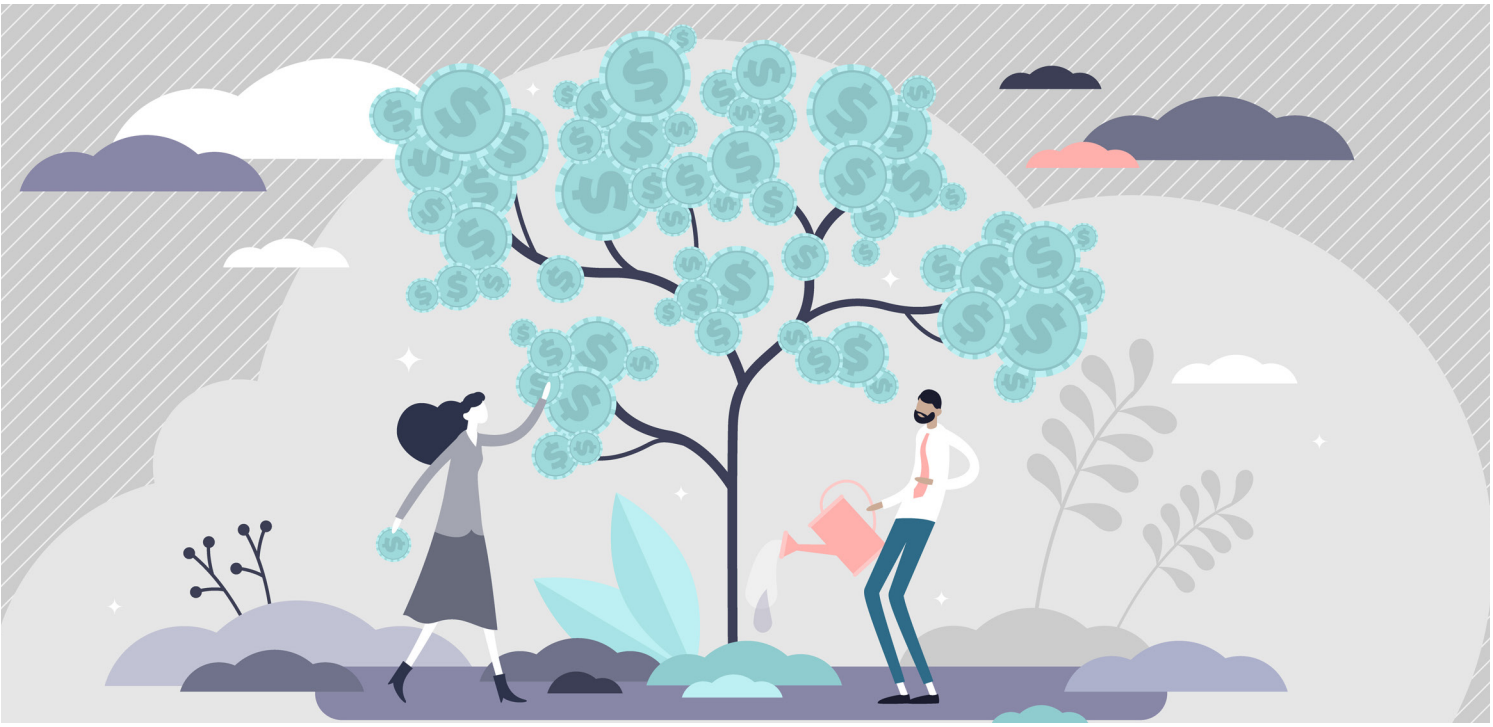
Investing Basics:

Get started putting your money to work for you



Investing is a crucial element of any long-term financial plan. Even if you have never invested before, it's fairly easy to learn the key principles of investing—knowledge that will help you make wise investment choices and avoid unnecessary risks—and the steps for getting started. This guide introduces the fundamentals of sound investing, presents key considerations when choosing investments, explains how to open an account, and provides resources to help you learn more.

Why invest?

Saving is important—it can help you make purchases (like a new appliance) and get you through a financial emergency (like a home or auto repair). But, if you want your money to really grow, you must invest. Whether you do so by purchasing stocks and bonds (the focus of this brochure), buying real estate or income properties, or starting your own business, it all boils down to putting your money to work for you so that it has a greater opportunity to grow and help you build wealth over time.

