction. The least costly way to buy U.S. Treasury bonds is directly from the government at **www.treasurydirect.gov**.

PICKING A BROKER OR ADVISOR

You buy stocks and bonds through a registered **broker**. When you want help in making investing decisions, you can seek advice from an **investment advisor**. The difference is that the broker helps you carry out investment transactions. An advisor provides advice to guide your investing strategies. Do your homework before selecting a broker or advisor by asking these questions:

- » Do the broker's or advisor's credentials check out?
- » How much will the services cost?
- » Do you trust that the broker or advisor will act in your best interests?

A SHOE-IN AT INVESTING

When 6-year-old Damon Williams asked his mom for the newest style of Nike Air Jordan shoes, his newly single mother put down her foot. She said that if he wanted another pair, he had to save up his money to buy them.

She also said if he was going to keep buying Nike shoes, he was going to own a piece of the Nike company. So, he also had to buy a share of the company's stock.

By age 18, Damon had a stock portfolio worth \$55,000. He did it by investing a little at a time in stable, growing companies. He holds his stocks at least seven years. And when stock prices fall, he purchases more shares at the lower prices.

"Anybody can do this. It's not just for the rich people," he says. "I want to pay my own way through college, buy real estate, and see my children graduate from college also."

STOCK UP OVER TIME

Like Damon Williams, you may be able to make money by investing in your favorite companies instead of just spending all your money buying their products!

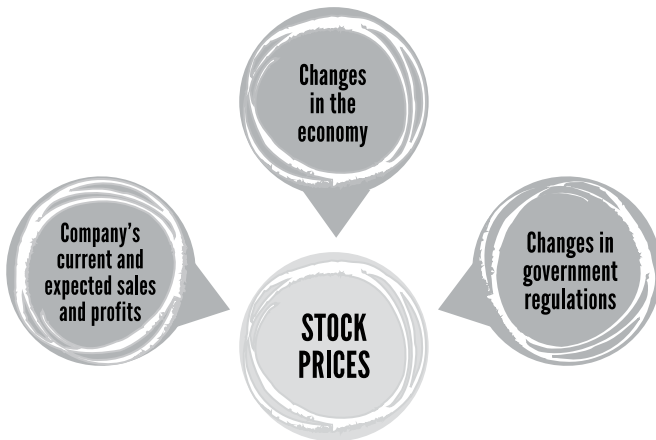
Buying **stock** gives you a front-row seat to the potential growth—and a piece of the possible profit—of some of the world's greatest companies. When you buy stock, you are providing money to a company to use to run the business.

In Justin's scenario, he essentially issued Derrick 15 shares of stock (assuming 100 shares total). He'll pay Derrick 15 percent of the company's net profit—however much or little that may be.

Here's the scoop on stocks:

- » Owning stock makes you a **shareholder** (aka stockholder). The more shares you own, the more of the company you own.
- » Stock prices constantly fluctuate. Ideally, you want to sell stock at higher prices than you paid, so you can make a profit.
- » There's no guarantee that you'll make money with a stock. You could break even or lose money. Historically, the long-term growth of businesses and their stocks has outpaced virtually every other non-stock market investment. But keep in mind that how a particular stock performed in the past doesn't ensure that it will perform that way in the future.
- » When a publicly owned (by stockholders) company makes a profit, the management might decide to give part of the profits to the shareholders. Shareholders receive a **dividend**, an amount paid in cash or shares of stock, based on the amount of stock shares owned.
- » Being a shareholder comes with responsibility. You get one vote per share in elections of the board members who oversee the company's management.

Some of the factors that may affect a stock's price:



How to Buy Stock: You can buy shares of stock through a registered broker. Or, you can use an online discount stock brokerage firm, which has no minimum purchase. Online brokerages usually charge a flat fee per trade, but there may be other fees and costs as well.



Activity 4.5: Own a Piece of the Business

The companies listed below offer stock you can purchase. Circle the names of the companies you would like to own as a shareholder:

Amazon

Google

Hershey

American Eagle

Electronic Arts

Nike

Apple

GameStop

Pixar

Coach

Harley-Davidson

Target

A **security** is any type of investment bought and sold through financial markets. Examples include stocks, bonds, and minerals.

