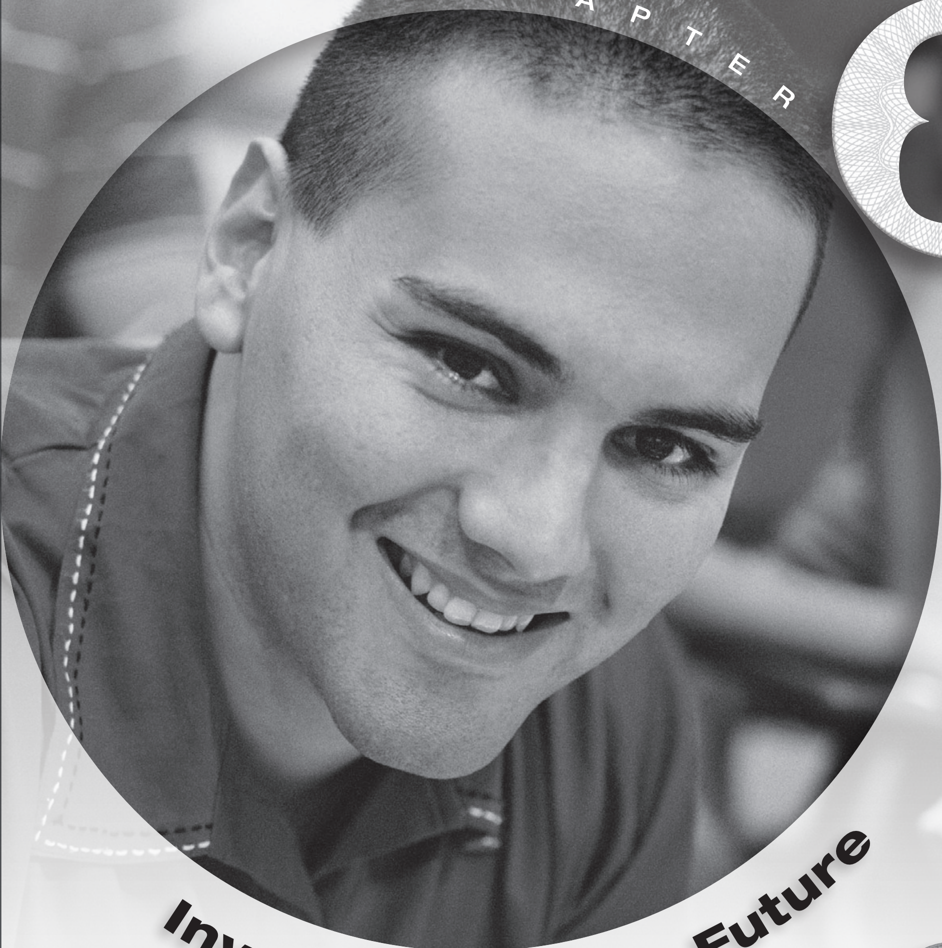
CHAPTER 8



Investing for the Future

Money is like manure. . . .
You have to spread it around or it smells.

J. PAUL GETTY, AMERICAN INDUSTRIALIST

Questions you will answer. . . .

1. What is investing?
2. What is return and risk?
3. What is the stock market?
4. What are the three most typical types of investments?
5. What are other types of investments outside the stock market?
6. How do you research investments?
7. How do you purchase securities?

Meet Eliza and Hannah

Hannah's grandmother, Eliza, worked for AT&T in the 1960s. As part of the company's retirement plan, Eliza faithfully invested 3% of her salary each month into AT&T stocks, and the company matched her contribution. Over the years, her investment grew, but Eliza always worried that if anything ever happened to AT&T, the stocks might lose their value and her retirement fund would be in trouble.

As she received promotions and her salary grew, she decided to open another retirement account and invest on her own. She started with some certificates of deposit (CDs), a few socially responsible mutual funds, and then purchased some individual stocks in a new high-tech firm and a wind energy company.

In the 1980s, when Eliza's granddaughter, Hannah, was born, Eliza decided to open an investment account for Hannah and start buying stocks and bonds for her college fund. When Hannah was a teenager, her grandmother visited her on weekends and they would look at the business section of the paper to see how her stocks and bonds were doing. Eliza taught Hannah how to research potential investments, read a prospectus, and go online to look at performance charts. By the time Hannah turned 18 years of age, she had quite a college fund and a strong foundation in the art of investing, thanks to her grandmother.

LIVE AND LEARN

You may not have a grandmother like Hannah's who successfully invests and takes time to teach you to do the same. However, you can still learn how to make money work for you. That is what investing is all about and what you will learn in this chapter.

WHAT IS INVESTING?

You have probably done some investing in your life without knowing it, especially when it comes to emotions. For example, did you ever take a risk and tell someone you liked him or her before you knew if that person felt the same way? You were investing your emotions, hoping they would pay off. If the person did not reciprocate your feelings, you probably felt bad, like you lost something; if the individual did reciprocate, you probably felt terrific, like you gained something. But if you had never taken the risk at all, you would never have known the outcome, good or bad.

Investing your money is a lot like investing your emotions—you hope that it will pay off in the end. Strictly speaking, **investing** means putting your money toward something so that it can grow. You invest when you buy securities such as stocks, bonds and mutual funds (more about these later), hold on to them for some time, and then sell them—hoping their value has increased over time so that you make some money. However, there is always the risk that their value may not increase and you will actually lose money.

Invest, verb

To put (money) to use, by purchase or expenditure, in something offering potential profitable returns, as interest, income, or appreciation in value.

WHAT IS RETURN AND RISK?

When it comes to investments, **return (or yield)** refers to the amount of money an investment generates over a given period of time. The **rate of return** (ROR) is a percentage value calculated by dividing the yield by the total investment. You can think of it like an interest rate because it indicates the rate at which the value of your investment is growing (or shrinking). If you want to figure a return of investment, you can also

Return, noun

The change in the value of a portfolio over an evaluation period, including any distributions made from the portfolio during that period.

Whether you invest time, energy, or money, return and risk always go hand in hand. **Risk** measures the uncertainty of your investment; the likelihood that the investment's return will be less than expected, or possibly nothing at all.

