<u>Audio Lesson #10 What to Do with Savings?</u>

It's not a hill, it's a mountain
As you start out the climb…

Hello. My name is Jeff Tyburski. Welcome to my 10th in a series of audio lessons. All that remains after this is a brief recap. Thanks for sticking it out.

I teach financial literacy with a focus on helping you save money. My initial focus was to ensure you are *in a position* to save – because you *can't save* if you have too much debt and you *can't save* if you can't get and hold a good job. The previous *two* sessions taught WHY we must save and HOW to save. Now it time to wrap up and talk about *growing* savings and building wealth. Now it is time to talk about *what to do with savings*.

You've saved! Now what? That is the question to answer in this session.

Don't be "like a deer in the headlights." We all know the expression. It refers to being caught in a state of paralysis. Sometimes in life people *aren't totally frozen*, yet they still aren't accomplishing what they need to do. Have you ever watched a hockey team on a power play obsessively passing the puck, looking for the *perfect* opportunity, but never shooting? Well, you can't score if you don't shoot.

This session will provide a high-level overview of what to do with your savings. This session will provide enough for you *to make an initial move*!

Here, I show you that **understanding *some* language and the landscape of savings and investments is enough to decide how to move ahead**: managing your investments yourself, engaging professionals, or a combination of the two. **What to do with your savings? Really, it is *not* too intimidating to move forward.**

I need to start with a *disclaimer*. As you'd suspect, a discussion on *what to do with savings* gets into ***investing***. Recall, however, investing is NOT my focus. My focus is on saving money. My initial concern, and what motivated me to teach financial literacy, was my observation that too few people are saving money, and you have to save before you can invest.

To be clear, I am not a money manager, registered investment advisor, or financial planner. There is an army of them out there wanting to help, if and when you or a family member decide to work with them. I actually did work as a senior analyst and portfolio manager in the research department of a large institutional money manager for almost 20 years. I was part of a team responsible for investing and managing 10s of billions of dollars. I have an MBA in finance, and I earned the Chartered Financial Analyst designation. Despite this prior experience, providing specific investment advice is not what I do in my book, in these audio lessons, or at Your Sherpa, LLC.

What **I *will*** do is **provide an overview of your options, introduce the language, and describe the general landscape** associated with savings and investing decisions. This is an important part of being financially literate. You will be ready if and when you decide to put your savings to work.

Perhaps the best starting point is ensuring that we all understand that **savings and investments are actually different**. Savings is the money you set aside for the future. Investing is more about putting your savings to work, to grow. Importantly, not all savings should be invested.

Think, protection versus growth. Some savings are really in effect 'spent' money: money saved and earmarked for a very near-term need. In this case, you can't put this money at risk because you don't have time to recover from losses, if they occurred. For this money, depositing in a bank is appropriate. It will be safe, in fact most deposits in the bank are insured. The bank will pay you a *small* amount of interest as they use your money to support loans to other bank customers. This type of lending and borrowing helps other people get home mortgages or small business loans and propels the broader economy through what academics call a multiplier effect.

Investing, on the other hand, is more about seeking growth and really putting your money to work for you. **Investing applies to longer time horizons in which you want to leverage compounding. Investing entails more risk** but over the long run you should be compensated with more reward, a higher return than you would achieve in a savings account. Since growth is not predictable, will not occur in a straight line, and you can lose money at any time, investing is not appropriate for money needed in the short-term.

Investing is a very broad topic; you could pursue a full degree program in finance or have a whole career in the investment field. Again, I will keep it at an overview level, and touch on some important terminology and concepts that will help you prepare to make savings and investing decisions.

Let's review some Investment Decisions and Considerations – First, the term <u>Allocation</u>

Allocation refers to your overall investment mix of cash, bonds, stocks, real estate, etc. An appropriate mix is **largely determined by your age** (that is, years until retirement) as this indicates your ability to ride through possible down periods in returns. Also, **a key factor determining your mix is your personal risk tolerance,** discussed later.

A second bit of terminology… <u>Diversification</u>

Diversification refers to mitigating risk, the risk that an investment may lose value or underperform other investments on a relative basis. Diversification is about *spreading out* your risk, *not concentrating* your risk in too few investments. You have likely heard the expression ***don't put all your eggs in one basket*.** Diversification is a form of risk management just in case one of your baskets spills and breaks *those* eggs. If that happens, you want *other* eggs that remained safe. If one of your investment decisions performs poorly, or even becomes worthless, you want a diverse set of other investments to potentially pick up the slack.

Some More terminology is -- <u>Risk Tolerance</u>

Risk tolerance refers to your *personal* ability to assume risk. Another expression you have likely heard is ***risk versus reward*.** Owning individual stocks or the whole stock market has more risk associated with it than holding a bank account or a bond, but over time they tend to reward you with higher returns. It is very difficult to predict the stock market direction over a short time period, but over the long-term the market should increase to at least reflect the long-term growth trajectory of corporate earnings plus dividends. At times, individual company fundamentals and macroeconomic conditions can take *jaw dropping* declines. **Risk tolerance is a personal and qualitative metric. It may be best illustrated by simply considering your ability to sleep at night knowing your investments.** People feel more pain associated with losses than joy associated with gains. So, when you consider risk versus reward, you need to have a sense of how you will *feel, cope, and behave* in turbulent times.

A bit more on Risk Management

We mentioned that **diversification is a form of investment *risk management*. But risk management isn't limited to investments.** We employ risk management in our everyday lives; **think of insurance**. There are many types of insurance: life, home, auto, and umbrella. The concept of insurance is basically that for a rather small or nominal amount, a premium, you pass the risk of a major loss onto another party (i.e., the insurance company). This major loss may be *statistically unlikely* but the magnitude, if it occurred, could be *devastating*, both as a disruption to your life and to your finances.

Another form of risk management may be the measures you take to protect your identity. Or even simply the common sense employed on a daily basis (for example, knowing not to access personal bank information on a public wi-fi!).

To wrap up, I'd like to give you a long-term goal. …it is called critical mass. Critical mass is a term used in several contexts. Generally, it means to reach a critical point of being sustained (for example, a sustainable reaction in the context of nuclear fission or sustainable growth in the context of a new business venture). In the context of saving and investing, you can think of critical mass as the *ultimate objective*. Reaching critical mass means you have successfully saved and built wealth *to the point* that your nest egg is large enough to generate income sufficient to live off. That is, you live your life and spend investment income, but your nest egg doesn't shrink. I did not create the term *critical mass* in the context of investing. A gentlemen named Bob Brinker coined the phrase. Bob Brinker's investment process inspired many people to work towards, what he called, *The Land of Critical Mass™*. I used to listen to him on the radio and he was my initial spark…getting me interested in finance, financial markets and the power of compounding. *Few* people reach investment critical mass but working towards it inspires a lifestyle of daily decisions to save and build wealth. That concludes this session, and the 3 sessions aimed at helping you to *Make Daily Decisions to Save and Build Wealth*!