Money not invested typically loses purchasing power because the interest rate on savings accounts is lower than the rate of inflation. Stocks and bonds, on the other hand, have the potential to gain purchasing power over time.

Unlike saving for the short term, investing for long-term financial goals, like retirement, allows you to focus on growing your money rather than keeping it liquid (available immediately, with no risk of loss). For example (https://www.schwab.com/how-to-invest/investing-basics#panel--text-29546), if you put $3,000 per year in a savings account paying 1%, you would have $67,083 after 20 years. If you instead invested that money and achieved a relatively moderate return of 6%, you would have $140,407 after 20 years.

Why now?

The earlier you start investing, the more time your earnings (capital gains, dividends and interest, as explained below), if reinvested (not withdrawn from the account), can generate additional earnings—called "compounding." For example (https://www.schwab.com/investing-principles), Maria

invested $3,000 on every Jan. 1 for the 10 years from 2001 to 2010 and then stopped. Ana invested the same total amount ($30,000 over 10 years), but didn't start until 2011. Both women earned the same returns, and both reinvested their earnings. But, because Maria had an extra decade for her money to compound, she had $134,544 at the end of 2020, while Ana had only $68,503.

When it comes to investing, time is an extremely powerful tool, and the best time to start is as early as possible.

How much?

The exact amount you invest depends on your income and your financial obligations, but a good guideline is to invest as much as you can afford to while still being able to cover your essential living expenses, build an emergency fund, contribute to short-term savings, and remain free of—or pay off—non-mortgage debt. Any amount, started early enough, has the potential to grow significantly over time.

Types of investments

There are many types of investments—from stocks and bonds to gold and real estate. For most investors, stocks and bonds (and funds containing stocks and/or bonds) are the most financially accessible and manageable options.

A stock is an ownership share in a company. If the company does well, and the value of the stock goes up, you could sell it for more than you paid for it (a capital gain). Some (not all) companies also pay dividends—a portion of the company's earnings paid out regularly (usually quarterly).

A bond is a debt security, like an IOU. Borrowers (typically companies or governments) issue bonds to raise money they use to fund things (like bridges, schools, etc.). The bond issuer promises to pay you back the amount of the loan, along with interest, by a specific date.

A mutual fund is a professionally managed portfolio (collection of investments) that pools money from many investors to purchase a range of stocks, bonds or other investment types. Every mutual fund has an objective (for example, growth versus income generation), making it possible to choose funds based on your investing goals. Mutual funds provide an easy way to reduce risk because your dollars are split among a range of investments—called diversification (see below).

An exchange-traded fund (ETF) operates much like a mutual fund in that it pools investors' money and uses it to buy a portfolio of investments. But, unlike mutual funds, ETFs can be traded on the stock exchange, with prices fluctuating throughout the day. (Mutual funds trade only once a day, after the market closes.) You can typically purchase an ETF share for less than the $500+ account opening fee of many mutual funds.

There are advantages and disadvantages to each type of investment, making each one a better choice than others for different investing goals.

Learn more about these investments at Investopedia.com:

Stocks: *https://www.investopedia.com/terms/s/stock.asp*

Bonds: *https://www.investopedia.com/terms/b/bond.asp*

Mutual funds: *https://www.investopedia.com/terms/m/mutualfund.asp*

ETFs: *https://www.investopedia.com/terms/e/etf.asp*

Managing risk

Investing comes with the risk that you could lose some or all of your investment in exchange for the opportunity to outpace inflation and build wealth.

While the thought of losing money is scary, it's important to know that the longer you invest (buy and hold), the more likely it is your money will grow (*https://www.investopedia.com/articles/investing/052216/4-benefits-holding-stocks-long-term.asp*). That's because, while the stock market has ups and downs (known as volatility) in the short term, it has, historically, gone up over the long-term (*https://www.fool.com/investing/how-to-invest/stocks/average-stock-market-return/*).