Risk-return Tradeoff

Typically, investments with potentially high returns have a greater risk, and investments with potentially lower returns have less risk. For example, suppose you are a risk-taker and decide to invest in a new, unknown, high-tech start-up company. If the company fails, you stand to lose everything (high risk); if it succeeds and does well, you *may* make a lot of money (higher return). If you prefer to play it safe with your money, you might decide to invest in an established, well-known, conventional firm. The company is not likely to fail (low risk), but you probably won't make as much money (lower return).

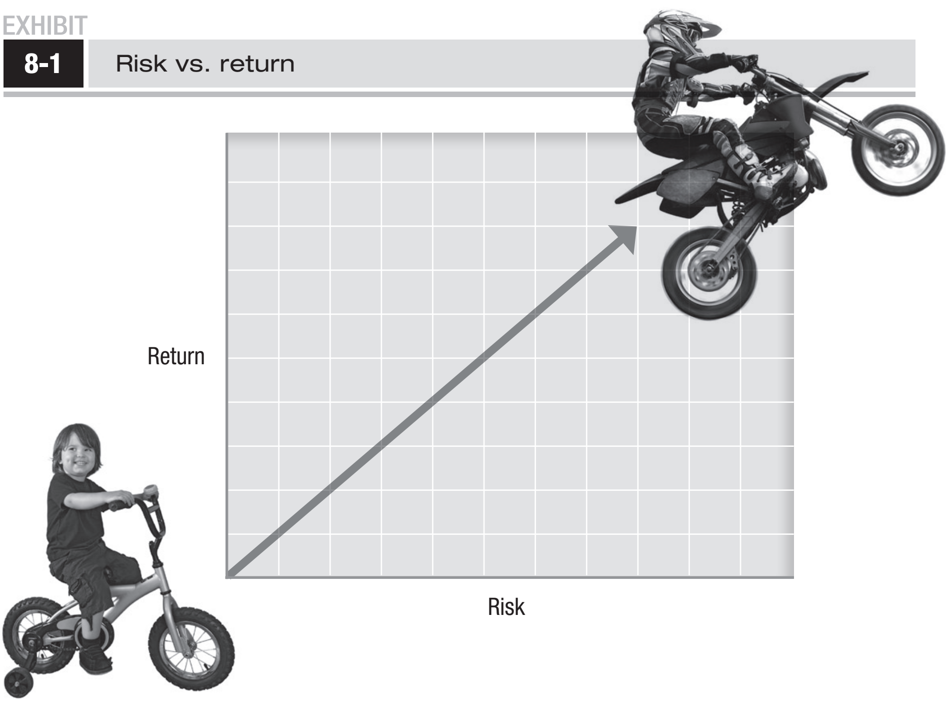
Exhibit 8-1 illustrates how return and risk are related.

Risk, noun

The uncertainty associated with any investment. That is, risk is the possibility that the actual return on an investment will be different from its expected return.

The risk-return tradeoff could be called the "ability-to-sleep-at-night test." While some people can handle the equivalent of financial *skydiving without batting an eye, others are terrified to climb the financial ladder without a secure harness. Deciding what amount of risk you can take while remaining comfortable with your investments is very important.*[1]

EXHIBIT **8-1** Risk vs. return



As an example of the risk-return tradeoff, let's revisit Hannah's grandmother, Eliza. In the 1990s, Eliza invested in Boo.com, a new global online fashion store. The stock price was low at the time, so Eliza could buy a lot of shares for relatively little money, but the risk was high—the company was unknown and online retail stores had not been around very long. However, Eliza reasoned that if the store took off, and people all over the world started buying fashions online, the stocks would be worth a lot (potential high return). As it turned out, the company went bankrupt in 2000 and Hannah's grandmother lost all the money she had invested in Boo.com. Such was the plight of a high-risk/high-return stock that didn't return as expected.

How Much Risk Can You Take?

Knowing your risk tolerance is very important before you invest. Are you a person who likes taking risks and can afford to lose some money? Or are you someone who prefers safety and cannot afford to lose money? How you feel about risk affects the type of investments you will feel comfortable making.

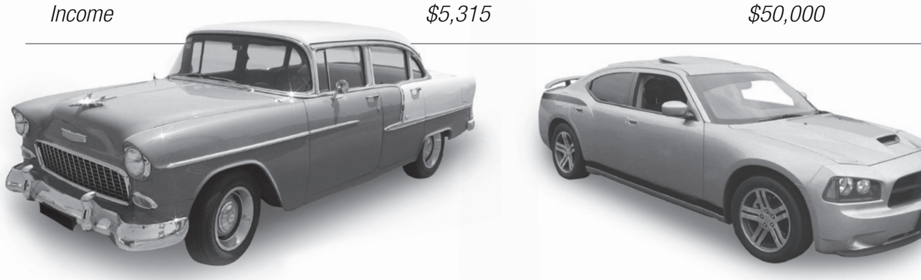
For example, with insured bank investments, such as CDs, you face **inflation risk**, which means that you may not earn enough over time to keep pace with the increasing cost of living. Exhibit 8-2 is a visualization of how costs have risen over the last 50 years.

Inflation, noun

Inflation is a persistent increase in prices, often triggered when demand for goods is greater than the available supply or when unemployment is low and workers can command higher salaries.

EXHIBIT **8-2** Rising prices over the years

ITEM	1950	2010
Home	*$12,700*	*$249,500*
Car	*$2,600*	*$29,217*
Gas	*$0.25/gallon*	*$2.90/gallon*
Income	*$5,315*	*$50,000*



If you examine the average income, you can see that the dollar went a lot farther in 1950 where a new house cost just a little more than twice someone's annual income and a car cost about one month's salary. By 2010, a new house cost at least five times someone's annual income, and a car cost about five times someone's monthly income. Now imagine what might happen to prices over the next thirty years or so while your investments are growing. Will the value of your investments keep up with those price increases? That's a risk.

