

Building **Wealth**

In the Classroom

Lesson 6

Save and **Invest**—Bonds, Stocks and Mutual Funds



Federal Reserve
Bank of Dallas



Instructional objectives

You will:

- Compare and contrast different types of investments such as stocks, bonds and mutual funds.
- Evaluate risk and return of various investment options.



Diversify Your Investments

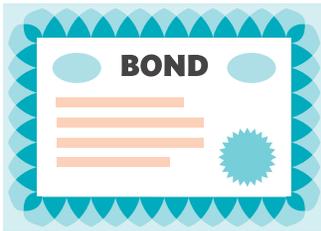
Once you have a good savings foundation, you may want to diversify your assets among different types of investments.

Diversification

Diversification is the distribution of investments among several companies to lessen the risk of loss.

Diversification can be neatly summed up as, “Don’t put all your eggs in one basket.” The idea is that if one investment loses money, the other investments will make up for those losses.

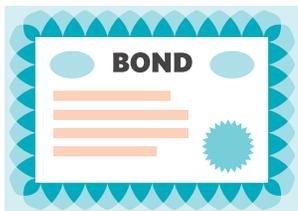
Diversifying investments in **bonds, stocks** and **mutual funds** can lessen the risk of loss.



Bonds

Lending your money

Bonds



Bonds are financial assets that represent loans to corporations, municipalities, governments or their agencies.



When you buy bonds, you are lending your money to a federal or state agency, municipality or other issuer, such as a corporation.

Bonds

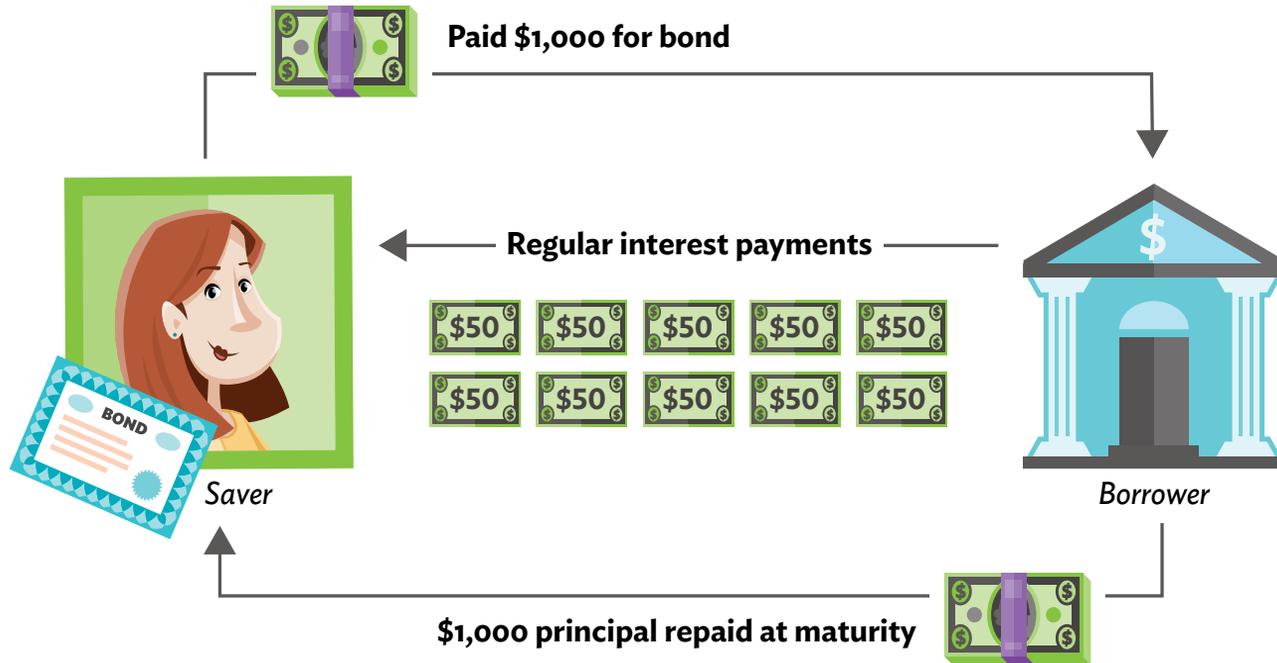


A bond is like an IOU. You lend your money and in return the issuer promises to pay you a stated rate of interest during the life of the bond and the entire face value when the bond comes due.



