1.How Will Your Investment Make Money?

After two years of saving and sacrifice - sweat and overtime - you have finally accumulated enough money to begin investing outside of your retirement accounts. You have just spent the afternoon with your new broker, while he or she went over a myriad of investment choices with you, explaining each one in detail and causing your head to swim.

Your broker presented you with several hypothetical scenarios outlining the overall rate of return that you could expect to receive in each case, until finally you decided to purchase some stock in a local company that you're somewhat familiar with.

But, as you drive away from his office, you think, "What exactly am I going to get out of this and how am I going to get it?"

When considering an investment's performance, it is sometimes easy to get distracted by the simple change in price it has returned (or is expected to return).

Investments, however, also can generate other forms of value aside from capital gains, including interest, dividends, and possibly certain tax breaks.

Instead of simply considering change in price, you should factor all of these value streams, in what is known as an investment's "total return."

Four Investment Ratios That Can Help You Make Money

1. Interest

Interest income is paid on any kind of debt instrument as compensation for loaning the investor's principal to the borrower or issuer. This type of income is paid by several different types of investments, listed as follows:

Fixed-income securities, such as CDs and bonds. The rate of interest is usually preset and lasts until the security matures or is called or put.

Demand deposit accounts, such as checking, savings and money market accounts. Depositors receive interest as compensation for parking their cash in the account from the depository institution.

Fixed annuities, which pay a set rate of interest on a tax-deferred basis until maturity.

Seller-financed mortgages, where the seller charges an agreed-upon rate of interest on the principal that is loaned to the buyer. Mutual funds that invest in the above vehicles.

No form of equity pays interest of any kind. Each of these debt instruments pays a stated rate of interest. This rate is usually fixed, but can be variable depending upon the terms of the investment.
The rates for demand deposit accounts usually fluctuate, according to changes in interest rates, while the rates for bonds, CDs and fixed annuity contracts usually stay constant until maturity. Interest-bearing investments are always tied to current interest rates and cannot, by nature, pay rates high enough to beat inflation over time, unless they are high-risk vehicles such as junk bonds.
Most interest-bearing securities carry a rating, such as AAA or BB, assigned by one of the major rating agencies, such as Standard and Poor's (S&P). If this rating declines after a security is issued, this could be a possible indicator that the issuer will default on their obligation. A noticeable decline in revenues, profits or liquidity could be another warning sign. Of course, in many cases, these changes will result in a lower rating.

2. Dividends

Dividends are a form of cash compensation for equity investors. They represent the portion of the company's earnings that are passed on to the shareholders, usually on either a monthly or quarterly basis.
Dividend income is similar to interest income in that it is usually paid at a stated rate for a set length of time. But dividends are only paid on stocks or from mutual funds that invest in stocks; however, not all stocks pay dividends. In general, only established corporations pay dividends, while small cap enterprises usually retain their cash for future growth.
Dividends are paid on both common and preferred stocks, although the rate is usually higher on preferred stocks than common. Dividends can also be either ordinary, which are taxed as ordinary income, or qualified, which are taxed as long-term capital gains. In most cases, companies are not required to pay dividends, at least on common stock. Because dividends are a function of corporate revenue, poor cash flow or profit margins can signal an upcoming reduction or absence of dividend payments to shareholders.
Dividend yields can vary, according to the type of security upon which they are paid; common stock dividends tend to fluctuate with a company's current profitability, while preferred stock dividends are generally tied to interest rates. Because they are considered higher-risk investments than bonds, the yields on

preferred stocks tend to float at a rate above that of CDs or most types of bonds, except perhaps junk bonds.

3. Capital Gains

Capital gains represent the appreciation in the price of a security or investment from the time that it was purchased. These gains can be either long or short term, depending upon whether the instrument sold was held for more than a year. Both equity and fixed-income securities can post gains (or losses). However, while fixed income securities can appreciate in price in the secondary market, they are designed primarily to pay current interest or dividends while stocks and real estate provide the bulk of their reward to investors in the form of capital gains.

Historically, the gains posted by stocks and real estate are the only investment returns that have outpaced inflation over time, which is one of their chief advantages. Of course, the markets move in two directions, and any security or investment capable of posting a gain can also result in a loss. Equities rise and fall with the overall markets as well as from corporate performance.

4. Tax Advantages

A few types of investments produce tax-advantaged income of various kinds. Working interests in oil and gas leases generate revenue that may be 15% tax-free because of the depletion allowance. Limited partnerships, which usually invest in either real estate or oil and gas, can pass through passive income, which is income generated from partnership activities that the investor is not actively involved in managing. Passive income can be written off with passive losses, which are usually expenses associated with operating the income-generating activities of the partnership.

