LESSON #1: WHY INVEST IN STOCKS/STOCK MARKET.

And can I do this?

What returns can I expect

What is your definition of financial freedom?

What risk is there?

1. Returns, Risk and Reward

The average return on the SP 500 is about 10.00% per year. Of that about 2%-3% comes from dividends and the rest from price appreciation

Real estate (and all real estate is local) grows about 5%-7% per year

As an example the day I bought my SCA house in 2016 the SP 500 was 2125, today it is 6000+ , the market value of my SCA house has not doubled (up about 70%), while the SP 500 has almost tripled (280% ish)

Risk: Market is up 3 of every 4 years. BUT average Bear market lasts 9 months and has an average drop of 30+%.

Also, almost every year sees a drop of 10% from either the January 1st value, or from some mid-year high, even though 3 of 4 of those years the market eventually finishes higher by an average of 10+%.

1. In the stock market a stock price moves 50% due to the market, 25% due to its sectors outlook, and 25% due to the efforts of management

1. The "stock market" or what you can buy in your brokerage account is much more than just stocks, and generally with zero commission or fees (unlike real estate)
    a. You can buy individual stocks
    b. Pools of stocks that are passively managed (indexes)
    c. Pools of stocks that are actively managed
    d. Stock pools based on a theme (sector) such as Oil, Tech, medical, etc

e. Bonds, and other investments whose purposes is to generate income/cash flow, not growth
f. Commodities, crypto proxies, precious metals, base metals

So, can you handle the risk/loss? Emotional Intelligence tells us that most people are more risk adverse (afraid of loss) than they are desirous of gains. Usually this is a 2:1 ratio, the loss of $100 bet is twice as emotionally painful as the joy in winning $100

We all remember our losses more than our gains. Many people have told me stories about losing in Lucent, or Worldcom, or Peloton, or Enron, more than they discuss or even remember their best gainer

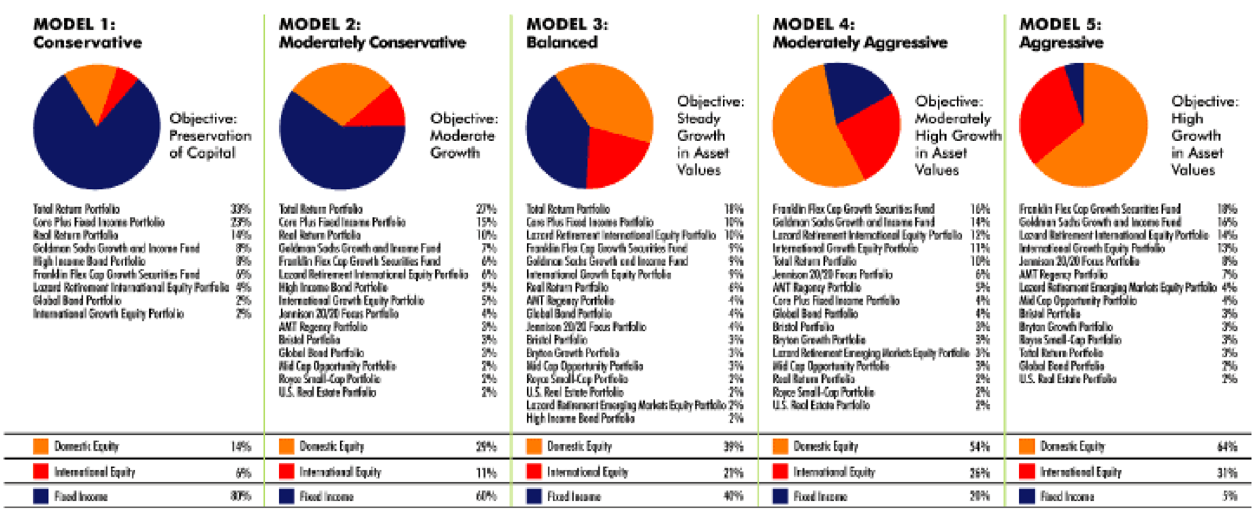
RISK and REWARD

2. You never put all your investable assets into one company, one stock, even one business type (tech, oil, income, etc) or even all into stocks
3. At the same most of you are too conservatively invested
    a. Fear of loss is twice as powerful as the desire for gain
    b. When you were working you were taught that you needed 3-6 months of savings in case you lost your job.
    c. Today most of you have WAY TOO much money sitting banks/savings/short term CDs, etc NOT WORKING for you
4. OLD joke.
    a. Bad economic times is when my neighbor losses his job
    b. A recession is when I lose my job
    c. A depression is when my spouse loses their job
    d. Good news YOU CAN NOT BE FIRED FROM BEING RETIRED
5. You want to be the casino not the gambler
    a. And the market IS NOT like gambling. In gambling the next roll of the dice is random, but in investing we can have a very good idea of the near term future prospects of a business (Coke or Apple as examples).
    b. The job of investing is to:

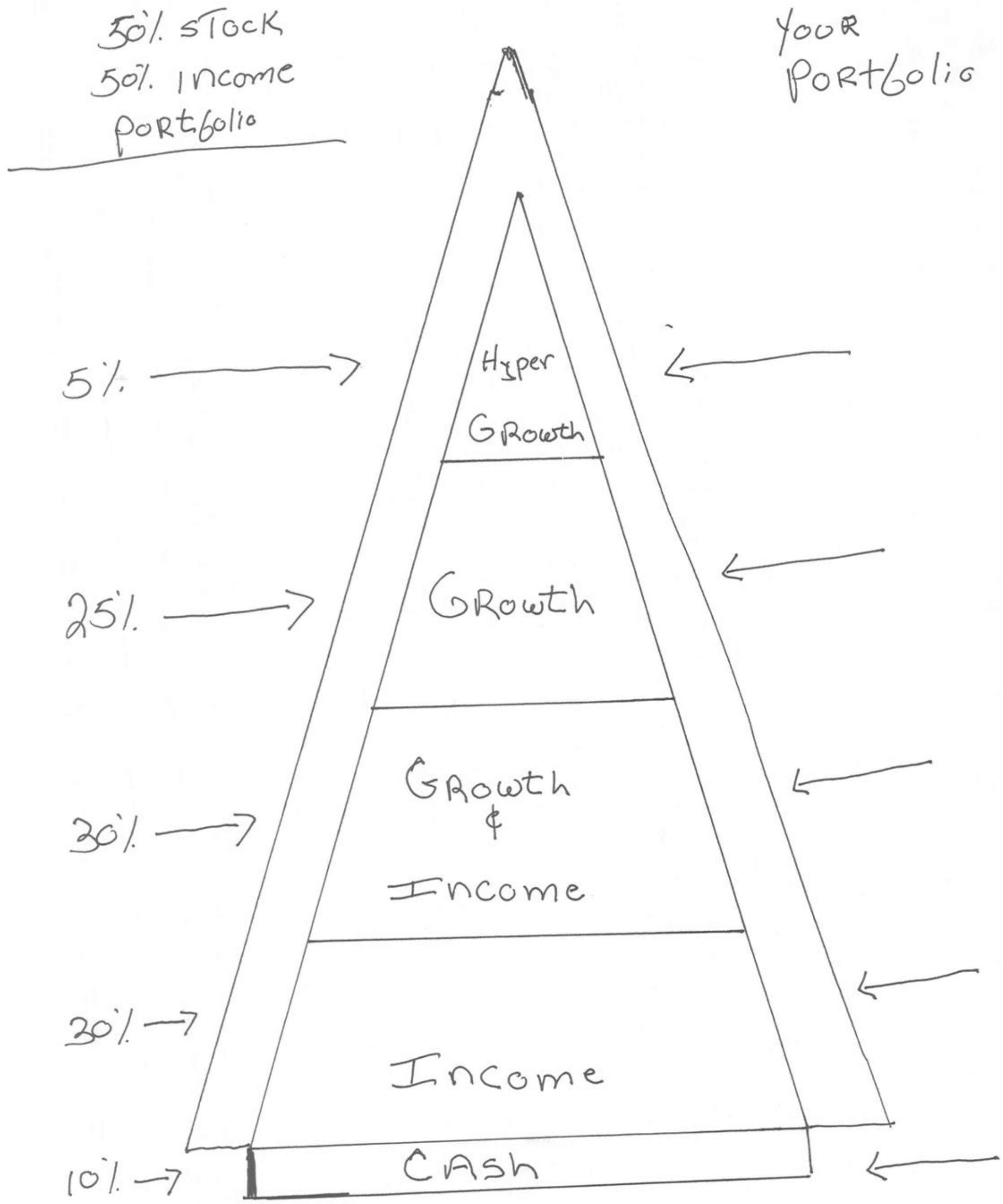
i. Find companies whose business you "understand" and who you believe offer a relatively clear vision of their future
ii. Try to determine if the current price of the stock under values or over values that companies' future business results

6. If you own your own house you are invested in real estate, virtually nothing you do will impact the value of your house 12 months from now. Only the market determines that, (Interest rates, desirability of your community, etc)
    a. But if you own a business, a company they have 1000's of employees working every day to improve that business (growth it, make it more efficient, move to new business opportunities) Thus increasing the value of your, their investment, your net worth.