Face value is the original value of the bond. This is usually stated in \$1,000's of dollars.

The life of a bond



Who issues bonds?



Corporations

Corporations issue bonds to borrow money to finance many types of activities, including capital projects, acquisitions, expansions and other business ventures.



Sovereign governments

The U.S. Treasury (along with other sovereign governments) issues bonds to borrow money to pay for government expenditures that exceed tax revenue.



Municipalities

Municipalities, including cities, counties and states, issue bonds to borrow money to pay for public works and other activities.

Where can you buy a bond?

Primary Market
Sellers are the original issuers of the bonds.
Buyers are investors (savers).

Secondary Market
Sellers are individuals or institutions that own bonds.
Buyers are investors (savers).

Understanding the lingo

U.S. savings bonds

Government issued and government backed. Savings bonds can be purchased in denominations from \$50 to \$10,000.

- **I savings bonds**

Low-risk savings product that earn interest while protecting you from inflation. Sold at face value.

- **EE savings bonds**

Secure savings products that pay interest based on current market rates until they reach 30 years or until you cash them, whichever comes first. Electronic EE savings bonds are sold at face value.

Understanding the lingo

Treasury investments

U.S. Treasury are ones that the U.S. Treasury issues and are sold to pay for government activities. They are backed by the full faith and credit of the federal government.

Treasury bonds

Securities with terms of 20 or 30 years. Interest is paid semiannually.

Treasury bill

Short-term securities with maturities ranging from a few days to 52 weeks. They are sold at a discount from their face value.

- The difference between cost and what you are paid at maturity is the interest you earn.

Understanding the lingo

Treasury note

Interest-bearing securities with maturities ranging from two to 10 years. Interest payments are made every six months.

Treasury inflation-protected securities (TIPS)

Marketable securities whose principal is adjusted by changes in the Consumer Price Index. TIPS pay interest every six months and are issued with maturities of five, 10 and 30 years.

Advantages of investing in bonds

Some government-issued bonds offer special tax advantages. There is no state or local income tax on the interest earned from Treasury and savings bonds.

- Low risk backed by the full faith and credit of the federal government.
- Can purchase directly from the Treasury through Treasury Direct at [treasurydirect.gov](https://www.treasurydirect.gov).



Try it on your own

Use handout 2 to research and compare different types of U.S. government bonds.

Name _____ Date _____



Lesson 6—Handout 2

Comparing Bonds

Instructions:

- Go to www.treasurydirect.gov/indiv/products/products.htm
- Click on each type of bond listed and record the information found for each column.

Comparisons	Treasury bill	Treasury notes	Treasury bonds
Minimum purchase			
Issue method			
Minimum term of ownership			
Rates and terms			
Interest-earning period			
Tax considerations			



Stocks

Owning part of a company

Markets

Markets consist of people and firms who buy and sell something.



Consumer markets

A marketplace to buy and sell consumer goods.

- eBay.
- StockX.
- Farmers market.



Stock exchange (market)

A marketplace to buy and sell securities such as stocks and bonds.

- New York Stock Exchange.
- Nasdaq.
- Tokyo Stock Exchange.

Understanding the lingo

Stockholder/shareholder

A person who owns stock in a company and is eligible to share in profits and losses.

Dividend

A share of profits paid to a stockholder.

Understanding the lingo

Common stock

A kind of ownership in a corporation that entitles the investor to share any profits remaining after all other obligations have been met.