You can further manage investing risk by tailoring your personal investment portfolio to match your risk tolerance—the amount of risk you are comfortable taking. For example, generally speaking, technology stocks are riskier than

blue-chip stocks (those of well-known, established, reliably-performing companies). Likewise, government bonds typically are safer than corporate bonds. You can use this knowledge to choose investments that offer the highest potential reward (growth and earnings) without being so risky they keep you awake at night.

Another very effective way to reduce your risk is to spread your money across many investments—called diversification. The idea is that even if one investment goes down in value, there are others to offset it. Mutual funds, which hold many different stocks, bonds and/or other investments, make it possible for even those with a modest amount to invest to achieve diversification.

And, if you invest in more than one type of mutual fund—for example, one that buys the stocks of large U.S. companies, another that invests in companies outside the U.S., and another that holds government bonds (or a single fund that buys a range of assets)—you further reduce your risk, because different "asset classes" react differently to economic conditions. For example, when stocks go down, bonds typically go up. The best asset allocation for you (the percentage of your total investment dollars invested in each asset class) will depend on your investment goals, risk tolerance and age.

There are many mutual fund selection tools (including those offered by brokerages for use by their accountholders) that indicate what types of investments a particular fund holds and how risky a particular fund is relative to other similar funds. The fund's prospectus—a document required by and filed with the Securities and Exchange Commission (SEC) that provides details about an investment—will also provide key information (*https://www.investor.gov/introduction-investing/investing-basics/glossary/mutual-fund-prospectus*).

Learn more about risk and reward and about the relative risk of different investments:

Determining Risk and the Risk Pyramid (*https://www.investopedia.com/articles/basics/03/050203.asp*)

Beginners' Guide to Asset Allocation, Diversification, and Rebalancing (*https://www.investor.gov/additional-resources/general-resources/publications-research/info-sheets/beginners-guide-asset*)

Understanding Asset Allocation for Your Portfolio (*https://www.fool.com/investing/how-to-invest/what-to-invest-in/asset-allocation/*)

Managing investing costs

Investing isn't free, but it's possible to minimize fees so that more of your dollars can remain invested and grow over time. Typical investing costs include:

Broker/brokerage fees: These are fees and commissions charged by a brokerage firm (for example, Charles Schwab, Fidelity or E*Trade) or an individual investment broker. Brokerages typically charge a flat fee per trade (purchase or sale of investments), though some brokerages or brokers may charge a percentage of the transaction. Financial planners/advisors who make investments on your behalf typically charge a percentage of the amount of money they manage for you per year (normally, 1%-2%). Brokerage firms may charge account maintenance and other fees, but many fees are avoidable—even the trade fees, if you make trades yourself (not with a broker's assistance) through your online brokerage account.

Expense ratio: This refers to the annual cost, expressed as a percentage of the mutual or exchange-traded fund's average net assets, of operating the fund (passed on to investors). It includes things such as portfolio management, administration, marketing, distribution and other expenses. All mutual funds and ETFs charge their shareholders an expense ratio, but the amount can vary widely.

Mutual fund loads: This is a fee or commission charged when you buy (front-end load) or sell (back-end load) shares in some mutual funds. It is easy to find excellent funds that do not charge these fees.

Retirement account fees: Even employer-sponsored retirement plans, such as a 401(k), charge fees. They may be paid by the employer, or they may be passed along to plan participants—or split. Learn more in the Department of Labor's "A Look at 401(k) Plan Fees" (https://www.dol.gov/sites/dolgov/files/ebsa/about-ebsa/our-activities/resource-center/publications/a-look-at-401k-plan-fees.pdf).

To minimize your cost of investing:

Choose a brokerage that charges no account fees and no fees for online trades. There are many. You can start your search here: https://money.usnews.com/investing/portfolio-management/articles/brokers-that-offer-commission-free-trading.

Compare expense ratios of mutual funds and ETFs—over time, they can have a significant impact on your balance. Many mutual funds with low costs perform better than similar high-cost funds. Learn more here: https://www.investopedia.com/articles/personal-finance/092613/pay-attention-your-funds-expense-ratio.asp.

Choose funds that do not charge a load (a fee to buy or sell shares). Learn more here: https://www.thebalancemoney.com/no-load-vs-load-funds-2466715.