Total Return

Of course, many types of investments provide more than one type of investment return. Common stocks can provide both dividends and capital gains. Fixed-income securities can also provide capital gains in addition to interest or dividend income, and partnerships can provide any or all of the above forms of income on a tax-advantaged basis. Total return is calculated by adding capital gains (or subtracting capital losses) to dividend or interest income and factoring in any tax savings.

2.Warren Buffet Investment Strategy

1. Stick With Long Term Value Investing Strategies

Don't let fear and greed change your investing criteria and values. Avoid being overwhelmed by outside forces that affect your emotions. Never sell into panic.

2. Invest in What You Understand

Buffet only invests in companies he understands and believes have stable or predictable products for the next 10 – 15 years. This is why he has typically avoided technology companies.

3. Invest Like You Are Buying the Entire Company

Treat investing in a stock as though you are buying the entire company. I always take a hard look at enterprise value because this is the total price of a company. In other words, it is the price you would be paying for the company if you could buy the whole company at current prices.

4. Companies with Competitive Advantages

Companies with pricing power, strategic assets, powerful brands, or other competitive advantages have the ability to outperform in good and challenging times. A long term investing strategy requires investing in companies that can weather both good and bad economic times.

5. Find Quality Companies

Buffet believes in quality investing. He would rather pay a fair price for a great company than a low price for a mediocre company.

6. Keep Cash On Hand

Investment opportunities become available through broad market corrections or individual stocks that become bargains. These are not predictable events; so cash on hand is an important concept in value investing.

7. Require a Margin of Safety

Purchasing stocks with a margin of safety below their intrinsic value reduces risk and provides an allowance for unforeseen negative events.

8. Compounding and Patience

Buffet believes in *long term value investing* because he understands the power of exponential growth. Companies with sustainable profits can pay and grow their dividends. There are few more powerful long term investing strategies than dividend growth compounding.

3.Book Value VS. Market Value: What's the Difference

1. Book Value VS. Market Value: An Overview

Valuing a listed company is a complex task, and several different measures are used to arrive at a fair valuation. While none of the methods is precise and each presents a different version with varying results, investors use them in combination to get a good understanding of how stocks have performed. Two most commonly used quantitative measures for valuing a company are market value and book value. This article compares the two popular factors, their differences, and how they can be used in analyzing companies.

2. Book Value

The book value literally means the value of a business according to its books (accounts) that is reflected through its financial statements. Theoretically, book value represents the total amount a company is worth if all its assets are sold and all the liabilities are paid back. This is the amount that the company's creditors and investors can expect to receive if the company is liquidated.

3. Book Value of Equity Per Share (BVPS)

Book Value Formula

Mathematically, book value is calculated as the difference between a company's total assets and total liabilities.

\text{Book value of a company} = \text{Total assets} - \text{Total liabilities}Book value of a company=Total assets−Total liabilities

For example, if Company XYZ has total assets of $100 million and total liabilities of $80 million, the book value of the company is $20 million. In a broad sense, this means that if the company sold off its assets and paid down its liabilities, the equity value or net worth of the business would be $20 million.

Total assets include all kinds of assets, such as cash and short term investments, total accounts receivable, inventories, net property, plant and equipment (PP&E), investments and advances, intangible assets like goodwill, and tangible assets. Total liabilities include items like short and long term debt obligations, accounts

payable, and deferred taxes.

4. Book Value Example

Deriving the book value of a company is straightforward since companies report total assets and total liabilities on their balance sheet on a quarterly and annual basis. Additionally, the book value is also available as shareholders' equity on the balance sheet. For example, technology leader Microsoft Corp.'s (MSFT) balance sheet for the fiscal year ending June 2018 reports total assets of $258.85 billion and total liabilities of $176.13 billion. It leads to a book value of ($258.85 billion - $176.13 billion) $82.72 billion. This is the same figure reported as shareholder's equity.

One must note that if the company has a component of minority interest, that value must be further reduced to arrive at the correct book value. Minority interest is the ownership of less than 50 percent of a subsidiary's equity by an investor or a company other than the parent company. For instance, retail giant Walmart Inc. (WMT) had total assets of $204.52 billion and total liabilities of $123.7 billion for the fiscal year ending January 2018, which gives its net worth as $80.82 billion. Additionally, the company had accumulated minority interest of $2.95 billion, which when reduced gives the net book value or shareholder's equity as $77.87 billion for Walmart during the given period.

Companies with a lot of machinery inventory and equipment, or financial instruments and assets tend to have large book values. In contrast, gaming companies, consultancies, fashion designers, or trading firms may have little to no book value because they mainly rely on human capital, which is a measure of the economic value of an employee's skill set. When book value is divided by the number of outstanding shares, we get the book value per share (BVPS) which can be used to make a per share comparison. Outstanding shares refer to a company's stock currently held by all its shareholders, including share blocks held by institutional investors and restricted shares.

5. Limitations of Book Value

One of the major issues with book value is that the figure is reported quarterly or annually. It is only after the reporting that an investor would know how the company's book value has changed over the months.