With **uninsured investments**, such as stocks, bonds, and mutual funds, you face the risk that you might lose money if the price falls and you sell for less than you paid to buy. It's important to remember that stock prices are based solely on peoples' perceptions of the companies that issue the stocks (more about this later when we discuss stocks). There is always a risk associated with investing in a stock that people think is "hot" or a stock that's receiving a lot of hype. You know how quickly the latest fashion and music goes out of style. Consider your stocks like one of these trends; people might be into it now, but the stock might suddenly fall when the company falls out of favor or the company doesn't live up to its reputation.

now you try it

Take the following quizzes to find out what kind of financial risk taker you are. Use your results to evaluate what kind of investments you could potentially make.

- **Rutgers** Investment Risk Tolerance Quiz: http://njaes.rutgers.edu/money/riskquiz/
- **MSN Money Central** How Much Will My Savings Be Worth Calculator: http://money.msn.com/saving-money/savings-calculator.aspx
- **Credit Cards.com** What's Your Tolerance for Financial Risk: http://www.creditcards.com/credit-card-news/quiz/whats-your-tolerance-for-financial-risk.php

WHAT IS THE STOCK MARKET?

Before we get too deep into talking about stocks, bonds, and mutual funds, it's important to explain the **stock market**. This is where stocks and bonds are bought and sold. The

FINANCIAL FIGURES

LEARNING FROM THE EXPERIENCE OF OTHERS

Robin Wise, *CEO of Junior Achievement-Rocky Mountain, The Greater Denver Area*

As president and CEO of Junior Achievement-Rocky Mountain, Robin Wise has a front-row seat to the high school maturation process. “It’s just so much fun to watch how light bulbs go on, whether it’s a class I teach for of one our programs like Business Week, or interviewing a kid for a potential Junior Achievement scholarship. I know JA has had an impact on their lives.”

Through a volunteer network, Junior Achievement provides in-school and after-school programs for students that focus on entrepreneurship, financial literacy and work readiness.

In the popular JA Stock Market Challenge, students learn about investing and trading in a hands-on simulation of the New York Stock Exchange. “It’s fun to see the metamorphosis, even in just a couple of hours,” Wise explains. “Kids come in, they’re ‘too cool for school,’ but 45 minutes later after the game has started, they’re standing on chairs yelling, whooping. You can see the panic in their eyes because something is happening with one or two of their stocks. It’s just a blast.”

Other JA offerings include Banks in Action, Capitalism with a Conscience and Be Entrepreneurial. JA Finance Park is an interactive expo that teaches eighth-graders financial planning and serves up challenges such as parenting, health care and job hunting. Imagine the board game Life, super-sized.

“You’ve got to understand what it means to be financially literate, understanding the elements that go into not only protecting yourself, but what you can do to build wealth,” Wise says. “So often, financial literacy is taught by fear—don’t let this happen to you, beware of evil business. That’s only a piece of being financially literate. The other piece is knowing how to build your own wealth and how to protect your assets.”

stock market is not a physical location like a grocery store, because people can buy and sell investments by phone and over the Internet from anywhere in the world.

However, there are actual **stock exchanges**, real organizations with physical locations, where buyers and sellers get together to trade during certain hours of the day. You may have heard of some of these exchanges: the New York Stock Exchange (NYSE), Tokyo Stock Exchange (TSE), and London Stock Exchange (LSE). Perhaps you have seen movies about the New York Stock Exchange, with images of hordes of people running around, shouting, and making gestures with their hands to indicate what they want to buy or sell. Luckily, you can make investments without ever stepping foot in a stock exchange. You'll learn how later.

IT'S A FACT!

Despite the New York Stock Exchange's notoriety, it was not the first stock exchange in the United States. That distinction belongs to the Philadelphia Stock Exchange, which was founded in 1790.[2]

WHAT ARE TYPICAL INVESTMENTS?

The most typical investments that people buy and sell are stocks, bonds, and mutual funds. As a group, these different types of investments are referred to as **securities**.

Stocks

A **stock** is a unit of ownership in a company. When you buy stock in a company you become a **shareholder** and actually own a piece of the company. Companies issue stocks to raise money for things like product research, purchasing or repairing buildings and equipment, or hiring more employees. When you own stock, you share in the company's profits. If the profit goes up, so does the price of the stock and your investment is worth more than you initially paid for it. If the company's profits go down, so does the price of the stock and your investment is worth less than you initially paid for it.

As mentioned earlier, the price of the stock does not necessarily reflect the true value of the company—it merely represents people's perception of the company or its reputation. For example, think about what students say about one another, and how those words affect the reputations of other students—whether they are true or not. Just because a stock's price goes down, it doesn't mean the company is no good. If the company still has its employees, its equipment and buildings, and good products, it's still worth investing in—even if the stock price is low. In fact, if you already own stock in such a company, you might consider buying more while the price is low, so that you could potentially get more for your money.

Securities, noun

A document; historically, a physical certificate but increasingly electronic, showing that one owns a portion of a publicly-traded companyor is owed a portion of a debt issue. Securities are tradable. At their most basic, securities refer to stocks and bonds, but the term sometimes also refers to derivativessuch as futures and options.

Bonds

A **bond** is a different type of investment than a stock. Instead of buying ownership in a company, you are lending money in exchange for interest. Here's how it works. Entities, such as corporations, municipalities (cities, counties, and states), or the Federal Government issue bonds to raise money. When you buy a bond, you are lending money to an entity for an agreed amount of time, usually called the **life of the bond**. In return, the entity promises to pay a specified amount of interest AND repay the **face value** of the bond (what it's worth) when it's due. Some bonds pay interest throughout their lives, rather than at the very end. You can think of the bond as an IOU that must be paid off, with interest, within a specific amount of time.

Some bonds are issued by municipalities to raise money to build or repair schools, roads, libraries, and other public structures. Others are issued by corporations to buy new equipment or pay for research and marketing. Finally, U.S. Savings Bonds are issued by the Federal Government to help pay off government debt. These are the safest kind of bonds.