Consider index funds. Generally speaking, index funds (https://www.investopedia.com/terms/i/indexfund.asp)—funds that mirror a stock "index," like the New York Stock Exchange or the Nasdaq—are less expensive than other funds because they are passively managed (nobody is being paid to select individual stocks). There are many index mutual funds, and most ETFs track market indexes.

Consider a robo-advisor. If you want help choosing and managing your investments, a robo-advisor might be the answer (https://www.nerdwallet.com/article/investing/what-is-a-robo-advisor). These are automated services that suggest a portfolio based on information you provide about your risk tolerance and investment goals, and then manage and rebalance the portfolio for you. Robo-advisors are less expensive than a traditional advisor, and some are even free.

Learn more about these and other tips here: https://www.consumerreports.org/bank-fines-fees/how-to-avoid-investment-fees/.

Reducing taxes

Taxes can have a big impact on your investments (https://equitable.com/retirement/products/variable-annuities/investment-edge-annuity/compare_taxable). Savvy investors delay or avoid taxes by using tax-advantaged accounts and making tax-efficient investments (https://www.schwab.com/learn/story/tax-efficient-investing-why-is-it-important).

There are typically two scenarios in which you have to pay taxes on your investments:

- You receive income from the investment. Typically, the income you receive from interest and/or dividends is taxed at your ordinary income tax rate (between 10% and 37% in 2023).
- You (or the fund you are invested in) sell an investment for more than the purchase price (a capital gain). Short-term capital gains are profits on investments held for a year or less. These gains are usually taxed at your ordinary income

tax rate. Long-term capital gains are profits on investments held for more than a year. The long-term capital gains tax rate (0%, 15% or 20% in 2023) is typically lower than your ordinary income tax rate (between 10% and 37%). (Note: Automatically reinvesting dividends and capital gains does not mean you do not have to pay taxes on that money.)

One of the most popular and effective ways to manage taxes is to invest within a tax-advantaged account that allows you contribute pre-tax dollars (such as an employer-sponsored 401(k) or a Traditional IRA [individual retirement account]), or in an account that allows your after-tax contributions to grow tax-free (such as a Roth IRA).

Learn more about tax-advantaged investment accounts:

Best Retirement Plans: Choose the Right Account for You (https://www.nerdwallet.com/article/investing/best-retirement-plans-for-you)

9 Best Tax-Advantaged Investments & Accounts to Build Wealth (https://youngandtheinvested.com/tax-advantaged-investments/)

Some investors further manage their taxes by intentionally choosing investments that don't pay interest or dividends (for example, stocks or stock mutual funds that focus on growth instead of earnings). And, many investors avoid selling investments that have grown in value sooner than one year after purchase.

There are also investments that offer automatic tax benefits. For example, the guaranteed interest you earn on municipal bonds is exempt from federal taxes, and may also be exempt from state or local taxes. Generally speaking, it makes sense to put tax-efficient investments (like municipal bonds) into taxable accounts, and put investments with a heavier tax burden into tax-advantaged accounts, where you won't have an immediate tax bill. Likewise, if you want to sell investments in order to rebalance your asset allocation, doing so in a tax-advantaged account will allow you to avoid an immediate capital gains tax on investments that have performed well. Learn more here (https://www.nerdwallet.com/article/investing/tax-efficient-investing) and here (https://www.investopedia.com/articles/stocks/11/intro-tax-efficient-investing.asp).

Of course, as with anything related to taxes, there are exceptions. Learn more about investment taxes at the TurboTax website (https://turbotax.intuit.com/tax-tips/investments-and-taxes/do-you-pay-taxes-on-investments-what-you-need-to-know/L8m0QiKM8).

Getting started

Ready to invest? Here's how to get started:

Open an account. If your employer offers a 401(k) or similar retirement plan, it usually makes sense to participate in that first, particularly if

your employer matches some or all of your contributions. (Tip: Contribute at least enough to get the full match.) If your employer doesn't offer a retirement plan, or if you want to save additional money for retirement or for non-retirement goals, you can open an IRA and/or a taxable investment account at a brokerage. Learn more about opening a brokerage account here (https://www.nerdwallet.com/article/investing/what-is-how-to-open-brokerage-account), here (https://money.usnews.com/investing/investing-101/articles/how-to-open-your-first-brokerage-account), here (https://www.investopedia.com/how-to-open-an-online-brokerage-account-4588908) and here (https://www.finra.org/investors/learn-to-invest/brokerage-accounts/opening-brokerage-account).

