Phase 4: Education

December 26, 2021

I. Investing Fundamentals

Components for building a solid foundation

Funds vs Stocks

Higher returns or lower costs?

Economic and Business Cycles

Financial Analysis

Asset Allocation

II. Funds vs Stocks

What is the difference between Funds and Stocks?

Research shows that it is really difficult to beat the market as a whole, thus even professional investment managers are beginning to put majority of their funds into passive investment strategies like ETFs which allows them to sell their funds just like a stock

FUNDS

1. Mutual Funds
   a. Index Funds (passive)
      i. Exchange Traded Funds (ETFs)
   b. Equity Funds
      i. large cap, small cap, etc
   c. $ Market Funds (MMF)
   d. Specialty Funds
   e. Style funds
      i. sector
      ii. country
      iii. etc

STOCKS

A. Can choose from thousands of companies
B. Have to be aware of company risk itself and the market as a whole
C. Can be difficult to diversify
D. High costs but also higher returns

What is the difference between Funds and Stocks?

Stocks are best for individuals who are positioned to work in the industry or have a significant amount of free time to delve into research and devouring reports. Even then, we don't consider stocks for anybody, only if, and that is ONLY IF, extreme events lead to major market disruptions. In those instances, one should try to buy as much stock as possible. Events that qualify are things such as: 1) COVID; 2) 9/11; 3) Financial Crisis

PROS AND CONS FOR OWNING FUNDS

Pros	Cons
• Liquidity • Diversification • Minimal investment requirements • Professional management • Variety of offerings	• High fees, commissions, and other expenses • Large cash presence in portfolios • No FDIC coverage • Difficulty in comparing funds • Lack of transparency in holdings