THE FOGGY CRYSTAL BALL

Stocks are listed for sale on **stock exchanges**, systems established to trade shares of stock. The New York Stock Exchange (**NYSE**) and National Association of Securities Dealers Automated Quotation System (**NASDAQ**) are the two major players in the U.S. For every trade on the exchanges, there is a buyer and a seller for the transaction.

Most North American securities are traded through whichever one of these exchanges they are listed on. The main difference between the NYSE and the NASDAQ is in how trades are made.

NYSE trades are made in a physical auction-style market in New York. When you place an order through a broker to buy a particular stock, your offer to purchase (**bid**) is matched to a seller's offer to sell (**ask**). Both the bid quote and ask quote list the quantity of stock at a certain price. For example, you can make a bid to purchase 100 shares of stock at a price of \$15 per share. If a seller is willing to

accept your offer, a trade is made. You now own stock. You can later offer to sell that stock at a different ask quote, say 100 shares at \$18 per share. If someone is willing to buy at your ask quote, you can complete the transaction for a gain.

The NASDAQ is not a physical place. Rather, all trading is done through a telecommunications network of investment companies. Your bid or ask order will be handled through an investment company dealer who keeps an inventory of securities on hand to sell. When your bid matches the ask quote, you will make the trade through the dealer. In reverse, when you want to sell stock, the trade will be completed when the dealer buys at your ask quote.

A stock price reflects what the overall market thinks the company is worth at the moment. When the company looks highly promising to investors, the value of the stock might climb. That's because more people want to own the stock, and the increased demand pushes up the price. When the company struggles, its stock prices tend to fall as more and more stockholders want to sell their shares.



Activity 4.6: Watch the Price

Select two or three companies that are interesting to you because you use their products. Look online or in a newspaper to find out the highest and lowest selling prices over the past 52 weeks for each company.

Company	Highest Price	Lowest Price



If anyone promotes a “foolproof system” for predicting stock prices, be very skeptical. No one yet has found the perfect crystal ball to predict prices—and it’s unlikely that anyone ever will.

A study of the stock market’s 120 biggest up and biggest down days over the course of 200 years found that only 25 percent of the market swings happened for a logical reason.¹ The other 75 percent were completely unexplainable!

MORE OWNERSHIP PATHS TO POTENTIAL WEALTH

Owning stock isn’t the only way to invest. Here are some other popular options:

► **Mutual Funds.** Each mutual fund invests in a variety of stocks and/or bonds to meet a specific investment objective—income or growth, among others. Individual investors then buy shares of the fund.

Advantages of this approach include the following:

- » A professional fund manager does all the work of researching investment opportunities and conducts the actual buying and selling.
- » A one-stop investment in many companies is less risky than owning shares in just a few.
- » Buying shares of a fund is more convenient than investing on your own in all the companies included in a fund’s holdings.
- » Earnings are automatically reinvested for you, which increases the number of fund shares you own.

How to Buy Mutual Fund Shares: Go to a broker, the website of your favorite mutual fund company, or an online brokerage. Minimum investments can be as low as \$500. Always find out about commissions and expenses, which can vary widely.

¹*Stocks for the Long-Run: The Definitive Guide to Financial Market Returns and Long Term Investment Strategies*, Jeremy Siegel, 2007



► **Real Estate.** Real estate investing focuses on buying land and buildings such as rental properties, office buildings, farmland, and more. It's possible to earn both income and growth rewards with real estate investments. For example, with rental property you collect monthly rent payments (income). Later you might sell the property for more than you paid for it (growth).

The major downsides are that real estate isn't cheap, it may take a long time to attract a willing buyer when you're ready to sell, and there's no guarantee that the property value will increase over time. Also, while you're making mortgage/loan payments, you're responsible for annual property taxes, insurance, maintenance, and repairs.

