

# Risk and Reward: A Guide to Investing

Many people have no idea where to invest their money or really how to start. In fact, a large portion of our population still believes investing is for the wealthy, when in reality it applies to anyone who is planning for their financial future. Regardless of the amount of money you have in your bank, the information in this guide will provide you with some simple and basic tips to help you begin the investing process.

## Developing Your Goals

A good starting place is to picture yourself where you want to be five, 10 or 20 years from now. Where will you live? Will you be working? In addition, ask yourself whether your motives for taking a risk to multiply your assets is based on greed. If that is the case, pray and ask the Lord for direction and peace before moving forward. Your goals may also be driven by a reliance on savings or hoarding for a false peace of mind. Once again, be sure to correct this before you begin investing. Instead, place your trust in God and remember the purpose of financial freedom is to serve Him. When we forget this objective and accrue savings for our own security or selfishness, all we have attained is financial independence, not financial freedom.

## Evaluating Common Investment Risks

Once you've established a solid set of goals, take some time to make yourself aware of common investment risks. While investments can have the potential for huge gains and big profits, they typically carry a substantial risk of loss as well. But risk comes in many shapes and sizes. Some are quite obvious, while others are inconspicuous. Listed below are some investment risks which are often overlooked.

1. The risk of not investing: Believe it or not, the biggest risk to your financial security is to do nothing. It's the same with your body. While exercise has the potential to hurt you, sitting still isn't a healthy alternative. Don't let a lack of knowledge or a fear of risk overwhelm you. Instead, take necessary steps to understand healthy investment strategies so you can exercise and build your finances.
2. The risk of playing it too safe: It is possible for investors who refuse to assume some level of risk to lose in the long run. For example, if you saved money diligently all your working years but insisted on investing in CDs, your savings may not have grown enough to surpass inflation and meet your needs. For this reason, diversifying your investments is a healthy alternative to putting all your eggs in one basket.
3. The risk of not planning ahead: Perhaps you invest faithfully for years, enjoying good returns from your investments. But when you stop to calculate your expenses, you find that you haven't been saving enough money to realistically meet your financial goals. Investing should help you provide for your financial future, so make sure to do your homework and anticipate what your financial needs will be later in life.
4. The risk of extremes: Investors who refuse to diversify are taking a gamble, regardless of where they're investing their assets. It's a careful balance, however, because too much diversification can also be risky. When investors chase varying products from year to year, their investment portfolios become a crazy quilt of holdings with no particular pattern. As you study the market and consider varying investment opportunities, set some investing boundaries for yourself as well.
5. The risk of solid investment: Solid investments are

good, but if they're not liquid you might end up in hot water. If you put your all money in conservative investments such as CDs, and you suddenly need or want your cash back, you may trade your gains for prepayment penalties. Once again, diversifying your investment portfolio will help address this issue.

## Strategies for Managing Investment Risk

You may be asking yourself, "How do I determine the difference between a good investment risk and a foolish one?" While there is no established set of steps for the perfect investment strategy, there are many ways to ensure you assume an adequate degree of risk. Here are three simple tips to help you manage investment risks in a healthy manner.

1. **Diversify:** Most types of risk can be managed by diversification—dividing investment dollars among different industries, countries, and asset classes (stocks, bonds, real estate, etc.). "Spreading the risk" through diversification helps cushion the impact from problems an investment might have on a portfolio. Savvy investors select a mix of savings and investment vehicles in order to meet their variety of objectives. Mutual Funds are also a popular investment vehicle, partly because they enable investors to instantly diversify. But depending on your short-term and long-term savings goals, different investment vehicles may be needed to reach each of those goals. For instance, if a portion of your savings is for college tuition, you should not select a bank savings account which is earning 2 percent interest or less and allows for extremely easy access to the funds. For most of us, this kind of access offers too great a temptation to draw the funds for a "great deal" on a vacation, sound system, or other major purchase with the good intention of paying it back later. A better plan would be to tie those

education savings funds up in a long-term vehicle with restricted access and higher interest earnings, thus limiting your temptation to use the funds for true emergency purposes only.

2. Be patient: Invest for the long term to reduce risk. Very high stock market returns occur only over short periods. On the other hand, losses disappear almost completely over 10-year holding periods, and they vanish over a 20-year time frame. For this reason, investing early on in life—once again, regardless of the amount of money you currently have—can be incredibly fruitful. In fact, a 25-year-old who chooses to invest small amounts at a young age has the potential to accrue more money than a 65-year-old who invests a larger sum later in life.
3. Jump in gradually: Lump-sum investing can produce spectacular returns if your timing is right, but that's a big "if." Very few professional investors consistently "time" the market correctly, and individual investors are notorious for timing it incorrectly, buying at market tops and selling at market bottoms. For most investors, dollar-cost averaging—investing a fixed amount of money on a monthly basis—provides a disciplined approach which can reduce investment risks and improve long-term returns.

### Seek Wise Counsel

If you don't obtain guidance from one or more investment counselors who have more wisdom and experience than you before making a questionable investment, you may be in for a rude awakening. So before you begin investing your money, contact a qualified financial advisor about investment options and for advice on creating a budget.

Excerpt adapted from *Financial Freedom: More Than Being Debt-Free* by Patrick L. Clements.

Invest with Church Extension Plan