Fund your account. If you're investing through a retirement plan at work, your account will be funded by contributions deducted from your paycheck. For other (non-workplace) accounts, the easiest way to make the initial deposit (and to make investing a monthly habit) is to link your bank account to your brokerage account. You might also have the option to deposit a check or make a wire transfer. Learn your options and get instructions from the brokerage. (Note: Some brokerages will allow you to open an account with no deposit, but you will need to have money in the account in order to invest.)

Choose your investments. Whether you are investing within an employer-sponsored retirement plan or on your own, you should research your investment options based on things like fees, minimum required investment, performance history, fund objective and holdings, risk and performance compared to similar investments, etc. Learn more about selecting investments here:

How to Choose the Best Mutual Fund (https://www.investopedia.com/investing/how-pick-best-mutual-fund/)

How to Pick the Best ETF (https://www.investopedia.com/articles/exchangetradedfunds/08/etf-choose-best.asp)

How to Pick a Stock (https://www.investopedia.com/articles/basics/11/how-to-pick-a-stock.asp)

Evaluating Stocks (https://www.finra.org/investors/learn-to-invest/types-investments/stocks/evaluating-stocks)

Find the Right Bond at the Right Time (https://www.investopedia.com/articles/bonds/08/bond-choice.asp)

Investment Products: Bonds (https://www.finra.org/investors/investing/investment-products/bonds)

Using the FINRA Fund Analyzer (https://www.finra.org/investors/tools-and-calculators/using-finra-fund-analyzer)

FundVisualizer (https://www.fundvisualizer.com/getting-started/mutual-funds/mutual-fund-screener/)

Generally speaking, because individual stocks are riskier than funds and require more research, beginning investors should build a solid investment foundation in mutual funds and/or ETFs before venturing into individual stocks.

Automate your investments. If you participate in a 401(k) (or similar) plan, you'll have instant automation through payroll deductions. Otherwise, you may be able to set up either payroll direct deposit (check with your employer to find out if depositing your paycheck into multiple accounts is an option) or recurring bank transfers (check with your bank and/or the brokerage). Once the money is in the account, you can make investments manually, or you may be able to set up automatic investments into funds you already own. Contact the brokerage where you have an account for options and instructions. Also, you can choose to have any interest, dividends or capital gains distributions automatically reinvested.

Monitor and rebalance your portfolio. It's necessary to buy or sell investments now and then to maintain your desired asset allocation (the proportion of your money invested in each asset class). The "weighting" (market value) of your investments can change over time due to individual investment performance, and this can throw off your risk profile. You might also need to rebalance if your investment goals change, or if your timeline changes (for example, you are nearing retirement). Rebalancing can be done manually, or it can be done automatically by a financial advisor or a robo-advisor. Learn more here: https://www.investopedia.com/terms/r/rebalancing.asp. (Investing in balanced funds and target-date funds is another way to maintain your desired asset mix: https://investor.vanguard.com/investor-resources-education/mutual-funds/what-are-multi-asset-balanced-funds.)

See the list at the end of this guide for links to online resources for getting started investing.

Getting investing help

If you mainly invest in mutual funds and ETFs—particularly index funds or target date funds (https://www.investor.gov/introduction-investing/investing-basics/glossary/target-date-fund)—rather than individual stocks, and you're comfortable using online fund comparison tools, you most likely can start and manage your investment portfolio on your own (https://www.businessinsider.com/most-people-dont-need-to-pay-someone-to-manage-investments-2016-8).

If you find you need professional investment guidance, you can hire an investment advisor (https://www.investor.gov/introduction-investing/getting-started/working-investment-professional). This can be a company or an individual. When looking for an advisor:

Narrow your search by the type of support you want. Are you looking for someone who reviews your portfolio once or twice a year, advises how to rebalance your assets, and suggests specific investments? Or do you want someone to choose, purchase and sell investments for you? Learn more: https://www.forbes.com/advisor/investing/how-to-choose-a-financial-advisor/.

Gather referrals from trusted sources—your attorney, tax accountant or bank, for example.