Book value is an accounting item and is subject to adjustments (e.g., depreciation) which may not be easy to understand and assess. If the company has been

depreciating its assets, one may need to check several years of financial statements to understand its impact. Additionally, due to depreciation-linked rules of accounting practices, a company may be forced to report a higher value of its equipment though its value may have gone down.

Book value may also not consider the realistic impact of claims on its assets, like those for loans. The book valuation may be different than the real value if the company is a bankruptcy candidate and has several liens against its assets.

Book value is not very useful for businesses relying heavily on human capital.

6. Market Value

The market value represents the value of a company according to the stock market. While market value is a generic term that represents the price an asset would get in the marketplace, it represents the market capitalization in the context of companies. It is the aggregate market value of a company represented as a dollar amount. Since it represents the "market" value of a company, it is computed based on the current market price (CMP) of its shares.

7. Market Value Formula

Market value—also known as market cap—is calculated by multiplying a company's outstanding shares by its current market price.

\text{Market cap of a company} = \text{Current market price (per share)} * \text{Total number of outstanding shares}Market cap of a company=Current market price (per share)*Total number of outstanding shares

If Company XYZ is trading at $25 per share and has 1 million shares outstanding, then the company's market value is $25 million. Market value is most often the number analysts, newspapers, and investors refer to when they mention the value of a company.

Since the market price of shares changes throughout the day, the market cap of a company also changes accordingly. Changes to the number of shares outstanding are rare as that number changes only when a company pursues certain types of corporate actions, due to which market cap changes are primarily attributed to per share price changes.

8. Market Value Example

Continuing the above-mentioned examples, the shares outstanding for Microsoft on June 29, 2018 (end of Microsoft's fiscal year) were 7.794 billion, and the stock closed at the price of $98.61 per share. The resulting market cap was (7.794 billion

* $98.61) $768.56 billion. This market value is more than nine times the book value of the company ($82.72 billion) calculated in the earlier section.

Similarly, Walmart had 3.01 billion shares outstanding and a closing price of $106.6 per share as of January 31, 2018 (end of Walmart's fiscal year). The firm's market value was (3.01 billion * $106.6) $320.866 billion, which is more than four times the book value of Walmart ($77.87 billion) calculated in the earlier section.

It is quite common to see the book value and market value differ significantly. The difference is attributed to several factors, including the company's operating model, its industrial sector, the nature of a company's assets and liabilities, and the company's specific attributes.

9. Market Value Limitations

While market cap represents the market perception of a company's valuation, it may not necessarily represent the true picture. It is common to see even mega-cap and large-cap stocks moving 3 to 5 percent up or down during a day's session. A stock often gets overbought or oversold, and relying solely on market cap valuations may not be the best method to assess a stock's realistic potential.

10. Book Value and Market Value Use

Most publicly listed companies fulfill their capital needs through a combination of debt and equity. Debt is raised by taking loans from banks and other financial institutions or by floating interest-paying corporate bonds. Equity capital is raised by listing the shares on the stock exchange through an initial public offering (IPO) or through other measures, such as follow-on issues, rights issues, and additional share sales. Debt capital requires payment of interest, as well as repayment of loaned money to the creditors; however, equity capital has no such obligation for the company as equity investors aim for dividend income or capital gains emerging from fluctuations in the stock prices.

Creditors who provide the necessary capital to the business are interested in the company's asset value as they are more concerned about repayment. Book value is used by creditors to determine how much capital to lend to the company since assets are typically used as collateral or determine a company's ability to pay back the loan over a given time. On the other hand, investors and traders are more interested in timely buying or selling of a stock at a fair price. Market value, when used in comparison with other measures, including book value, provides a fair idea of whether the stock is fairly valued, overvalued, or undervalued.

11. Comparing Book and Market Value

Most investors and traders use both values; there can be three different scenarios while comparing the book value and market value.

Book value greater than market value: If a company is trading at a market value which is lower than its book value, it usually indicates that the market has momentarily lost confidence in the company. It may be due to problems with the business, loss of important business-related lawsuits, or chances of financial anomalies. In other words, the market doesn't believe that the company is worth the value on its books or that there are enough assets to generate future profits and cash flows. Value investors often like to seek out companies in this category in hopes that the market perception turns out to be incorrect in the future. In this scenario, the market is giving investors an opportunity to buy a company for less than its stated net worth, meaning the stock price is lower than the company's book value. However, there is no guarantee that the price will rise in the future.

A market value greater than book value: When the market value exceeds the book value, the stock market is assigning a higher value to the company due to the potential of it and its assets' earnings power. It indicates that investors believe the company has excellent future prospects for growth, expansion, and increased profits that will eventually raise the book value of the company. They may also believe the value of the company is higher than what the current book value calculation shows. Consistently, profitable companies typically have market values greater than book values, and most of the companies in the top indexes meet this criterion, as seen from the examples of Microsoft and Walmart mentioned above. Growth investors may find such companies promising. However, it may also indicate overvalued or overbought stocks trading at a high price.