Preferred stock

A kind of ownership in a corporation that entitles the investor to the payment of fixed dividends and priority in the distribution of assets.

- Preferred stockholders do not have voting rights while common stockholders do.

Understanding the lingo

Stock appreciation

Value of the stock increases.

Stock depreciation

Value of the stock decreases.

Ticker symbol

Provides a unique identifier by which individual securities can be researched and traded.

Understanding the lingo

Market capitalization (market cap)

refers to the total value of a company in the stock market.

- Large-cap companies have a market value over \$10 billion.
- Mid-cap companies have a market value between \$2 billion and \$10 billion.
- Small-cap companies have a market value from \$300 million to \$2 billion.

Appreciation/depreciation news headlines

For each news headline, predict if the stock price appreciated or depreciated.

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THE Building **Wealth** TIMES

Today

Alibaba shares

_____ to six-month low despite proposed rise in shares buyback.

Zoom stock

_____ after service outage.

Airbnb, now a \$100 billion company after stock market debut, sees stock price _____ after COVID-19 vaccine.



Boeing stock _____ after FAA emergency order on thousands of 737 jets.



AMC and Cinemark stocks

_____ on vaccine news.



Appreciation/depreciation news headlines

Answers

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THE Building **Wealth** TIMES

Today

Alibaba shares slump (depreciate) to six-month low despite proposed rise in shares buyback.

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Zoom stock falls (depreciates) after service outage.

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Airbnb, now a \$100 billion company after stock market debut, sees stock price double (appreciate) after COVID-19 vaccine.



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Boeing stock falls (depreciates) after FAA emergency order on thousands of 737 jets.

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AMC and Cinemark stocks soar (appreciate) on vaccine news.

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Purchasing a stock



When the bid price and the ask price match, a transaction occurs, and shares of stock are sold.

Bid price

Buyers offer to buy shares of stock at a given price.

Ask price

Sellers offer to sell shares of stock at a given price.

Questions to ask when evaluating a company

Before purchasing a stock, you will need to research the company first.

Who

- Name of the company.
- Ticker symbol.

What

- Goods and services produced.
- Line of business.
- Sector of the economy.

When

- Founding date.
- Dividend payment schedule.

Where

- Location of headquarters.
- Production facilities or major markets.

How much

- Revenue.
- Total sales.
- Profit margin.
- Earnings.
- Value of company.



Would You Rather?

Use the information on each slide to determine which stock example you would rather invest in.

Would you rather?

Target

- Sells consumer retail products.
- Founded in 1902.
- Minneapolis, Minnesota.
- Five-year dividend yield—3.07.
- Profit margin 4.31%.
- Quarterly earnings growth (year/year)—42%.

Walmart

- Sells consumer retail and wholesale products.
- Founded in 1945.
- Bentonville, Arkansas.
- Five-year dividend yield—2.25.
- Profit margin 3.60%.
- Quarterly earnings growth (year/year)—56.20%.

Source: finance.yahoo.com, 1/22/2021.

Would you rather?

Amazon

- Retail sales of consumer products and subscriptions.
- Founded in 1994.
- Seattle, Washington.
- Five-year dividend yield—*N/A.
- Profit margin 4.99%.
- Quarterly earnings growth (year/year)—196.70%.

Alphabet Inc.

- Provides online advertising services and operates through Google.
- Founded in 1998.
- Mountain View, California.
- Five-year dividend yield—*N/A.
- Profit margin 20.80%.
- Quarterly earnings growth (year/year)—59.10%.

*Amazon and Alphabet Inc. have never paid dividends.
Source: finance.yahoo.com, 1/22/2021.

Would you rather?

Proctor & Gamble

- Provides branded consumer packed goods in beauty, grooming, health care, fabric and home care and baby, feminine and family care.
- Founded in 1837.
- Cincinnati, Ohio.
- Five-year dividend yield—2.93.
- Profit margin 18.72%.
- Quarterly earnings growth (year/year)—3.70%.