Unlike with stock values, you have some control over a property's value. You can choose a unit in a good location and one that's in good condition. You also can make improvements that may increase the property's value.

How to Buy Real Estate: Real estate typically is sold through an authorized agent. Besides the purchase price, you pay a variety of fees and closing costs.

► **Collectibles.** Collectibles are rare or highly desired items that you believe will increase in value over time. Paintings, coins, comic books, and baseball trading cards are a few examples. The rarer the collectible is—and the better its condition—the more it's worth to prospective buyers.



You don't make a dime on your investment until you sell the collectible, though. Your buyers are limited to other collectors, and prices depend on their whims. In some cases, collectibles require special storage and insurance, which add to your costs.

How to Buy Collectibles: You can find collectibles nearly anywhere, including your own attic. Before you buy from others, research how to spot fakes and reproductions so you don't get ripped off.

► **Start Your Own Business.** While stocks may make it possible for you to profit from the success of other people's companies, starting your own business means all the profits go to you. As a person who takes the risk of starting and running a company (aka **entrepreneur**), you have to pay all the expenses and put in all the hard work. Launching a business is not without risk—the failure rate for startup businesses is high.

On the other hand, the potential rewards are unlimited. Build it and grow it right, and later you may be able to sell your business at a profit—or pass it on to your kids.

How to Start a Business: You need an idea, a plan, and some development money to get started. The Small Business Administration (www.sba.gov) and SCORE (www.score.org) offer helpful, free information for aspiring entrepreneurs.

RISKY BUSINESS

Six months have flown by. It's time for Justin to repay the bond his dad bought in his business. He also needs to pay Derrick the 15 percent net profit. But sales have slowed and he hasn't been good about managing his money. So, he doesn't have enough to pay them both.

He asks his mom what to do and she calls a family meeting. His dad explains that Justin doesn't have a choice. In the real world, bondholders must be paid before the stockholders. Derrick starts to protest but his dad reminds him that he took the extra risk of being a stockholder, with the expected tradeoff of getting a higher return. If Justin really can't pay, Derrick will just have to deal with it.

Derrick asks for the notebook in which Justin was logging all the sales and expenses. He sees that Justin stopped updating it two months ago. So, he asks for a printout of the transactions in their payment account. Justin gets angry and refuses. His dad explains that as a stockholder, Derrick is entitled to see the company's financial records.

Justin prints it out and waits for Derrick to go ballistic about the bunch of video games Justin bought for himself last week using company money. Derrick criticizes him for spending the company's money instead of making good on his responsibilities. Justin argues that Derrick shouldn't get mad at him, because Derrick failed to keep an eye on his investment.

Justin agrees that from now on he'll show Derrick the notebook and payment account statements every month. In the meantime, Justin needs to pay his father the \$200 plus 3 percent interest as promised. Then, he'll write his dad a new IOU for \$200 to buy more movies. But because his investment seems riskier than before, Justin's dad now wants 5 percent interest on the new bond, which will be due in another six months.

“ You can measure opportunity with the same yardstick that measures the risk involved. They go together. ”

*~ Personal development pioneer
Earl Nightingale*

THE INVESTING STRESS TEST

Risk is the uncertainty of achieving a desired result. It's part of everyday life. Just as there are no guarantees that someone you ask out will say yes or you'll make the team, there are no guarantees that your investments will make money. The greater the risk, the greater your potential loss—and the greater your potential reward.

All investments involve some degree of risk. To make informed investment decisions, you'll need to identify those risks and gauge your willingness to accept them.

No one enjoys losing money on an investment, but some people stress about it more than others. How comfortable you are with the ups and downs of investing is called your **risk tolerance**. Knowing your risk tolerance is crucial to choosing the right investments for you.

Match Your Risk Tolerance			
Tolerance level	Low	Medium	High
Investor's Behavior	Loses sleep whenever investments decline in value	Doesn't fret over small declines but stresses about bigger ones	Not bothered by ups and downs; just wants to maximize returns over the long term
Possible Investments to Consider	Savings Account MMDA CDs	Stocks of large, established, financially healthy companies; mutual funds that balance stock and bond holdings	Sophisticated, higher-risk investments and startup companies



Activity 4.7: My Risk Tolerance

How would you rate your risk tolerance? Rutgers University has developed a quiz to help you determine your comfort level with risk: (njaes.rutgers.edu/money/riskquiz).