12. Book value equals market value:

The market sees no compelling reason to believe the company's assets are better or worse than what is stated on the balance sheet. A popular ratio that is used to compare market and book values is the price-to-book (P/B) ratio, which is calculated as the price per share divided by the book value per share. For example, a company has a P/B of 1, meaning that the book value and market value are equal. The next day, the market price drops and the P/B ratio becomes less than 1, meaning the market value is less than the book value (undervalued). The following day the market price zooms higher and creates a P/B ratio greater than 1, meaning

market value now exceeds book value (overvalued). Since prices change every second, it is possible to track and spot stocks which move from a P/B ratio of less than one to more than one and time the trades to maximize the profits.

4.How to Start Investing in Stocks: A Beginner's Guide

Let's say that you have $1,000 set aside, and you're ready to enter the world of investing. Or maybe you don't. Maybe you only have $10 extra a week, and you'd like to get into investing? In this article, we'll walk you through getting started as an investor and show you how to maximize your returns while minimizing your costs.

What Kind of Investor Are You?

Before you commit your money, you need to answer the question, what kind of investor am I? When opening a brokerage account, a broker like Charles Schwab or Fidelity will ask you about your investment goals and how much risk you're willing to take on. Some investors want to take an active hand in managing their money's growth, and some prefer to "set it and forget it." More "traditional" online brokers, like the two mentioned above, allow you to invest in stocks, bonds, ETFs, index funds and mutual funds. Investopedia's broker reviews will show you which brokers are best for every investor. Investopedia's *The Complete Guide to Choosing an Online Stock Broker* will give you step-by-step instructions on how to open and fund an account once you've decided which one is right for you.

1. Online Brokers

Brokers are either full-service or "discount." Full-service brokers, as the name implies, give the full range of traditional brokerage services, including financial advice for retirement, healthcare and everything related to money. They usually only deal with higher net-worth clients, and they can charge substantial fees, including a percent of your transactions, a percent of your assets they manage and a yearly membership fee. It's common to see minimum account sizes of $25,000 and up at full-service brokerages.

Discount brokers used to be the exception, but now they're the norm. According to a report by Charles Schwab, 58 percent of Americans say they will use some sort of roboadvice by 2025. As the space of financial services has progressed in the

21st century, online brokers have added more features including educational materials on their sites and mobile apps. Still, traditional brokers earn their high fees by giving advice detailed to your needs.
In addition, although there are a number of discount brokers with no (or very low) minimum deposit restrictions, you will be faced with other restrictions, and certain fees are charged to accounts that don't have a minimum deposit. This is something an investor should take into account if he or she wants to invest in stocks.

2. Roboadvisors

After the 2008 Financial Crisis, a new breed of investment advisor was born: the roboadvisor. Jon Stein and Eli Broverman of Betterment are often credited as the first in the space. Their mission was to use technology to lower costs for investors and streamline investment advice.
Since Betterment launched, other robo-first companies have been founded, and established online brokers like Charles Schwab have added robo-like advisory services. If you want an algorithm to make investment decisions for you, including tax-loss harvesting and rebalancing, a roboadvisor may be for you. And as the success of index investing has shown, if your goal is long-term wealth building, you might do better with a roboadvisor.
Investing Through Your Employer
If you’re on a tight budget, try to invest just one percent of your salary into the retirement plan available to you at work. The truth is, you probably won’t even miss a contribution that small. You'll also get a tax deduction, which will make the contribution even less painful. Once you're comfortable with a one percent contribution, maybe you can increase it as you get annual raises. You won't likely miss the additional contributions

3. Learn the Costs of Investing

As economists like to say, there's no free lunch. Though recently many brokers have been racing to lower or eliminate commissions on trades, and ETFs offer index investing to everyone who can trade with a bare-bones brokerage account, all brokers have to make money from their customers one way or another.
Opening an Account: What Are the Minimums?
Many financial institutions have minimum deposit requirements. In other words, they won't accept your account application unless you deposit a certain amount of money. Some firms won't even allow you to open an account with a sum as small

as $1,000. Some newcomers don't require minimum deposits, but often they lower other costs, like trading fees and account management fees, if you have a balance above a certain threshold.

4. Commissions

Investing in stocks can be very costly if you trade frequently, especially with a small amount of money available to invest. If your broker charges commission fees, every time that you trade stock, either through buying or selling, you will spend extra money. Trading fees range from the low end of $5 per trade but can be as high as $10 for some discount brokers.

Remember, a trade is an order to purchase shares in one company – if you want to purchase five different stocks at the same time, this is seen as five separate trades and you will be charged for each one.