Source: finance.yahoo.com, 1/22/2021.

Nike

- Designs, develops and sells footwear, apparel, equipment and accessories.
- Founded in 1964.
- Beaverton, Oregon.
- Five-year dividend yield—1.06.
- Profit margin 7.39%.
- Quarterly earnings growth (year/year)—12.20%.



Try it on your own

Use Handout 3: Stock Research to complete your research.

- Select two companies included in the Dow Jones Industrial Average.
- Research the who, what, when, where and how much.
- Create an investor information sheet for both companies.

Name _____ Date _____



Lesson 6—Handout 3

Stock Research

Directions:

Part 1

Select two companies from the list of stocks included on the Dow Jones Industrial Average. Write the names of the companies below.

- _____
- _____

Use newspapers, corporate websites and online news sources to research information about both companies you selected. Information should include:

- **Who**—Name of the company.
- **What**—Description of the company and its business, major products or services that it produces, name of president and CEO (may be the same person) along with other leaders that you feel are important.
- **When**—Founding date, dividend payment schedule.
- **Where**—Location of headquarters, production facilities or major markets.
- **How much**—Information about the performance of the stock, including price, revenue, total sales, profit margin, earnings, value of company, dividends and yield over the past year.

Part 2

Create an investor information sheet about both of your companies. Provide information that a person should consider before purchasing stock in the company. The sheet should include:

- Information about the company that you gathered in your research.
- Graph of the stock price for the last year.
- Major competitors or related companies.
- Your assessment of the future prospects for the company (see note).

Note: When you assess the future of the company, consider economic developments that would help the company make profits and grow in coming years. Also, consider threats to the company's future growth or profitability. For instance, does the company produce goods or services that are increasingly popular? Are competitors from around the world threatening the company's market share?



Mutual Funds

“Mutual funds were created to make investing easy, so consumers wouldn’t have to be burdened with picking individual stocks.”—Scott D. Cook

Mutual funds



Mutual funds are made up of a group (or basket) of stocks.

The performance of a mutual fund relates to the performance of all the group (or basket) of stocks.

A **mutual fund** is a pool of money managed by an investment company.

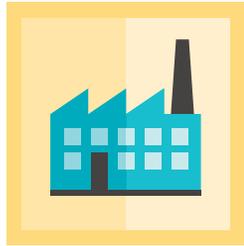
An **index fund** is a type of mutual fund that components of the fund track the performance of a financial market index.

Indexes by location

U.S. Indexes
DJIA
SP500
Russell 2000
SP400
NASDAQ Composite Index

International Indexes
MSCI EAFE
Nikkei 225
DAX
Hang Seng
FTSE 100

Sector indexes



Manufacturing



Telecom



Pharmaceutical



High Tech



Energy

Market cap indexes

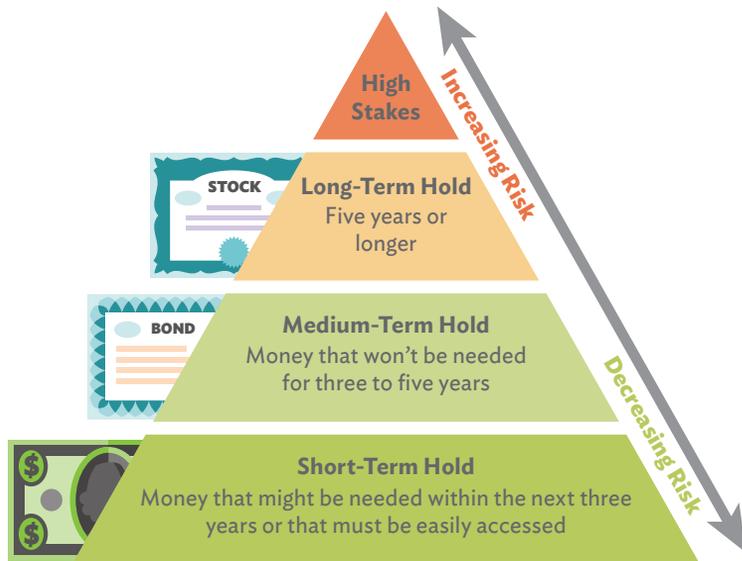
Market cap indexes are based on the size of the companies within the index.