There are two types of U.S. Savings Bonds you can buy:

EE Bonds. These are discount bonds. You buy these for half their face value, they accumulate interest over time, and when they come due, they are worth their face value. For example, suppose you pay $500 for a $1000 EE savings bond that earns 1.5% interest a year (on the $500) and comes due in 20 years. This means that over the next 20 years you are guaranteed to receive $15 per year or $300 in interest over the life of the bond. At the end of the 15 years, you can cash in the bond for its face value of $1,000.

I bonds. These are non-discounted bonds. You buy these bonds for their face value. They accumulate interest over time, and when they come due, they are worth more than their face value. Their interest rates are usually higher than those of discounted bonds. For example, suppose you spend $1,000 on a bond that pays 4.5% interest annually and matures in 20 years. This means that over the next 15 years you are guaranteed to receive $45 per year or $900 in interest over the life of the bond. At the end of the 20 years, you can cash in the bond for its face value, $1,000.

Figure 8-3 illustrates the difference between discounted bonds (EE) and non-discounted bonds (I).

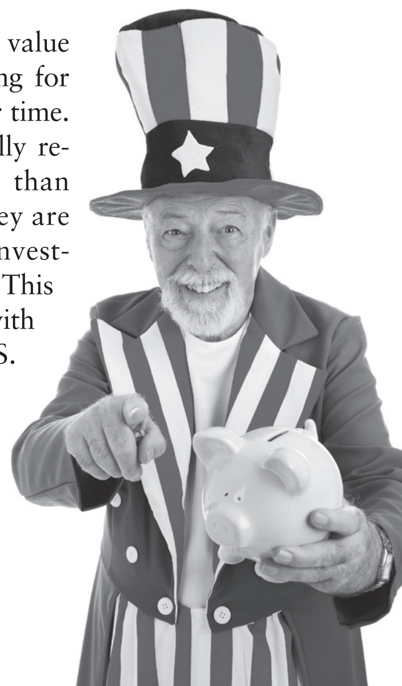
With bonds, you are not looking for their value to go up, like stocks; instead, you are looking for steady interest over time. Bond prices typically remain more stable than stock prices, so they are considered safer investments than stocks. This is especially true with U.S. Treasury bonds that are backed by U.S. government and municipal bonds that are insured. For example, a family might invest in U.S. Treasury bonds when their children are born and then cash them out to pay for their children's college education.

***quick**check*

What is a stock?

What is a shareholder?

What are the two types of U.S. Savings bonds?



FINANCIAL FOUL-UPS

LEARNING FROM THE MISTAKES OF OTHERS

Ever since Jacqueline and her mom Janice had a "financial talk" she's been worried about her mother aging and not having the means to retire from the hard work she's done her entire life.

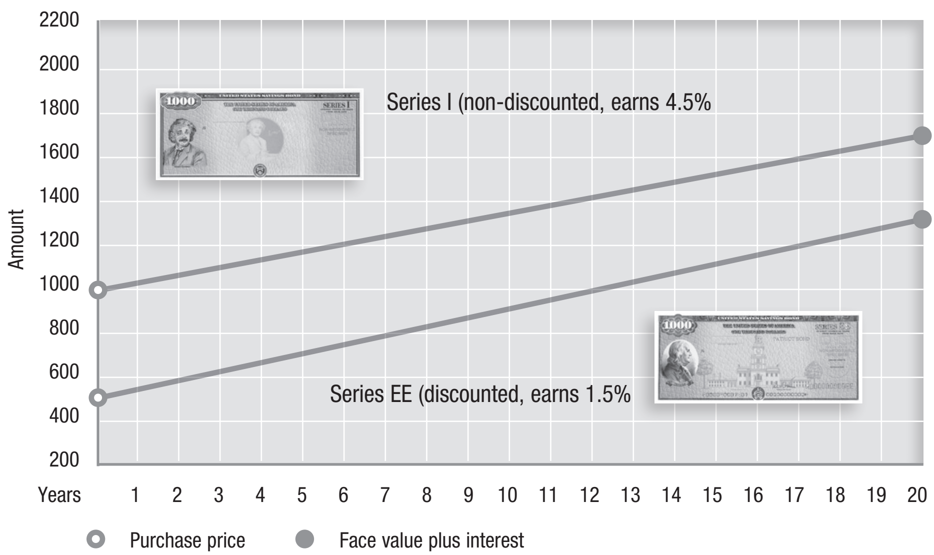
At school, Jacqueline learned about setting aside a percentage of her wages in a savings account and she wanted to know if her mom was saving for anything. Janice tries to explain that she's wanted to set up a savings since her business started taking off, but she can't seem to get on top of it. She pays a lot of taxes on her business come tax time, but she doesn't put money away throughout the year to pay them off, so she's constantly on a payment plan with the IRS to pay off back taxes.

Since she works for herself, she's opted to not pay for a personal health insurance plan so doctor's visits come directly from her pocket. She also has never invested in the stock market, has no 401K, or even a life insurance policy.

Janice admits she's concerned about retiring. Her friends are already talking about retirement, how they've paid off their homes, and their next vacation. Janice has no retirement savings, is still renting, and hasn't had a vacation in years. She fears it's too late to start saving and investing, but she really fears Jacqueline never learned the financial skills she needs to not end up in like her.

EXHIBIT

8-3 Two types of U.S. Savings Bonds



Mutual Funds

If you think stocks are too risky, and bonds are too safe, you might try a mutual fund. This is a fund that consists of a wide variety of stocks, bonds, and money market assets. This type of fund is considered **diversified** because it consists of a variety of securities.

A full-time, experienced and dedicated fund manager researches investments and decides what goes into the fund. As a result, you don't have to pick and choose the stocks. When you buy shares of a mutual fund, you are actually buying shares in lots of different companies. The benefit of a mutual fund is that even if one or two investments in the fund do not do well, as long as others do well, you don't see big losses.

Short-term Investments

You can also invest in the money market accounts and CDs that you learned about in Chapter 7. These are good when you only want to tie up your money for a year or so and want your investment in liquid form. People tend to use these types of investments as a way to save for emergencies or for a particular purchase, such as a vacation, car, or new computer.

Why Diversify?