My investment risk tolerance: _ _ _ _ _

Here's the curveball: **Your risk tolerance changes** as your investment goals, financial situation, and life experiences change. Generally, the longer the length of time until you need your money, the more risk you can afford to take.

For instance, your risk tolerance is probably highest for investments you've chosen to help you meet faraway financial goals, like retirement. That's because you have many years for your investments to potentially recover from any drops in value. For closer goals, like college, you may prefer less-risky, steadier investments.

Bottom line: There's no "right" risk tolerance to have. You should never take on so much risk that you lose sleep over your investments. Only you can decide how much risk you're comfortable with.

VARY YOUR ASSETS

How many times have you heard that you should apply to more than one college or for more than one job? The idea is that applying to a variety of places improves the likelihood of a positive outcome. The same thinking is behind the familiar saying, "Don't put all your eggs in one basket." If the basket breaks, you could lose all of your eggs.

In a way, when you fill out multiple college or job applications, you're practicing **diversification**. In investing, that practice is an important risk-reducing strategy. Having a variety of diverse investments is less risky than having too few investments or too many similar ones.



Having a mix of different types of investments helps to boost your odds of having at least one type that's performing well.

Here is how you can diversify your investment portfolio:

Invest in a combination of asset categories:

- » Invest in more than one asset. Imagine what would happen if your only investment was stock in a company that failed.
- » Invest in a variety of investment assets such as interest-bearing savings, stocks, mutual funds, bonds, and real estate.

Mix investments within an asset category:

- » Avoid investing in only one industry. Investing in different industries can balance your risk in times when one industry struggles and another performs well. You would have been disappointed to own stock only in Internet companies (aka dot-coms) during the 1990s as the prices of tech-industry stocks plummeted.



- » Vary your investments to include stocks of different-sized companies.

Broad-market mutual funds are a way to own stock in a wide range of companies of different sizes and industries.

CHOOSE SMART

Tips From Celebrities Who Invest

Singer/songwriter Justin Bieber	"I'm not going to invest in something I don't like. I have to believe in the product."
Rapper and record producer Jay-Z	"You know, music is like stocks, too. There's the hot thing of the moment. There's this hot, electro sound ... or the hot whatever's new and exciting. People tend to make emotional decisions based on that. They don't stick with what they know ..."
Entertainer, media mogul, and philanthropist Oprah Winfrey	"I don't invest in anything I don't understand—it makes more sense [for me] to buy TV stations than oil wells."

Inspired by her uncle's story, Whitney texts him and asks if he knows any hot stocks she can invest in. She says she needs to double or triple her small savings account in the next year before college.

He says he'd be happy to talk to her about investing, but her goal isn't realistic. He explains that it takes time for investments to grow. That's why he holds on to stocks for at least five years. To make the kinds of returns she wants in a year, she'd have to take some crazy risks and get wildly lucky to make it happen. She's more likely to lose a bunch of money instead.

He says that if Whitney wants to start investing, he'll teach her what he knows. He suggests that she start by investing 10 percent of each of her paychecks in stocks of some stable but growing companies. But the rest of her money should probably go into a CD that pays an interest rate that's both higher than what her savings account pays and compounded more often. Whitney agrees to look for a CD, and they set up a time to talk after her next payday.

8 MUST-ASK QUESTIONS BEFORE YOU INVEST

Before you choose an investment, you need to ask yourself:

1 What's my financial objective? What do I plan to do with the money? When will I need it? The answers will start narrowing down your options.

2 What's my risk tolerance? How upset will I be when my investments hit a rough patch?

3 Am I ready to hold the investment for a while? Investing is a long-term relationship. Successful investors stick with their choices for five, 10, 20, or more years. These buy-and-hold investors outperform short-term investors by a wide margin—with 62 percent higher returns.²

4 Do I understand what I'm buying? If you don't understand the company's products or services and how it makes money, don't invest in it.