Check credentials and disciplinary history. Online tools enable you to verify a financial advisor or broker's credentials (https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-bulletins/updated-0) and find out if they have been the subject of an SEC action (https://www.sec.gov/litigations/sec-action-look-up). Learn more about checking out financial professionals: https://www.nerdwallet.com/article/investing/background-check-financial-pro.

Interview candidates. Among the questions you should ask (https://www.nerdwallet.com/article/investing/10-questions-ask-financial-advisor): Are you a fiduciary (https://www.consumerfinance.gov/ask-cfpb/what-is-a-fiduciary-en-1769/), and how do you get paid (https://smartasset.com/financial-advisor/how-do-financial-advisors-make-money)?

If you would like some investment advice but don't want to pay the fees or commissions charged for one-on-one services (remember, the money you pay an advisor is money that can't stay invested and grow), a lower-cost robo-advisor might be the right fit (https://www.fool.com/the-ascent/buying-stocks/best-robo-advisors-beginners/).

If what you need is not advice about particular investments or tax strategies, but about things like opening an account, executing a trade, transferring funds, etc., you typically can get that kind of help from your brokerage, bank or retirement plan administrator.

Avoiding scams and fraud

Every year, thousands of people lose money to investment scams. That doesn't mean you should avoid investing—only that you need to know how to spot the warning signs of investment fraud.

Follow these rules of thumb for protecting yourself:

- Ignore unsolicited offers to invest.
- Don't believe promises of guaranteed high returns, assurances that you can't lose money, or claims that it is an "exclusive" or "once-in-a-lifetime" investment opportunity.
- Decline offers of free seminars, meals or gifts in exchange for listening to an investment pitch.
- Don't invest under pressure.
- Don't invest in anything you don't understand.
- Don't follow investment trends. In addition to lacking a lengthy performance history, trendy investments—like cryptocurrency (https://oag.ca.gov/news/press-releases/attorney-general-bonta-provides-guidance-californians-considering-investing)—are a magnet for scammers (https://www.techtarget.com/whatis/feature/Common-cryptocurrency-scams).
- Verify credentials. Use BrokerCheck (https://brokercheck.finra.org) to review a broker's qualifications, registration, employment history, disciplinary events and more. Also find out whether the person is licensed to sell securities in your state (https://www.nasaa.org/contact-your-regulator/).
- Get documentation. Stocks, mutual funds and ETFs typically are required to have a prospectus, and bonds are required to have an offering circular (a legal document detailing the structure of a bond). Get company financial statements and check out many investment products by searching EDGAR (https://www.investor.gov/introduction-investing/getting-started/researching-investments/using-edgar-research-investments).
- If you're unsure about an investment or the person offering it, get the opinion of a savvy, trusted friend or advisor.

Learn about specific types of investment fraud here: https://www.investor.gov/protect-your-investments/fraud/types-fraud.

If you have a question or concern about an investment, or you think you have encountered investment fraud, contact the SEC (https://www.sec.gov), FINRA (https://www.finra.org/investors#/) or your state securities regulator (https://www.nasaa.org) to report the fraud and to get assistance.

Learn more

Learn more about getting started investing:

Introduction to Investing (https://www.investor.gov/introduction-investing)

How to Start Investing: A Guide for Beginners (https://www.nerdwallet.com/article/investing/how-to-start-investing)

How to start investing in 2022 (https://www.bankrate.com/investing/how-to-start-investing/)

How to invest: An essential guide (https://www.getrichslowly.org/how-to-invest/)

5 Tips for Beginning Investors (https://www.kiplinger.com/article/investing/t023-c006-s003-investment-advice-for-beginners.html)

Investing Basics: FAQs (https://www.schwab.com/how-to-invest/investing-basics)

Investing Basics: Bonds, Stocks, Mutual Funds and ETFs (https://finred.usalearning.gov/Saving/StocksBondsMutualFunds)

Investing Basics (https://www.navyfederal.org/makingcents/investing/investing-basics.html)

About Consumer Action

www.consumer-action.org

Through education and advocacy, Consumer Action fights for strong consumer rights and policies that promote fairness and financial prosperity for underrepresented consumers nationwide.

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