III. Higher Returns or lower costs

Assumes reinvesting funds at 6%
IRA tax free and bank acct taxed every year 28%

Tax Deferral Contributions

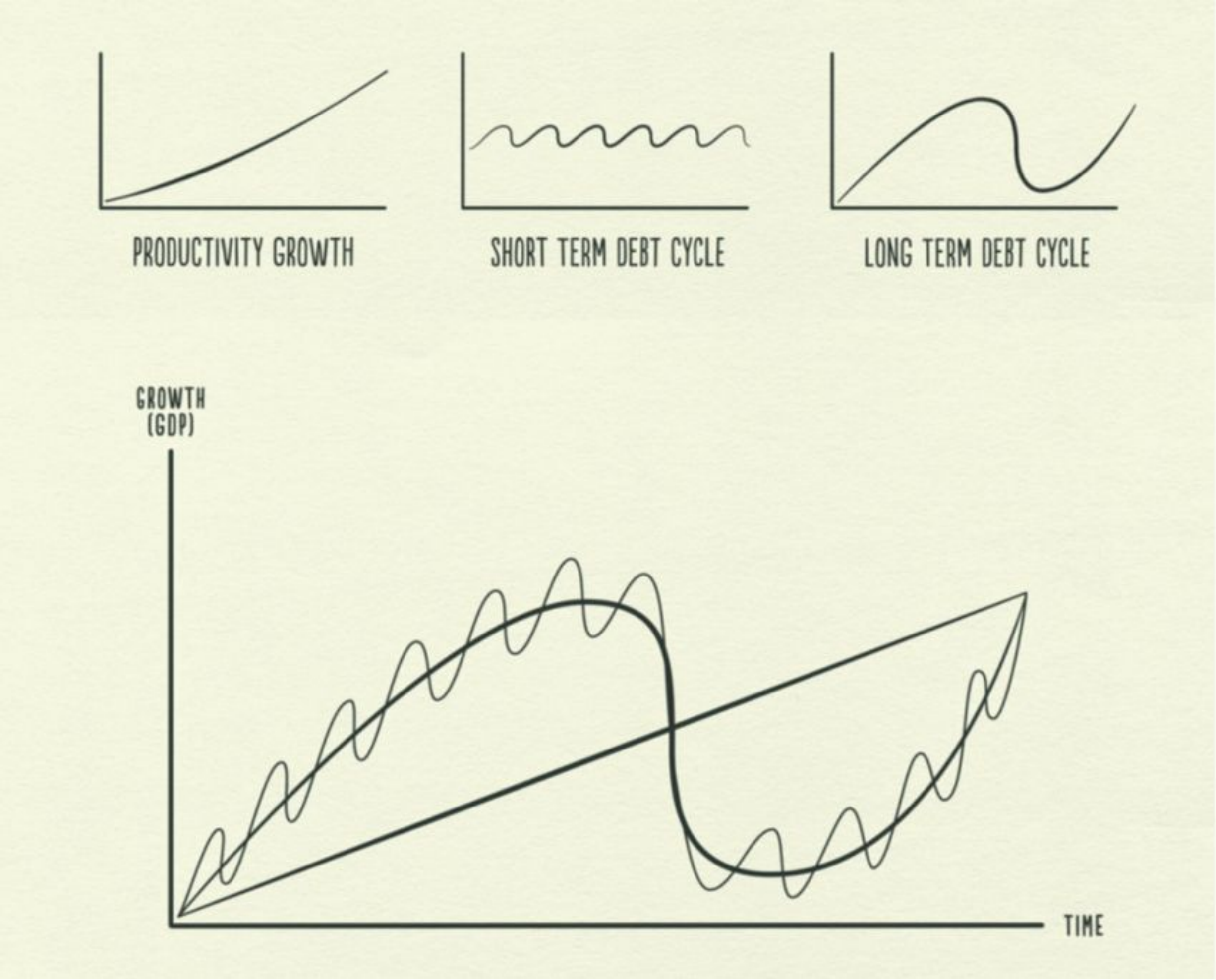
YEAR	TOTAL CONTRIBUTIONS	IRA VALUE	BANK ACCOUNT VALUE
1	$5,000	$5,000	$5,000
2	$10,000	$10,300	$10,216
3	$15,000	$15,918	$15,657
4	$20,000	$21,873	$21,333
5	$25,000	$28,185	$27,255
10	$50,000	$65,904	$60,928
15	$75,000	$116,380	$102,532
20	$100,000	$183,928	$153,932
30	$150,000	$395,291	$295,895
Taxes Due*		- $66,681	None
Net After Tax		$326,610	$295,895

Three words: Taxes Taxes Taxes!

01	Tax control decreases your costs	• Seek low expense ratios on funds with reasonable returns • Seek funds with low turnover ratios • The effect is greater as you climb tax bracket
02	Tax savings can be reinvested to achieve a higher compound effect	• Look at prior slide • Savings can be compounded by investing • Enables tax diversification (401K pre-tax and roth after tax)
03	Know the different types of tax treatment for investments	• Capital gains tax • Income tax • Tax exempt (municipals for example)