Now, imagine that you decide to buy the stocks of those five companies with your $1,000. To do this, you will incur $50 in trading costs, which is equivalent to 5 percent of your $1,000. If you were to fully invest the $1,000, your account would be reduced to $950 after trading costs. This represents a 5 percent loss before your investments even have a chance to earn a cent!

If you were to sell these five stocks, you would once again incur the costs of the trades, which would be another $50. To make the round trip (buying and selling) on these five stocks would cost you $100, or 10 percent of your initial deposit amount of $1,000. If your investments don't earn enough to cover this, you have lost money by just entering and exiting positions.

5. Mutual Fund Fees

There are many fees an investor will incur when investing in mutual funds. One of the most important fees to focus on is the management expense ratio (MER), which is charged by the management team each year, based on the amount of assets in the fund. The MER ranges from 0.05 percent to 0.7 percent annually and varies depending on the type of fund. But the higher the MER, the worse it is for the fund's investors. It doesn't end there, however. You'll also see a number of sales charges called "loads" when you buy mutual funds. In terms of the beginning investor, the mutual fund fees are actually an advantage relative to the commissions on stocks. The reason for this is that the fees are the same, regardless of the amount you invest. Therefore, as long as you meet the minimum requirement to open an account, you can invest as little as $50 or $100 per month

in a mutual fund. The term for this is called dollar cost averaging (DCA), and it can be a great way to start investing.

6. Reduce Risk with Diversification

Diversification is considered to be the only free lunch in investing. In a nutshell, by investing in a range of assets, you reduce the risk of one investment's performance severely hurting the return of your overall investment. You could think of it as financial jargon for "don't put all of your eggs in one basket."

In terms of diversification, the greatest amount of difficulty in doing this will come from investments in stocks. This was illustrated in the commissions section of the article, where we discussed how the costs of investing in a large number of stocks could be detrimental to the portfolio. With a $1,000 deposit, it is nearly impossible to have a well-diversified portfolio, so be aware that you may need to invest in one or two companies (at the most) to begin with. This will increase your risk.

This is where the major benefit of mutual funds or exchange-traded funds (ETFs) come into focus. Both types of securities tend to have a large number of stocks and other investments within the fund, which makes them more diversified than a single stock.

7. A Small Step Toward a Large Future

It is possible to invest if you are just starting out with a small amount of money. It's more complicated than just selecting the right investment (a feat that is difficult enough in itself) and you have to be aware of the restrictions that you face as a new investor.

You'll have to do your homework to find the minimum deposit requirements and then compare the commissions to other brokers. Chances are, you won't be able to cost-effectively buy individual stocks and still be diversified with a small amount of money. You will also need to make a choice on which broker you would like to open an account with. To make sense of all the different platforms, browse the different online broker and roboadvisor options in Investopedia's broker center.

5.Smart Investing on a Small Budget

A common myth about investing is that a big fat bank account is required just to get started. In reality, the process of building a solid portfolio can begin with a few thousand—or even a few hundred—dollars.

This story offers specific advice, organized by the amount you may have available to begin your investments. But it first covers some smart moves low-rollers can make to kickstart a savings and investment program.

1. Strategies to Start

Whether you're planning to invest a little or a quite a lot, in safe bets or high-risk gambles, these steps should help get your plans off on the right track.

2. Automate Savings

The diligence to dependably set aside a certain amount in savings every month will reap rewards in the long run. If you lack the willpower or organization to do that alone, technological help is available via various smartphone/computer applications.

The apps that make saving the least painless are those that simply round up your purchases and other transactions, and put aside the "savings."

KEY TAKEAWAYS

- Set aside a certain amount to save regularly
- Look into savings apps that round up your purchases and save the small change.
- First, pay off high-interest debts.
- Take advantage of retirement plans.
- Focus on low-fee options, at every investment level.
- Think about the level of risk you are comfortable with, and how that changes over time.
- Trade up to better choices as your investment pot grows.

Acorns puts the money into one of several low-cost ETF portfolios; these are good vehicles for small savers, as we cover below. Qapital adds the option to automatically transfer money, based on rules you choose, to an FDIC-insured Wells Fargo account. Chime, which is an online bank as well as an app, offers a savings account that automatically sets aside 10% of every paycheck you deposit, among other features.

Short of using these apps, check with your bank about their own apps, and other ways you might automatically transfer funds from non-savings accounts to those

better suited to savings and investment.

3. Deal With Your Debts

Before you begin to save, analyze what it's costing you to carry debts you already have and consider how rapidly you might discharge those. After all, high-interest credit cards can carry rates of 20% or more and some student loans have interest rates over 10%. Those rates far eclipse the average annual earnings of 7% or so that the U.S. stock market has returned over time.

If you're carrying a lot of high-interest debt, then, it makes more sense to pay off at least some of it before you make investments. While you can't predict the exact return on most of your investments, you can be certain that retiring debt with a 20% interest rate one year early is as good as earning a 20% return on your money.