When we talked about the mutual fund, we mentioned that it was a diversified fund because it contained a variety of securities, not just one stock. As a result, if one stock in the fund does poorly, its losses may by offset by gains in another stock. Remember Hannah's grandmother, Eliza, and the fiasco with Boo.com? Luckily, Eliza had only a small amount of her money invested in Boo.com; her other money was invested in a wide variety of stocks in different industries. So, when Boo.com went bankrupt, Eliza had plenty of other stocks that were doing well and the loss did not hit her finances that hard.

WHAT ARE OTHER TYPES OF INVESTMENTS?

To round off the discussion of investments, we'll take a look at a variety of investments that you might make outside of the stock market.

401K Plans

Remember when we talked about "painless" saving in Chapter 7 and suggested automatic transfers to your savings account. Here is an-

REAL-WORLD MATH

Here is an example of how 401K accounts work. Remember Hannah? Suppose she gets a job as a part-time bagger at her local supermarket when she's 18 years old, making about $883 a month or approximately $8,400 a year before taxes. The company she works for offers a 3% 401K contribution option, with employer matching. This raises the contribution to 6%.

- Each month, Hannah contributes $26.49 to her 401K account (.03 x $883)
- Her company contributes another $26.40
- Her total invested is $26.49 + $26.49 = $52.98 per month.

The predicted rate of return for the investment is 8%. Hannah works out that if she retires at age 67 and never gets a raise or another job (highly unlikely since she works hard and plans to get better full-time positions as she gets more education and experience), she will have almost $250,000 for retirement!

other "painless" and effortless way to save that makes you even more money. A **401K plan** is a retirement plan offered by many companies that allows you to contribute a percentage of your paycheck into a retirement fund, while the company matches that contribution. For example, if you contribute $100 per paycheck, the company contributes another $100, and you end up investing $200 every time you get paid. The 401K fund is handled by an investment management firm that decides what to invest in.

Because the investment is automatically deducted before you even receive your paycheck it's easy to save money because you do not even realize that something is missing.

Don't Forget!

When you leave your job, your 401K money stays with the investment firm that manages the 401K fund. The fund will continue to grow (hopefully) and you will be able to withdraw money when you retire. However,

Twenty-six percent of families with dependent children say that if a primary wage earner dies they'll only be able to cover expenses for a few months.[3]

because the fund is managed by an investment firm, you will not have a say in how the money is invested. Plus, if you change jobs several times, you may end up with a lot of 401K funds hanging around. If you want to consolidate your retirement savings and have some control over where they get invested, consider rolling over the funds from a 401K plan into your own IRA when you leave a job. That way you have the freedom to choose your own investments and choose what kind of IRA you want—a Roth or a traditional IRA—both of which you learned about in Chapter 7.

Real Estate

If you prefer to see and touch your investments, you might consider real estate. As we mentioned in the previous chapter, a home is an investment because it acquires equity the longer you own it, and you can borrow money against that equity. Your home is also an investment because it can increase in value over time and be worth more than you paid for it. Some people purchase rental properties so they can collect rent from the tenants to pay the mortgage on the properties. They hope that the rental properties will eventually increase in value so they can sell them for a profit.

Like the values of stocks, the values of real estate are often based on perceptions, not necessarily on reality or actual value.

For example, in the late 1990s, an earthquake damaged ranch-style homes, with three bedrooms and two baths in less than 1200 square feet, were selling for more than $500,000 in the Bay Area. But by 2010, the real estate bubble had burst and the same homes were suddenly worth about half that much. The value of real estate can be quite volatile. You cannot predict its future value, so it can be a very risky investment.

Life Insurance

Finally, let's look at life insurance, a different type of investment. It provides a sense of security in the case of death, rather than in the case of retirement. Instead of protecting your retirement funds, it protects your dependents. If you die, your husband or wife and any children you have, will receive the full value of the insurance policy to help them deal with the loss, pay for medical expenses, make the house payments, and have something to live on.

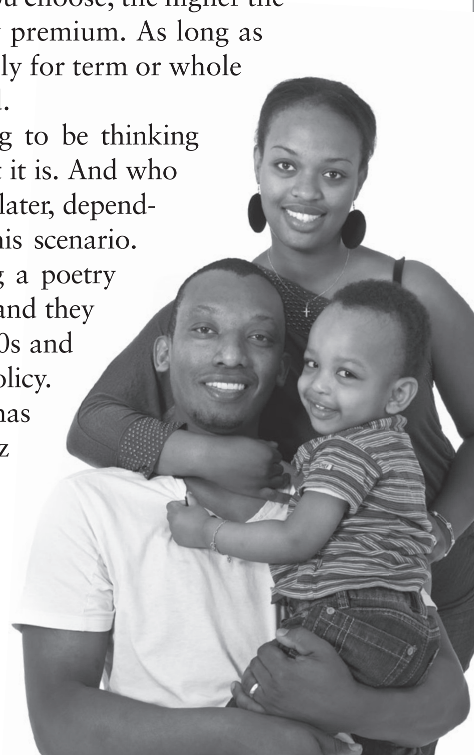
In general, most single people don't need life insurance because no one depends on them financially. But there are exceptions. For instance, some single people provide financial support for aging parents or siblings and others may be carrying significant debt that they don't want to pass on to family members who survive them.

If you decide to get insurance, what kind should you purchase? **Term life insurance** is the cheapest type of life insurance. It is considered temporary insurance because it provides coverage for a specific number of years. This period of time is called a **term** and you get to pick how long you want the term to is: 10 years, 25 years, 20 years, etc. You pay a fixed monthly premium that never changes for the duration of the term. At the end of the term, you can terminate the insurance (in which case your dependents are not covered), or you can renew it for another term. However, the payments will now be higher because you are older, and therefore more likely to need life insurance than when you were in your youth.

As you get older, it makes more sense to purchase **whole life insurance**. Whole life insurance is permanent insurance because it lasts for your entire lifetime. The monthly premiums are higher, but they never change. Plus, as you get older, the premiums become lower than what you would pay if you kept renewing term insurance.

Regardless of what type of insurance you choose, the higher the value of the policy, the higher the monthly premium. As long as you continue to make the payments regularly for term or whole life insurance, your dependents are covered.