5 What's the outlook? Are there trends that could boost or dampen demand for a company's products and services over the next decade? Does the company itself have any issues that could affect future sales and profitability?

²"Trading is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors," *Journal of Finance*, February 2000

6 Is this a good (or too good) price? How does the current price compare with its past prices and with similar investments? And if it seems to be a bargain, why is it so low? Something that seems too good to be true probably is.

7 What are the costs? Check out fees, commissions, loads, and expenses. The more costs you pay to acquire the asset, the less money you make. Everyone who sells investments gets paid somehow, usually in several different ways. Know what they are.

8 Why am I buying it? If you can't answer that question, you shouldn't buy it.

UNDER AGE? NO PROBLEM!

If you're not yet an adult according to the law in your state, you can't legally hold stocks, bonds (except U.S. Savings bonds), and other investments. Instead, a parent or guardian can set up a **custodial account** for you at a brokerage or mutual fund company. The assets in the account belong to you, but you won't have legal control of them until you're no longer a minor.

STEER CLEAR OF TROUBLE

Do your homework before investing so you feel comfortable with your decisions. Keep in mind these guidelines:

» **Avoid trusting others blindly.**

It's YOUR money that's at stake. Think for yourself and research the expertise of anyone offering advice before you follow it.

» **Avoid falling for fairy tales.**

It can't be said often enough: If something sounds too good to be true, it probably is. Red flags should go up if anyone promises a big return on an investment.

» **Avoid relying only on past performance.** Choosing investments solely on past performance is like driving using only the rearview mirror. The economy changes; management changes. Past performance is an achievement, not a predictor of what will happen in the future.

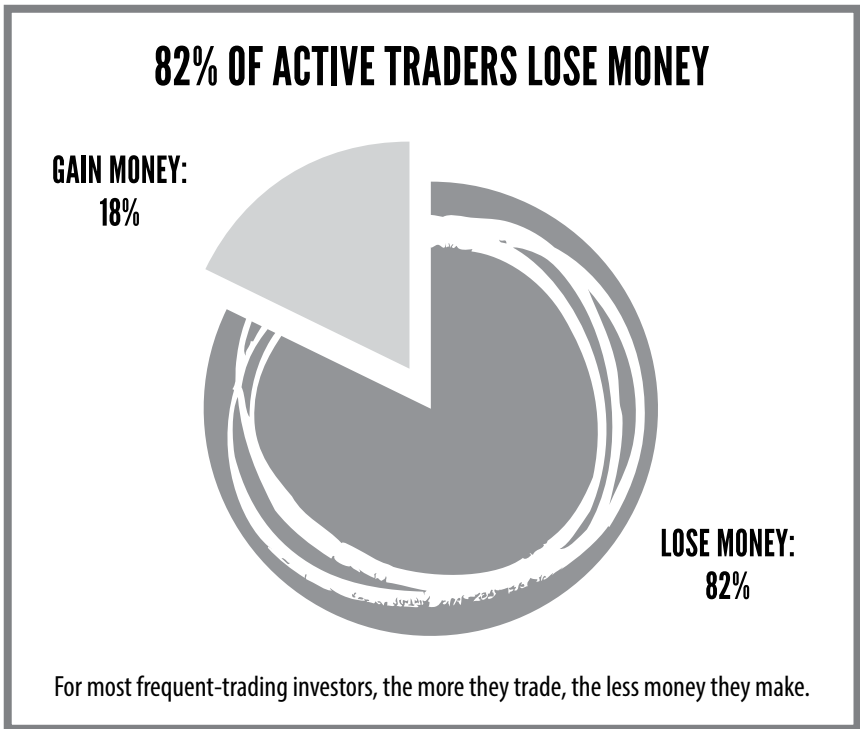
» **Avoid borrowing to invest.** If your investment goes bust, you've lost your money and may not be able to repay the lender. Be aware that lenders can demand early repayment when investments decline in value by a specific amount.

