Lesson 5: What to Buy

Lesson Objectives: By the end of this lesson, you should be able to:

- explain the three-step investment process

Lesson Summary:

This lesson discusses a three-step process to get started on your investment plan.

- **Step 1: Determine your risk level.** Simply subtract your age from 100. The answer is how much of a percentage of your portfolio should be in growth investments, with income investments covering the rest. Do this every year and rebalance.

- **Step 2: Dollar cost average.** Choose an amount you will invest every month and set up an automatic plan to have that money transferred from your paycheck or checking account.

- **Step 3: Set up an account and buy something.** Your local bank or financial company can help you set up an investment account. If you are employed, ask Human Resources for information on your company's retirement plan.

Review Questions:

- What if you set up an investment account but want to change something? Are you locked in?

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Homework Assignment:

Write your investment plan by answering three questions:

1. What is your risk level?
    a. Write your age here: _________________

b. Subtract from 100: __________________
c. The answer is the percent of investments in growth: __________________
d. Your age = amount of investments in income investments: __________________

2. How much will you invest monthly? ___________________ (Even if it is one dollar, write something down.)

3. Choose one bank or financial company you will talk to within the week about opening a retirement account: _____________ Even if you are deep in debt and don't have a dime to your name, choose a company and call them; discussions are free but valuable.

Class Activity:

Do a sample rebalancing activity as a class.

- Imagine in 2007, a 50-year-old woman had $50,000 in growth investments and $100,000 in income investments. The growth investments have done well due to the strong stock market of the previous few years. However, based on her age, she needs to rebalance. What should she do?

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- In 2008, the market drops considerably, and her new portfolio is $75,000 in income investments and a sad $32,000 in growth products. Her portfolio is again out of whack, only this time in the other direction. What should she do?

Additional Information:

www.yahoo.com: Here you will find a great and free financial site for quotes and research about stocks.

www.irs.gov: This is the official website of the Internal Revenue Service, and it provides easily accessible information on Roth IRAs and other retirement accounts.

www.magicformulainvesting.com: If a student is really interested in investing, this website is a great start. It was created by Joel Greenblatt, author of *New York Times* bestseller *The Little Book That Beats the Market*.

Fun Facts:

It is important to review your investments periodically, as things do change. Before 1997, the Roth IRA did not exist. The Dow Jones Industrial Average began in 1896, with 30 companies in the index. Today, only one of those companies is still there, General Electric.

Notes:

Sample Retirement Account Portfolios

These portfolios are merely samples. Research to find out what is comfortable for you. Some people prefer to take on greater risk, hoping for greater reward. Others are more cautious and hesitant. The most important thing is to start, then stick with it and be consistent.

Age: Under 25 years

- **Risky: 75%**
  - 20% U.S. stock index funds
  - 20% foreign stock index funds
  - 20% real estate index funds
  - 15% natural resource index funds
- **Safe: 25%**
  - 10% guaranteed funds
  - 5% money market funds
  - 10% income funds

Age: 26-35 years

- **Risky: 70%**
  - 20% U.S. stock index funds
  - 20% foreign stock index funds
  - 20% real estate index funds
  - 10% natural resource index funds
- **Safe: 30%**
  - 12.5% guaranteed funds
  - 5% money market funds
  - 12.5% income funds

Age: 36-45 years

- **Risky: 60%**
  - 17.5% U.S. stock index funds
  - 17.5% foreign stock index funds
  - 17.5% real estate index funds
  - 7.5% natural resource index funds
- **Safe: 40%**
  - 15% guaranteed funds
  - 10% money market funds
  - 15% income funds

Age: 46-55 years

- **Risky: 50%**
  - 15% U.S. stock index funds
  - 15% foreign stock index funds
  - 15% real estate index funds
  - 5% natural resource index funds

- **Safe: 50%**
  - 20% guaranteed funds
  - 10% money market funds
  - 20% income funds

Questions to Ask When Opening a Stock Brokerage / IRA Account

- **What is the minimum amount of money I need to open an account?** Depending on the company, this will be somewhere between $500 and $2,500. Often, companies waive this minimum if you agree instead to contribute $25 to $50 through a monthly withdrawal from your bank account.

- **Can you tell me all the fees associated with this account?** These will vary, but when in doubt, lean toward lower fees. These include:
  - **Annual maintenance fee:** ($25-100)
  - **Commissions:** to buy stocks ($7.50 to 5 percent of the amount of the transaction). Don't worry too much about this because to start we aren't buying stocks but mutual funds.
  - **Loads on mutual funds:** Do not pay these! They are commissions to buy mutual funds. Most companies have both load and no-load funds, so choose the no-load options.

- **Can you tell me about customer support?** All companies should have a toll-free number and customer support during business hours.

- **What is your website?** Once you have the link, browse their website. If it is not easy to use, find another company. Remember that some company websites are loaded will all sorts of doohickeys for serious stock investors, and they can be cluttered and cumbersome.