Although you think you are too young to be thinking about life insurance, it's good to know what it is. And who knows, you may need it sooner, rather than later, depending on your life circumstances. Consider this scenario. Hannah is now in college. While attending a poetry slam at a local coffee house, she meets Luz and they hit it off. Although Luz is only in her late 20s and unmarried, she already has a life insurance policy. Her mother died several years ago and Luz has been taking care of her disabled brother. Luz just took out a life insurance policy because she wants to make sure that if something happens to her, her brother will be taken care of.



now you try it

INVESTIGATE INVESTING

Thinking about so many different investments probably makes your head spin. Here's you chance to take a break and ask yourself a few questions.

1. What kinds of investments do your family members have?

2. If they don't have investments, why not?

3. If they do have investments, how did they choose the investments they have?

4. Does anyone you know have life insurance?

5. If they do not, why?

6. If they do, what type is it and what is the policy worth?

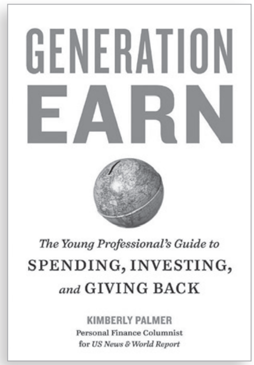
HOW DO YOU RESEARCH INVESTMENTS?

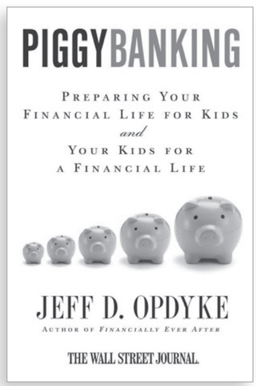
If you did the activities in Chapter 7, you probably have a pretty good sense of how much money you have available to save or invest. Based on the questions raised earlier in the chapter, you should also have an idea of how comfortable you are with risk. Now it's time to research the specific investments you would like to make.

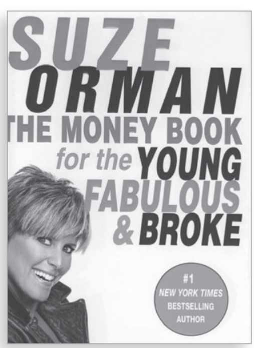
Books

If you enjoy relaxing and reading books at your leisure, here are several books that will help you understand investing and how to make good investment decisions:

- ***Generation Earn: The Young Professional's Guide to Spending, Investing, and Giving Back,* by Kimberly Palmer.** This book helps you understand not only where you should invest your money, but also what kinds of life decisions you can afford, such as what kind of job to get or if you can afford a baby.
- ***Piggybanking: Preparing Your Financial Life for Kids and Your Kids for a Financial Life,* by Jeff D. Opdyke.** This book is for parents (or future parents) who want to raise their children to be comfortable and confident managing the daily finances of life.
- ***The Money Book for the Young, Fabulous and Broke,* by Suze Orman.** This book is for people in their twenties and thirties who are working hard, struggling to make ends meet, and are buried in credit card debt and student loans. It offers a clear introduction to practical investing and money management techniques that can turn around the most dismal financial situations.







Magazines and Newspapers

If you're someone who likes flipping through magazines and newspapers to find the good articles, here are several periodicals with the latest investment tips and trends. All appear in print and online.

- ***Forbes.*** Contains articles for CEOs and individual investors. Articles include profiles of companies and private investors, as well as helpful statistics. Famous for its lists, such as: 50 Most Powerful Women in Business, 400 Richest Americans, Best Paid Celebrities Under 30.
- ***Kiplinger's.*** Magazine and newsletter that provides professional advice about personal finance, investing, and retirement. Excellent source of information to help you make financial decisions now and in the future.
- ***The Wall Street Journal.*** Great source of the latest global and financial news. Written for serious investors and business people. Some of the articles may be overwhelming (and boring) for those just learning about investments. Most famous for its daily, detailed list of stock market quotes.
- ***The Economist.*** Provides a global perspective on what is going on in terms of world news, politics, economics, and finances. Some of the articles may be a little over your head, but others may improve your understanding of the economy of the whole world, not just the United States.

Websites

If you prefer scanning the Internet, here are several websites with tutorials, forums and real-time market updates for investors.

- **Investopedia.** Comprehensive investing dictionary with a stock simulator and lots of tutorials for learning about how investing works.

  http://www.investopedia.com/
- **Scottrade.** Commission-free online trading site for stocks, bonds, and mutual funds.

  http://www.scottrade.com/
- **TDAmeritrade.** Commission-free online trading site with educational and research materials available.

  http://www.tdameritrade.com
- The Motley Fool. Amusing site with lots of humor and plenty of tips and instructions for investing wisely.

  http://www.fool.com/

For more financial references and tools, refer to the appendices in the back of the book.

now you try it

OPTIONS FOR INVESTING

1. Use the resources you just read about as a jumping-off point to research what investments you could make.

2. Organize your research in two lists: a) What you can invest today and b) what you can invest in the future.

Today:

Soon:

Prospectus

The most important part of your research involves studying the prospectus for any investment you are considering buying. The **prospectus** acts much like a job candidate's resume acts for potential employers. It is legal document that provides relevant information to help investors make decisions about whether or not to purchase shares of the stock, bond, or mutual fund. This relevant information includes:

- Structure and goals of the company or fund
- Terms of purchase
- Amount of load (extra cost for buying or selling shares)
- Investment strategy
- Historical financial statements[4]

The **U.S. Securities and Exchange Commission** (**SEC**) requires every publicly-owned company or mutual fund to file a prospectus and make it available to all potential and existing investors. This is because the primary mission of the SEC is to protect investors. Because stocks and bonds are not guaranteed by the federal government, they can lose value, which can dramatically affect the lives of the people who purchase them. These are often people who depend on those investments to pay for college or retirement. By reading the prospectus, potential investors have a chance to study the company's financial information before deciding to invest.

Figure 8-4 shows you a few pages from a sample prospectus.