ASSET ALLOCATION MODELS



1. SCOTTS ALLOCATION MODEL vs THE WORLDS ALLOCATION MODEL
    a. Standard allocation shows and allocates to stocks/bonds/ cash, and then within stocks, to large cap/small cap/ international
    b. Scott's Allocation model has 4 categories
        i. Cash
        ii. Income
        iii. Growth
        iv. Hyper or speculative growth
            1. There are some stocks that offer BOTH growth & Income
    c. Using income as an example, you can get income from stocks, REITS, bonds, CD's, treasuries, annuities, investment real estate.


50% STOCK
50% INCOME
PORTFOLIO
YOUR
PORTFOLIO
5%
Hyper
Growth
25%
Growth
30%
Growth
&
Income
30%
Income
10%
CASH

2. What is YOUR definition of Financial Freedom?

A. paid for roof over your head, $$$ for food and fun

B. being able to give some to kids/grandkids, charity

C. More fun, explore the world, do those things you put off when working,

D. ???

Scott's two part definition of Financial Freedom

1. **Have 3 times the value of assets that produce income growth than you have in assets that eat your money**
2. Rule of thumb is that assets that product can create cash flow at about 4%-5% of their value.
3. So $1,000,000 pool of assets should create $40,000-$50,000 in cash flow (some subject to tax)
   a. Assets that EAT: house, car, children, hobbies
4. One asset is your Social Security, govt/ corp pension, other guaranteed cash flow
   a. Its value as an assets is 20-25 times its taxable cash flow
      i. Example, if you get $2500 a month, that equals $30,000 per year, which to duplicate you would need a pool of money worth $600,000- $750,000 (4%-5% distribution rate)
      ii. These assets are NOT part of your inheritable estate, AND might not transfer (or 100% transfer) to your spouse/partner if you were to pass away.
5. **Have 1 ½- 2 times the potential cash flow as your expenses**
   a. Where is my cash flow coming from?
      i. Social security/Pension, etc
      ii. Working, or spouse working
      iii. IRA distributions
      iv. Investment income

b. If you are married and one spouse passes away the other might loss all the deceased Social security, or pension, or substantial parts of it
c. Our Social security benefit is set up for a major reduction in 2033 (ish?) .   By law, they will reduce payouts by 40%
d. Example, 2025 you are receiving $2500 per month, by 2033 that will increase to $3200 per month (3% COLA per yr) , then it will reduce to $1920 per month.
e. But if your expenses are $2500 a month, they will also go up to $3200 a month by 2033.
f. So you will transition from getting enough from Social Security to cover your expenses (I know I didn't calculate for taxes) to in 2033 you will be $1280 short every month
    1. $1280 X 12= $15,360, which @ 5% distribution rate means you need to have about $300,000 MORE in income/growth assets in 2033 than you do today
    2. SO YOU NEED TO INVEST IN SOMETHING

6. CAN I DO THIS

a. Following markets, economics is great for your brain health
    i. Since you retired you challenge your brain, grow your mental capacity at a far slower rate than you did when you were working. brain stimulation
b. To be successful you have to know WHAT is going on
    i. Need to anticipate changes
c. You do not need to know WHY things are changing, WHY they are changing, just WHAT and HOW

d. Everything in life takes a combination of TIME, ENERGY and or MONEY
e. Do you have the time to do this?   What is your time worth?

i. If you turned your portfolio management over to a "professional" you can expect to pay 1%-1.5% of the total amount under management
ii. Example you give a money manager $1,000,000 to invest you will pay $10,000 per year
iii. If we calculate your free time at $20.00 per hour you would need to put in about 500 hours per year, 10 per week
    1. You will probably purchase some research/subscriptions so slightly fewer hours
iv. If you have a portfolio of Mutual funds/ETFs then you need to spend about 1-2 hours a month reviewing your investments
v. If you also have stocks in the portfolio you need to add an hour per month per each stock
vi. If you are going to be an active trader, or invest in options, (an investment opportunity that we will NOT be discussing) then you are at 30-40 hours a week, it's a job/ a vocation

7. HOMESWORK

a. Homework is for your value only I will not be reviewing or grading your homework, Though I will be happy to sit down with anyone
b. WHAT IS YOUR RISK TOLERANCE
    i. Use two inserts in this lesson
c. WHAT IS YOUR PERSONAL DEFINATION OF FINANCIAL FREEDOM
d. Pick an index to track your portfolio returns against.
    i. Write down the value of that index and the value of your portfolio on the same day, so you can track your performance vs your chosen index
    ii. SPY 100% stock
    iii. 80% stock 20% income VASGX
    iv. 60% stock 40% income VSMGX
    v. 40% stock 60% income VSGX
    vi. 20% Stock 80% Income VASIX