» **Avoid holding only one investment.** Diversify your portfolio. Many pros have a rule of not investing more than 5 percent of their total portfolio in a single company or industry.

“When emotions run high, logic usually flies out the window, and performance usually follows.”

~ John Bogle, founder of Vanguard Funds

- » **Avoid flipping stocks.** Trying to “beat the market” by frequently buying and selling your stocks is a losing proposition. Researchers found that a whopping 82 percent of daily traders lose money thanks to bad stock picks and the costs of all those trades.³



- » **Avoid getting emotional about your investments.** Come up with a strategy to select investments that meet your financial goals. Having a plan and sticking to your plan can help you avoid making impulsive decisions to buy or sell an asset.

³ Do Individual Day Traders Make Money? Evidence from Taiwan, May 2004, faculty.haas.berkeley.edu/odean/papers/day percent20traders/day percent20trade percent20040330.pdf

TOOLS OF SUCCESSFUL INVESTORS

Before you make your first investment, you'll want to know about two ways to get off to a good start for the long term.

WIN LIKE THE TORTOISE

Dollar cost averaging is a fancy phrase for investing a set amount of money each month or at other regular intervals. It's a particularly handy strategy when you're starting out, because it doesn't matter if the amount is big or small. What matters most is that it's consistent.

Benefits of dollar cost averaging include:

- » **Being able to start tapping the mighty power of compounding to grow your money right away.** You skip the frustration of waiting to save up a sizable lump sum to invest.
- » **Eliminating worries about whether you're investing at the "right" or "wrong" time.** Simply put, your investment buys more shares when prices are lower and fewer shares when they're higher.
- » **Lowering the cost per share.** For the investment period, the average price you pay per share will always be below the overall average cost per share.



Set up a regular investing routine. You can arrange for regular automatic withdrawals from your paycheck or checking account to a brokerage firm so you don't even have to remember to do it!

“Your ultimate success or failure will depend on your ability to ignore the worries of the world long enough to allow your investments to succeed.”

~ Peter Lynch, former mutual fund manager at Fidelity Investments



Activity 4.8: Dollar Cost Averaging

Whitney decides to invest \$50 in Rockstar Mutual Fund every month. Here's a break-out of the transactions for a year:

Date of Investment	Amount of Investment	Cost Per Share	Number of Shares Bought
Jan. 5	\$50	\$15.23	3.28
Feb. 5	\$50	\$16.70	2.99
Mar. 5	\$50	\$16.04	3.12
April 5	\$50	\$14.63	3.42
May 5	\$50	\$13.11	3.81
June 5	\$50	\$12.84	3.89
July 5	\$50	\$10.79	4.63
Aug. 5	\$50	\$11.24	4.45
Sept. 5	\$50	\$11.97	4.18
Oct. 5	\$50	\$14.52	3.44
Nov. 5	\$50	\$16.87	2.96
Dec. 5	\$50	\$16.45	3.04

\$_____ By year's end, what is the total amount Whitney paid for the fund shares?

\$_____ How many shares does Whitney own at the end of the year?

\$_____ What is the value of Whitney's fund on December 5?

\$_____ What is the average price Whitney paid per share?

\$_____ Using the costs shown, what is the overall average cost per share for the 12-month period?

RETIRE THOSE TAXES

Retirement probably seems eons away for you right now. But when you finally retire, you could need enough income to support you for three decades—maybe longer. How will you afford it? Retirement plans are designed to help you invest for your distant future. They offer tax advantages and other attractive incentives.

Here are two plan types to get to know:

401(k) Plans. A 401(k) plan is known as an employer-sponsored plan, but you own your account. You decide the amount to contribute and how it's invested. In some cases, your employer will match what you contribute, which is an added benefit to help you build your account.

Individual Retirement Accounts (IRAs). Outside of work, you can invest for long-term goals, while getting the benefits of tax-free growth and compounding, within IRA accounts. There are several types of IRAs, each offering some type of tax advantage. If you need money well before retirement, a Roth IRA allows you to withdraw money for higher education without the 10 percent early-withdrawal penalty. You must have held the account for five years, though, and you'll have to pay taxes on any earnings.