EXHIBIT 8-4 Sample prospectus

Hypothetical Summary Prospectus – Prepared By SEC Staff – For Illustrative Purposes Only

THE XYZ BALANCED FUND — SUMMARY PROSPECTUS

(Class A and Class B Shares) November 1, 2007

Before you invest, you may want to review the Fund's prospectus, which contains more information about the Fund and its risks. You can find the Fund's prospectus and other information about the Fund, including the statement of additional information and most recent reports to shareholders, online at [Web address]. You can also get this information at no cost by calling 1-800-000-0000 or by sending an e-mail request to [e-mail address]. The Fund's prospectus and statement of additional information, both dated April 27, 2007, and most recent report to shareholders, dated June 30, 2007, are all incorporated by reference into this Summary Prospectus.

Investment Objective: Income and capital growth consistent with reasonable risks.

Fees and Expenses of the Fund: The tables below describe the fees and expenses that you may pay if you buy and hold shares of the Fund. You may qualify for sales charge discounts if you and your family invest, or agree to invest in the future, at least $25,000 in XYZ Funds.

Shareholder Fees (fees paid directly from your investment)	Class A	Class B
Maximum Sales Charge (Load) Imposed on Purchases (as percentage of offering price)	5.75%	None
Maximum Deferred Sales Charge (Load) (as percentage of the lower of original purchase price or sale proceeds)	None	5.00%

Annual Fund Operating Expenses (ongoing expenses that you pay each year as a percentage of the value of your investment)	Class A	Class B
Management Fees	0.66%	0.66%
Distribution (12b-1) Fees	0.00%	0.75%
Service (12b-1) Fees	0.23%	0.23%
Other Expenses	0.28%	0.46%
Total Annual Fund Operating Expenses	1.17%	2.10%

Example

The Example below is intended to help you compare the cost of investing in the Fund with the cost of investing in other mutual funds. The Example assumes that you invest $10,000 in the Fund for the time periods indicated. The Example also assumes that your investment has a 5% return each year and that the Fund's operating expenses remain the same. Although your actual costs may be higher or lower, based on these assumptions your costs would be:

	1 year	3 years	5 years	10 years
Class A (whether or not shares are redeemed)	$687	$925	$1,182	$1,914
Class B (if shares are redeemed)	$713	$958	$1,329	$1,974
Class B (if shares are not redeemed)	$213	$658	$1,129	$1,974

HOW DO YOU PURCHASE SECURITIES?

You've done all the research, reading, and thinking. You are ready to take action and make some investments. If you are under 18 (or under 21 in some states), you will not be able to open an investment account in your own name, because you are legally not old enough to sign a contract. So you will need help from an adult.

There are several ways to open an investment account and purchase securities.

In Person

To open an account in person, you must visit a broker or investment adviser. These people are typically located in the phone book. However, before you make any investments, make sure that the broker, investment adviser, or investment firm meets the following criteria:

- **Is licensed or registered.** This is required by federal and state laws. If you do business with an unregistered securities broker or firm that later goes out of business, there may be no way for you to recover your money.
- **Has not had any problems with regulators or complaints from other brokers.** You don't want to make the mistake of sending your money to a con artist, a bad financial professional, or disreputable firm.

How do you find out if the broker, adviser, or firm is licensed, has received any complaints, or has done anything illegal? Here two great sources of information:

- Information concerning brokerage firms and individual brokers is publicly available through **FINRA's Broker Check Program**. This program provides information about brokerage firms and individual brokers, such as the address, legal status, owners and officers, felony charges and convictions, investment-related misdemeanor charges and convictions, courts actions and more. The contact information for FINRA is as follows:

  Website: http://www.finra.org/Investors/ToolsCalculators/BrokerCheck/index.htm

  Phone: 1-800-289-9999

- You can also find out information about certain investment adviser firms through the SEC's **Investment Adviser Public Disclosure (IAPD) Program.** Search for a firm or adviser to view professional background and conduct, including current registrations, employment history, and disclosures about certain disciplinary events.

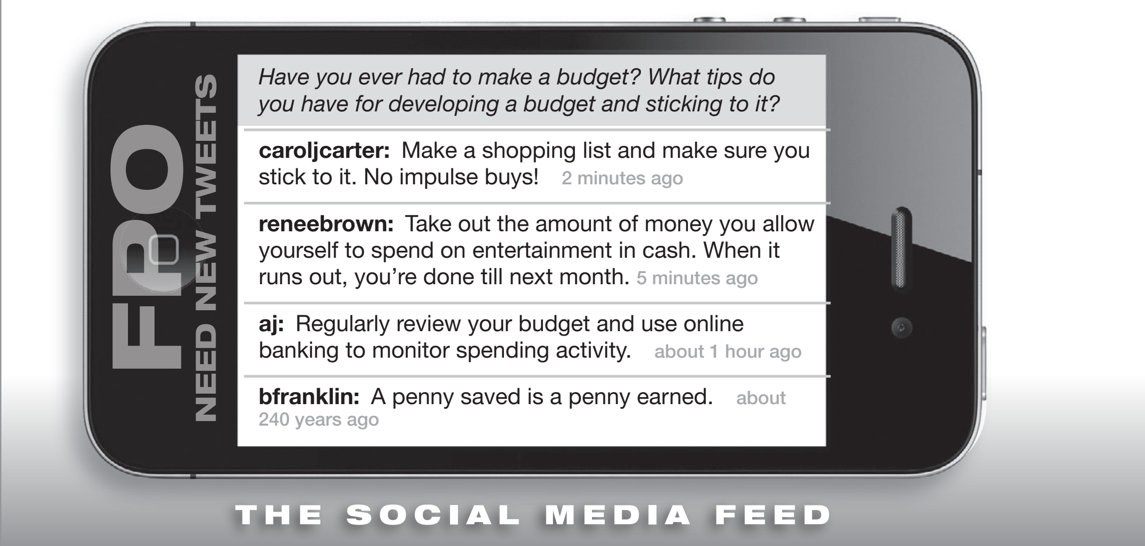
Website: http://www.adviserinfo.sec.gov/%28S%28beelzxfzuae4zkscxgiwvyjy%29%29/IAPD/Content/IapdMain/iapd_SiteMap.aspx

When it comes to working with a financial adviser, there is no such thing as asking a dumb question. It's your money at stake. You are paying for the assistance of a financial professional.