4. Consider Your Retirement

A key goal of saving and investing, even at an early age, should be to help ensure you have enough money after you stop working. One priority in your planning, then, should be to take full advantage of the inducements dangled by governments and employers to encourage retirement security.

If your company offers a 401(k) retirement plan, don't overlook it. That's doubly the case if your company matches part or all of your contribution to the plan.

For example, if you have an income of $50,000 and contribute $3,000, or 6% of your income, to your 401(k) plan, your employer might match that by contributing an additional $3,000. A less generous employer might contribute up to only 3%, adding $1,500 to your $3,000 contribution.

You'll *always* want to invest enough to get the full amount of your employer's match. Not to do so is essentially to throw money away.

401(k)s and some other retirement vehicles are also powerful investments because of their favorable tax treatment. Many allow you to contribute with pre-tax dollars, which reduces your tax burden in the year you contribute. With others, such as Roth 401(k)s and IRAs, you contribute with after-tax income but withdraw the funds without tax, which can reduce your tax hit on the year of withdrawal. And remember, if your money has grown for many years, there will be much more than you originally contributed so those tax-free withdrawals will truly be worth it.

In both scenarios, the earnings on what you invest accumulate tax-free within the account. Even if your employer doesn't offer any match on your 401(k) contributions, a plan is still a good deal.

5. Invest Your Tax Refund

If you find it hard to save money throughout the year, consider setting aside part or all of your tax refund as a way to get started with investing. It's one of the few moments in the year where you're likely to get a windfall that you weren't already counting on.

6. Recommendations by Investment Amount

Before the specifics, a few general points are worth underlining. No matter your net worth, it's important to minimize your investment fees, whether it's on a checking account, a mutual fund, or any other financial product.

That's especially the case when you're investing on a budget because fixed fees will take a bigger chunk of your savings. A $100 annual fee on a $1 million account is trivial, but a $100 fee on a $5,000 account is a hefty financial hit. If you're investing on a budget, carefully choose the costs associated with where you put your money.

You'll also need to weigh likely returns on your investments against the level of risk you're comfortable with taking and that's appropriate to your age. In general, your portfolio should become steadily less risky as you approach retirement.

7. How to Invest $500

It may seem like a small amount to work with, but $500 can go farther than you might think in starting an investment portfolio

If you prefer to play it safe, park your sum in a certificate of deposit from a bank or other lender or use it to purchase short-term Treasury bills, which can be purchased through an online broker. The growth potential with both options is limited but the risks are virtually zero. It's a way to earn a little on your money until your nest egg grows to the point where other options are available.

For those who are comfortable with a little more risk, a range of choices are available, even for small investors, that promise greater returns than CDs or T-bills. One is a dividend reinvestment plan (DRIP). You buy shares of stock, and your dividends are automatically used to purchase additional shares or even fractional shares.

This is a great choice for small investors because the shares are purchased at a discount and without paying a sales commission to a broker. Buying a single share of a company's stock will get you started.

Another option for starting small is an exchange-traded fund (ETF), most of which

require no minimum investment. Unlike most mutual funds, ETFs typically feature a passive management structure, which translates to lower ongoing costs. However, among other drawbacks to ETFs, you must pay fees on their transactions, To lessen these charges, consider using a discount broker that does not charge a commission or plan to invest less often, perhaps investing larger amounts quarterly rather than making small monthly purchases.

Towards the top of the risk continuum, there's investing in peer-to-peer lending. Crowdfunders connect investors with money to lend and entrepreneurs trying to fund new ventures. As the loans are repaid, each investor receives a share of the interest in proportion to the amount they have invested. Some crowdfunding platforms have high minimums to open an account, such as the $1,000 one for Lending Club, but you can get started with others, such as Prosper, for as little as $25.

Crowdfunding offers high risk, since many new ventures fail, but also the prospect of higher earnings. Generally, annual returns fall in the 5% to 8% range but can climb to 30% or more for investors who are willing to take a big risk, or are simply lucky enough to back an especially profitable newcomer.

8. How to Invest $1,000

If you're saving for retirement or a home purchase that's some years away, you might look for a low-fee target-date fund with a relatively low minimum investment, typically of $1,000 or so.

With this type of fund, you choose the target date. The investments in the fund are automatically adjusted over time, with the overall mix moving from riskier to safer as your target date becomes closer.

Why is this important? When you're just starting out, you have time. You can make riskier investments that might earn higher returns. But as you near your target date, especially if that's your retirement date, you want to protect yourself from sudden losses that can derail your plans.

With that $1,000, you also could consider purchasing individual stock shares, which come with higher risk but can generate higher returns. Investing in individual stocks that pay dividends is a smart strategy. You will have the option of receiving the dividends as cash payouts or reinvesting them in additional shares.