ADDING IT UP

Overall, you've learned how to use saving and investing to help you reach your goals—even if you're just building your wealth a little at a time. You've learned about the important role that time, money, and returns can play in your efforts to achieve your financial goals and dreams.

Both Justin and Whitney are ready to sit down and create a roadmap to a richer future. Now it's time for you to start putting what you learned into action. First, you need to set some SMART saving and investing goals to help your dreams become a reality.

Challenge 4-B: Set My SMART Investing Goals

Use the SMART goal guidelines to set your own saving and investment goals. If you completed Challenge 1-A in *Module 1: Money Management*, review your SMART financial goals for this challenge. (Look for the SMART Goal Guide in the Appendix or online at www.hsfpp.org.)

If you have more than one goal, rank them from most to least important so you know where to focus if you can't tackle them all right now.

Each time you save or invest, you choose to apply your money toward longer-term goals rather than buy things you want right now. Remember these seven practices as you set up an investing plan:

- 1 Develop a strategy** to match your financial goals.
- 2 Start now** to benefit from the time value of money.
- 3 Invest for the long term.** Take advantage of compounded earnings.
- 4 Invest regularly.** Use the dollar cost averaging strategy.
- 5 Diversify** by owning different types of assets.
- 6 Do your homework.** Select options that match your goals and risk tolerance.
- 7 Monitor your investments** and make adjustments as your life situation changes.

Challenge 4-C: DECIDE My Investment Plan

Now, use the DECIDE steps to choose the right investment route for you. (You will find the steps listed in the Appendix or go online at www.hsfpp.org to get the DECIDE guide.)

APPENDIX – MONEY MANAGEMENT AIDS

SMART Goal Guide

Goal Setting

S**Specific****M****Measurable****A****Attainable****R****Relevant****T****Time-Bound**

Stop, Drop, and Think Before You Buy Test

- » Do I need this or do I want it?
- » If I don't need it, why do I want it?
- » Exactly when will I use (or wear) it?
- » Can I find it for less somewhere else?
- » What will I have to give up or put off by buying this now?

DECIDE Steps

- 1 Define what you want to achieve.
- 2 Establish your must-have and nice-to-have criteria.
- 3 Choose a few options that match your criteria.
- 4 Identify and compare the pros and cons of each option.
- 5 Decide the most logical option for your situation.
- 6 Evaluate the results and make adjustments for next time.

Financial Planning Process

Analyze your values, money management habits, and your financial situation.



Set SMART financial goals.



Plan what needs to be done with checkpoints and plan strategies to cope with unexpected events.



Carry out your plan and track your progress using systems that work for you.



Monitor and reflect on your progress; adjust your plan as your situation changes.

Additional NEFE Resources for Teens and Young Adults

Entering the Real World

www.onyourown.org

Just starting out on your own? This blog can help! From lessons learned with real people to money tips, strategies, and options, On Your Own supports you on your path to financial independence.

Prep for College or Workplace

www.cashcourse.org

CashCourse is a website that can help you prepare financially for college or the workforce. It includes worksheets, calculators, and an easy-to-use Budget Wizard to help you manage your money.

Spending Habits

www.spendster.org

Spendster is a YouTube™-like website that showcases people's stories of impulse buying, overspending, or just plain wasting money on stuff they don't need. Watch their video confessions, and then submit your own spending story.

Money Management Tips

www.smartaboutmoney.org/40moneytips

What are the *40 Money Management Tips Every College Student Should Know?*

Find out by downloading this booklet and learning how to stretch your financial resources, whether you're just starting out on your own or heading off to college.





HIGH SCHOOL FINANCIAL PLANNING PROGRAM

“Start saving early because it pays off well the earlier you start.”

Student ~ 2010

This **NEFE** program will equip students in Grades 8-12 with fundamental personal finance skills to prepare them for financial independence and mindful money management decisions and behaviors.

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