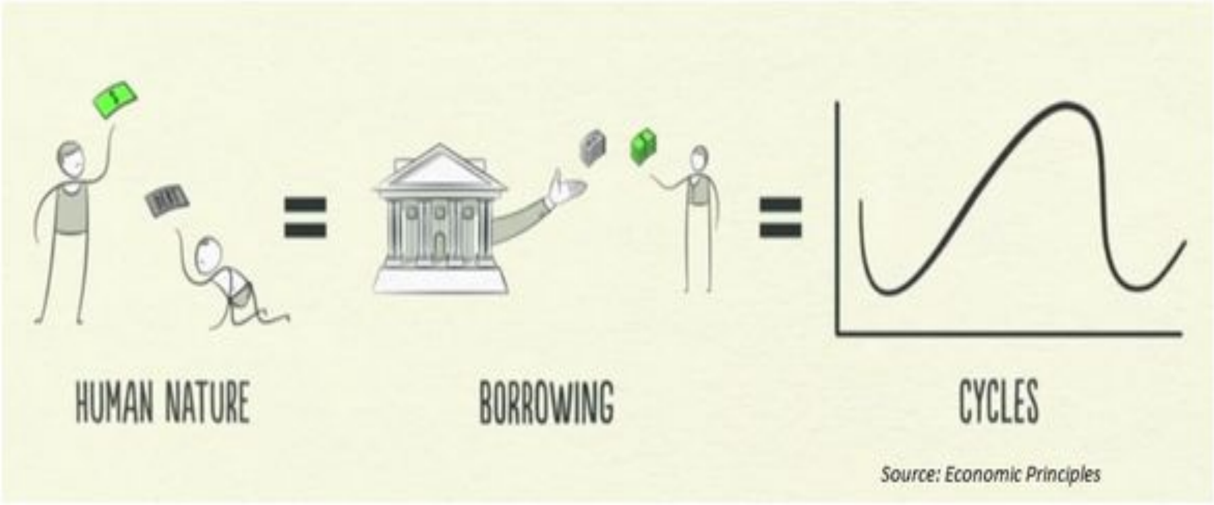
IV. Economic and Business Cycles

The Economic Cycle: Up and downs of credit in the economy



Credit is important because it means borrowers can increase their spending; which is fundamental to the economy because one person's spending is another person's income. Now the person with the more income can do the same which creates a credit cycle.

Credit is bad when used to finance over-consumption, but good when used to finance resources that produces income that can in turn pay debts



The Business Cycle

It's important to note that the business cycle is applicable to all companies! Just like every person, a company has its own lifecycle in which if executed timely by an investor, one can financially benefit from the company's early stage and future growth

2008-2019	Feb. 2020	Late Feb to Mid March	3/23/2020
EXPANSION	**PEAK**	**CONTRACTION**	**TROUGH**

EXPANSION

- Increasing employment
- Economic growth
- Upward pressure on prices

PEAK

- Producing at maximum allowable output
- Employment is at or above full employment
- Inflationary pressure

CONTRACTION

- Growth slows
- Employment declines (unemployment increases)
- Pricing pressures subside

TROUGH

- Economy has hit a bottom from which the next phase of expansion and contraction will emerge.

VI. Fundamental Analysis

Look deeper than just the stock price

1

Income Statement (Business Performance)

The income statement allows one to see how the business performed for a given year. The main components are revenue or sales, cost of goods sold (COGS), selling general and administrative (SG&A), and our bottom line or net income (same as profit)

2

Cash Flow Statement (Cash is king)

This statement enables one to see how much cash the actual business is producing. Just because you see a high amount of net income doesn't mean the business is turning those sales into cash. Think of subscription businesses

3

Balance Sheet (Overall Financial Health)

This is an important statement because one gets to see the full financial picture of a company (basically it's net worth. The balance sheet consists of **assets** which is equal to the business's **liabilities + equity**

Using financial statements to assess a stock

By using financial statements, one can identify a variety of things about the business. But the most important is to use the financials to see if the stock is cheap or expensive. Here are the common uses for financial statements:

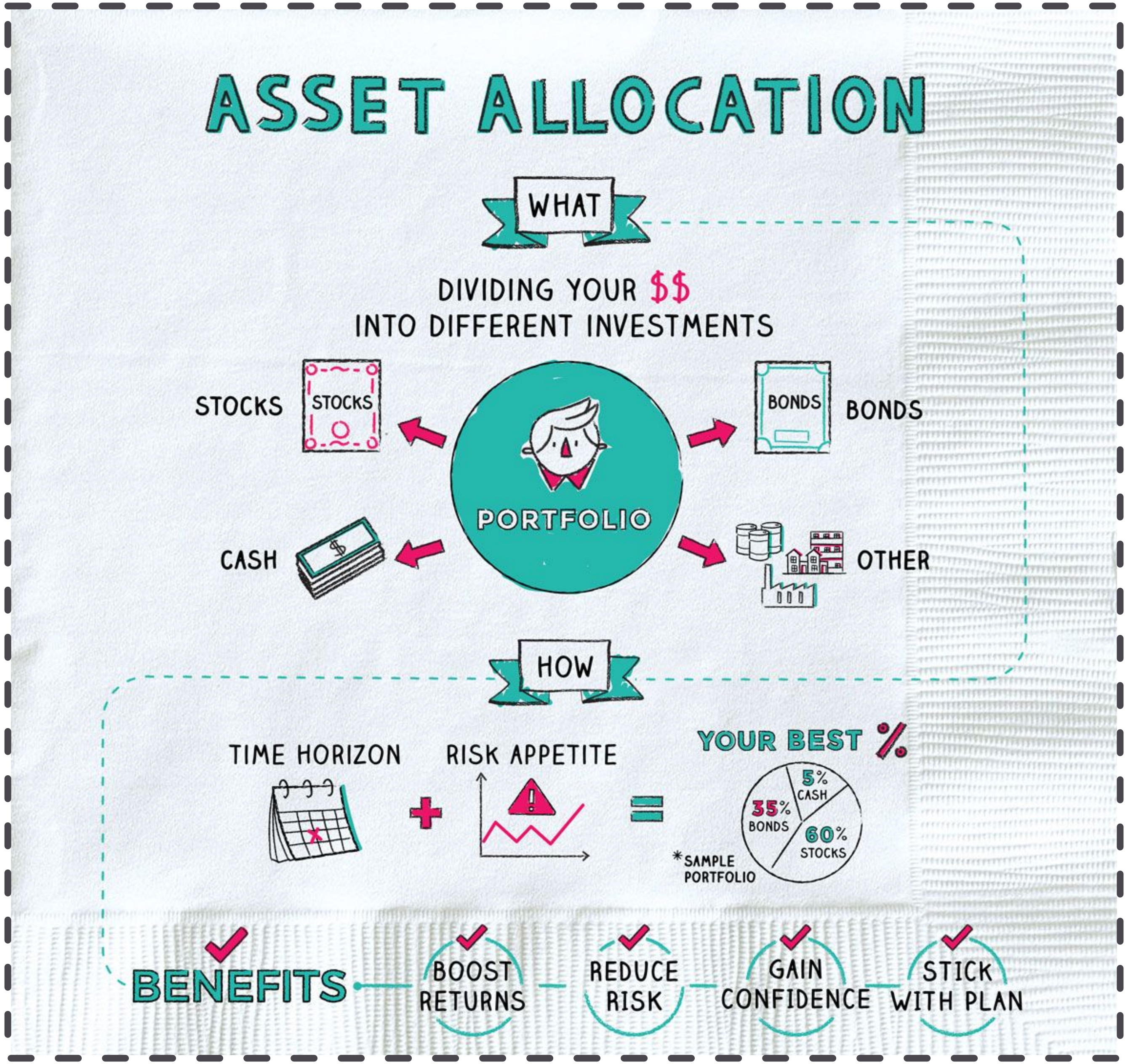
1. **RATIO ANALYSIS**
    a. liquidity
    b. solvency
    c. activity
    d. profitability
    e. valuation
2. **COMMON SIZE ANALYSIS**
    a. identifies each number as a % of its base
    b. I/S - uses revenue as denominator
    c. B/S - uses assets as denominator
    d. CFS - uses Operating Cash Flow (OCF) as denominator
3. **Management Discussion and Analysis**
    a. This is not in the financials but it is related to a financial analysis. One finds this form in 10K which is a fancy word for an annual report filed with the government. One can use this section to read what **MANAGEMENT BELIEVES** about where the business stands today and projections **going forward**

VI. Asset Allocation

Why is asset allocation important

1. DIVERSIFY
2. PLAN PORTFOLIO AHEAD
3. KNOW RISK EXPOSURE
4. FEEDBACK LOOP

A common industry standard or rule of thumb for asset allocation is what's called a "60/40". This means 60% in stocks and 40% in bonds. However, there are more assets one can invest in such as physical real estate, tradable real estate, crypto, etc.



VI. Any Questions?