9. How to Invest $3,000

This investment level allows access to additional options, including more mutual

funds. While some funds require a minimum investment of $1,000 or less, a larger sum is more common, such as the $3,000 required by Vanguard for most of its funds.

Among the many fund types, consider looking first to an index fund, a type of mutual fund that tracks a specific market index, such as the Standard & Poor 500 or the Dow Jones Industrials and offers relatively low fees. Like ETFs, index funds are passively managed, which means a lower expense ratio, which in turn moderates fees.

The goal of an index fund is to at least match the performance of the index. It also gives you broad exposure to a number of asset classes.

10. How to Invest $5,000

The possibilities become broader at the $5,000 level, including more options for investing in real estate. While $5,000 isn't enough to purchase property, or even to make a down payment, it's enough to get a stake in real estate in several other ways.

The first is to invest in a real estate investment trust (REIT). This is a corporation that owns a group of properties or mortgages that produce a continuous stream of income. As a REIT investor, you're entitled to a share of the income generated by the underlying properties. REITs are required by law to pay out 90% of their income to investors as dividends annually. REITs can be traded or non-traded, with the latter carrying much higher upfront fees.

Real estate crowdfunding is a second option. Real estate crowdfunding platforms are now permitted to accept investments from both accredited and non-accredited investors. Many platforms set the minimum investment for gaining entry to private real estate deals at $5,000.

Investors can also choose between debt and equity investments in commercial and residential properties, depending on the platform. Returns for debt investments range from 8% to 12% a year. Equity investments can see higher yields if the value of the property increases. Keep in mind, this type of investment can carry more risks than more traditional investments.

11. The Bottom Line

Investing can get complicated, but the basics are simple. Maximize the amount you save and your employer's contributions. Minimize taxes and fees. Make smart choices with your limited resources.

That said, building a portfolio can also raise such complexities as how best to balance the risk of some investments against their potential returns. Consider

getting help. Given technology and the fierce competition for your investments, more resources than ever are available. Those options include robo-advisors, virtual assistants that can help you create a balanced portfolio at a low price, and fee-only financial advisors, who do not depend on income from commissions on the products they sell you. The hardest part of investing is getting started. And the sooner you do so, the more you should make, by odds. It's as simple as that.

6. How Do Interest Rates Affect the Stock Market?

The investment community and the financial media tend to obsess over interest rates—the cost someone pays for the use of someone else's money— and with good reason. When the Federal Open Market Committee (FOMC) sets the target for the federal funds rate at which banks borrow from and lend to each other, it has a ripple effect across the entire U.S. economy, not to mention the U.S. stock market. And, while it usually takes at least 12 months for any increase or decrease in interest rates to be felt in a widespread economic way, the market's response to a change (or news of a potential change) is often more immediate.

Understanding the relationship between interest rates and the stock market can help investors understand how changes might affect their investments and how to make better financial decisions.

The Interest Rate That Impacts Stocks

The interest rate that moves markets is the federal funds rate. Also known as the discount rate, this is the rate depository institutions are charged for borrowing money from Federal Reserve banks.

The federal funds rate is used by the Federal Reserve (the Fed) to attempt to control inflation. Basically, by increasing the federal funds rate, the Fed attempts to shrink the supply of money available for purchasing or doing things, by making money more expensive to obtain. Conversely, when it decreases the federal funds rate, the Fed is increasing the money supply and, by making it cheaper to borrow, encouraging spending. Other countries' central banks do the same thing for the same reason. Here is a chart from the Fed showing fluctuations in the federal funds rate over the past 20 years:

Why is this number, what one bank pays another, so significant? Because the prime interest rate—the interest rate commercial banks charge their most credit-worthy customers—is largely based on the federal funds rate. It also forms the basis for mortgage loan rates, credit card annual percentage rates (APRs) and a host of other consumer and business loan rates.

What Happens When Interest Rates Rise?

When the Fed increases the federal funds rate, it does not directly affect the stock market. The only truly direct effect is that borrowing money from the Fed is more expensive for banks. But, as noted above, increases in the federal funds rate have a ripple effect.

Because it costs them more to borrow money, financial institutions often increase the rates they charge their customers to borrow money. Individuals are affected through increases to credit card and mortgage interest rates, especially if these loans carry a variable interest rate. This has the effect of decreasing the amount of money consumers can spend. After all, people still have to pay the bills, and when those bills become more expensive, households are left with less disposable income. This means people will spend less discretionary money, which will affect businesses' revenues and profits.

But businesses are affected in a more direct way as well because they also borrow money from banks to run and expand their operations. When the banks make borrowing more expensive, companies might not borrow as much and will pay higher rates of interest on their loans. Less business spending can slow the growth of a company; it might curtail expansion plans or new ventures, or even induce cutbacks. There might be a decrease in earnings as well, which, for a public company, usually means the stock price takes a hit.