Large Cap
DJIA
SP500

Mid Cap
Russell MidCap
SP400

Small Cap
Russell 2000
Russell Small Cap Completeness

Understanding the risk-return relationship



When you are saving and investing, the amount of expected return is based on the amount of risk you take with your money.

Generally, the higher the expected return, the higher the risk of losing money.

Summarize learning objectives

Bonds are financial assets that represent loans to corporations, municipalities, governments or their agencies.

A **stock exchange (market)** is a marketplace to buy and sell securities such as stocks and bonds.

A **stockholder/shareholder** is a person who owns stock in a company and is eligible to share in profits and losses.

Summarize learning objectives

A **dividend** is a share of profits paid to a stockholder.

A **mutual fund** is a pool of money managed by an investment company.

An **index fund** is a type of mutual fund where components of the fund track the performance of a financial market index.

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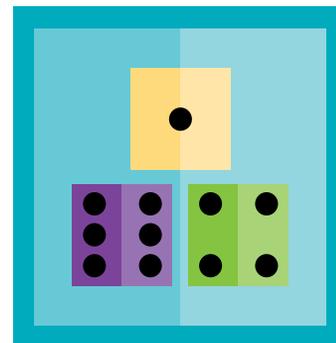
In the Classroom

Up Next: Lesson 7

Save and Invest—Risk and Return



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I want to learn how to build wealth for myself and my family.

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For Community Leaders

I lead a group of adults interested in improving our personal finance skills.

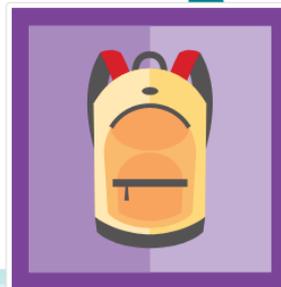
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For Teachers

I teach financial education to high school or college students.

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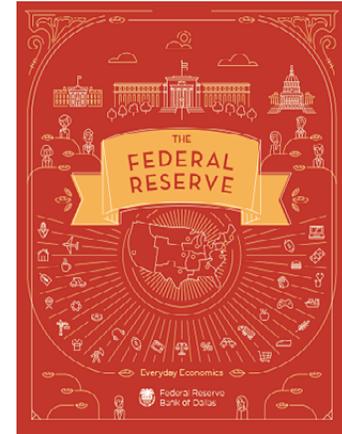
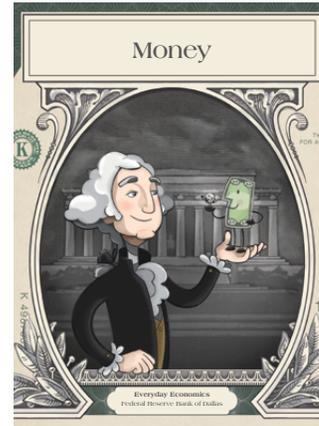
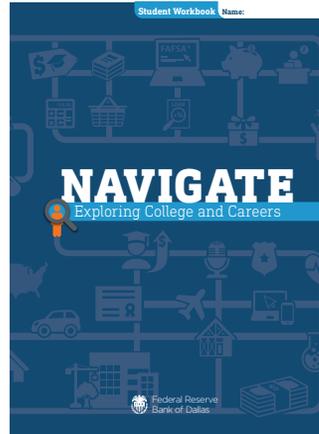
For Students

I am a student and want to learn how to create personal wealth and meet my financial goals.

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