Online

You don't have to go to a financial adviser to open an account. You can open the account online and do your own research to decide what to buy and sell. There are more than 100 online brokers to choose from. Most charge you nothing to open an account, but all charge a fee for buying or selling shares. Whenever you buy or sell shares, you are performing a **transaction**.

Some online brokers charge as little as $7 per transaction, others charge a percentage based on the value of what you are buying or selling. For example, suppose an online broker charges a 1% transaction fee and you decide to shell 100 shares of a stock worth $10 a share. The total value of the transaction is $1000 and you have to pay a fee of 1% or $10. Often, online brokers charge lower fees as your transaction increases in value.



Online trading can save you time and money, but it forces you to do all the research and make all the decisions about your investments. You may be able to make a trade with a click of the mouse, but making wise investment decisions takes time. Before you trade online, take time to study your investments and their performance, so you can make an educated decision about whether to buy or sell.

Investment Clubs

One other way to invest is through investment clubs. An **investment club** is a group of people who research and pool their money to make investments. Of course, the club will probably do its investing online. The benefit of the club is that you do not have to pay a financial advisor to help you, nor do you have to do your investing alone. Instead, members of the club study different investments and share what they learn with each other. The club decides what to buy or sell based on a majority vote by the members. By joining an investment club you meet other investors, gain an education, and actively participate in investment decisions.

LET'S REVIEW

This chapter presented a lot of financial information and many new terms. But the overall message is simple: Investing is about making your money work for you over time; it's not about getting rich quick. If you start thinking about and researching investments while you are still in high school, you will be better prepared to invest early so your money has time to grow. You will also feel more comfortable making your own financial decisions, rather than handing those decisions over to someone else.

What Did You Learn?

1. There are no guarantees in investing, which is why you need to evaluate risk beforehand.
2. Investing is something anyone can do.
3. Different kinds of investments have different levels of risk.
4. There are many different resources to help you understand and choose your investments.
5. You can invest in person or online.

New Terms

- Investment
- Risk
- Stocks
- Bonds
- Mutual Funds
- Money Market Funds
- CDs
- 401K Plans
- Life Insurance
- Real Estate
- Prospectus
- SEC

END OF CHAPTER ACTIVITIES

Here's your chance to put your pen to paper, as well as discuss what you've learned with others. Doing activities and talking about them are a great way to make sure you really do understand the concepts you've read about.

Remember the Basics

1. What is investing?

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2. What kinds of investments are available?

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3. What is the risk-return tradeoff?

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4. How well do you tolerate risk?

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5. What kinds of investments should you invest in, considering your comfort level with risk?

6. What is the difference between stocks and bonds?

7. Why is diversification a good idea?

8. What is the difference between a discounted and non-discounted bond?

9. Why is the SEC important to investors?

10. What is the benefit of having a 401K? How is it different than other savings plans?

Put Math into Practice

Hannah is thinking about investing in some stocks for her future. She asks her grandmother for advice. Eliza suggests that Hannah invest in a mutual fund, rather than an individual stock so that her investment is more diversified, and safer. Together they research promising mutual funds. Hannah finds a green energy fund that has been doing well for the last 5 years. It invests in companies associated with wind energy, solar energy, and biofuel. The energy fund requires an initial investment of $5000 initial investment and earns an average of 7% a year.

1. Assume the energy fund is currently trading at $10 a share.
   a. How many shares will $5000 buy?

   ____

   b. If the fund performs as expected, how much money will Hannah earn at the end of the year on her $5000 investment? (use the simple interest calculation you learned in Chapter 7)

   ____

   Answer: $5,000 / $10 per share = 500 shares
   $5,000 x .07 = **$350 earned**

2. Suppose the value of the fund increases to $20 a share several years after Hannah buys it.
   a. Assuming Hannah still owns the same number of shares, what will be the value of her investment?

   ____

   b. Now how much interest will her investment earn in one year? (use the simple interest calculation you learned in Chapter 7)

   ____

   Answer: 500 shares x $20 per share = $10,000
   $10,000 x .07 = **$700 earned**

Work with a Team

Start your own investment club where you research and track investments without actually buying or selling.

NOTE: If you have any questions about starting an investment club, visit Better Investing Community, a non-profit, volunteer-based educational group dedicated to providing "sound investment information, education and support that helps create successful lifetime investors"[5]

- Visit: http: **//www.betterinvesting.org/public/default.htm**
- Go to the **Get Started?** link to find out how to start an investment club, the things you need to look out for, and who to contact if you have questions.

1. Discuss the following criteria with the members of your group:
    - **Risk tolerance.** Are you comfortable taking risks for potentially higher returns or do you prefer safer investments?
    - **Diversity.** Do you want to purchase individual stocks and bonds, or mutual funds? What industries are you interested in?
    - **Investment period.** Do you plan to hold on to your investments less than a year, a year, more than a year?
2. Research companies that fit your group's criteria. This may involve reading articles in newspapers, magazines, or online, or ordering a prospectus from each company.
    - Decide how much money the group could afford to invest if it were using real money.
    - Decide which investments to purchase and how many shares to buy.
3. For the next two months, track the performance of your investments each week to note whether you are losing or gaining. Notice how prices fluctuate.
4. At the end of the two months, discuss the performance of your investments and decide whether to stick with the same investments or make some changes.
5. On page 00, what is one thing Jacqueline could take away from her mom's financial regrets?

6. What can Janice start doing today to take back control of her finances? Is it important that she get financial control? Explain.

ENDNOTES

1. "Financial Concepts: The Risk-Return Tradeoff." *Investopedia* tutorials. Accessed on 13 June 2011 from http://www.investopedia.com/university/concepts/concepts1.asp
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5. "Mission." *BetterInvesting Community* website. Accessed on 13 June 2011 from http://www.betterinvesting.org/public/default.htm