Interest Rates and the Stock Market

So now we see how those ripples can rock the stock market. If a company is seen as cutting back on its growth or is less profitable—either through higher debt expenses or less revenue—the estimated amount of future cash flows will drop. All else being equal, this will lower the price of the company's stock. (For related reading, see: *Taking Stock of Discounted Cash Flow*.)

If enough companies experience declines in their stock prices, the whole market, or the key indexes (e.g., Dow Jones Industrial Average, S&P 500) many people equate with the market, will go down. With a lowered expectation in the growth and future cash flows of the company, investors will not get as much growth from stock price appreciation, making stock ownership less desirable. Furthermore, investing in equities can be viewed as too risky compared to other investments.

However, some sectors do benefit from interest rate hikes. One sector that tends to benefit most is the financial industry. Banks, brokerages, mortgage companies and insurance companies' earnings often increase as interest rates move higher, because they can charge more for lending.

Changes in interest rates can create opportunities for investors. To be able to take advantage or to hedge against these swings in interest rates you would need an investment account through a broker. Investopedia has a list of some of the best brokers in the industry for those who are looking to trade or invest.

Interest Rates and the Bond Market

Interest rates also affect bond prices and the return on CDs, T-bonds and T-bills. There is an inverse relationship between bond prices and interest rates, meaning as interest rates rise, bond prices fall, and vice versa. The longer the maturity of the bond, the more it will fluctuate in relation to interest rates. (For related reading, see: *How Bond Market Pricing Works*.)

When the Fed raises the federal funds rate, newly offered government securities, such as Treasury bills and bonds, are often viewed as the safest investments and will usually experience a corresponding increase in interest rates. In other words, the "risk-free" rate of return goes up, making these investments more desirable. As the risk-free rate goes up, the total return required for investing in stocks also increases. Therefore, if the required risk premium decreases while the potential return remains the same or dips lower, investors might feel stocks have become too risky and will put their money elsewhere.

One way governments and businesses raise money is through the sale of bonds. As interest rates move up, the cost of borrowing becomes more expensive. This means demand for lower-yield bonds will drop, causing their price to drop. As interest rates fall, it becomes easier to borrow money, causing many companies to issue new bonds to finance new ventures. This will cause the demand for higher-yielding bonds to increase, forcing bond prices higher. Issuers of callable bonds may choose to refinance by calling their existing bonds so they can lock in a lower interest rate.

For income-oriented investors, reducing the federal funds rate means a decreased opportunity to make money from interest. Newly issued treasuries and annuities won't pay as much. A decrease in interest rates will prompt investors to move money from the bond market to the equity market, which then starts to rise with the influx of new capital.

What Happens When Interest Rates Fall?

When the economy is slowing, the Federal Reserve cuts the federal funds rate to stimulate financial activity. A decrease in interest rates by the Fed has the opposite effect of a rate hike. Investors and economists alike view lower interest rates as catalysts for growth—a benefit to personal and corporate borrowing, which in turn leads to greater profits and a robust economy. Consumers will spend more,

with the lower interest rates making them feel they can finally afford to buy that new house or send the kids to a private school. Businesses will enjoy the ability to finance operations, acquisitions and expansions at a cheaper rate, thereby increasing their future earnings potential, which, in turn, leads to higher stock prices. Particular winners of lower federal funds rates are dividend-paying sectors such as utilities and real estate investment trusts (REITs). Additionally, large companies with stable cash flows and strong balance sheets benefit from cheaper debt financing. (For related reading, see: *Do Interest Rate Changes Affect Dividend Payers?*)

Impact of Interest Rates on Stocks

Nothing has to actually happen to consumers or companies for the stock market to react to interest-rate changes. Rising or falling interest rates also affect investors' psychology, and the markets are nothing if not psychological. When the Fed announces a hike, both businesses and consumers will cut back on spending, which will cause earnings to fall and stock prices to drop, everyone thinks, and the market tumbles in anticipation. On the other hand, when the Fed announces a cut, the assumption is consumers and businesses will increase spending and investment, causing stock prices to rise.

However, if expectations differ significantly from the Fed's actions, these generalized, conventional reactions may not apply. For example, let's say the word on the street is the Fed is going to cut interest rates by 50 basis points at its next meeting, but the Fed announces a drop of only 25 basis points. The news may actually cause stocks to decline because assumptions of a 50-basis-points cut had already been priced into the market.

The business cycle, and where the economy is in it, can also affect the market's reaction. At the onset of a weakening economy, the modest boost provided by lower rates is not enough to offset the loss of economic activity, and stocks continue to decline. Conversely, towards the end of a boom cycle, when the Fed is moving in to raise rates—a nod to improved corporate profits—certain sectors often continue to do well, such as technology stocks, growth stocks and entertainment/recreational company stocks.