St. Joseph School finlit Course
7th Grade & 8th Grade
Winter Term 2022 – 2023
February 6, 2023

Planning for the future

Class 26: Financial Objectives

NITWOM

News In The World Of Money

02/03/2023: The U.S. Bureau of Labor Statistics reported nonfarm payrolls increased by 517,000 in January 2023 -- crushing the 187,000 estimate. The unemployment rate fell to 3.4% versus the estimate of 3.6%. This is a 53-year low -- the lowest unemployment rate since May 1969. However, the strong employment data may keep wage inflation at elevated levels. Paradoxically, a stronger than expected labor market may result in the U.S. Federal Reserve holding interest rates higher for longer. [Source]

Recap Investments Introduction Questionnaire

Large Group Exercise

How familiar are you with investing?

a. Not familiar at all

- 1

b. Somewhat familiar

- 17

c. Very familiar

- 1

d. Prefer not to answer

- 0

Have you ever invested in stocks, bonds, or other investment products?

a. No

- 7

b. Yes

- 11

c. Prefer not to answer

- 1

What are your future financial goals? *(Select all that apply)*

a. Saving for a down payment on a home

- 1+1+1 = 3

b. Paying for college education

- 1+1+1+1+1 = 5

c. Retiring comfortably

- 1+1+1+1+1+1+1+1+1+1+1+1+1+1+1 = 15

d. Building an emergency fund

- 1

e. Other (please share)

- Getting lots of money
- Before retirement financial comfort
- Retire early (FIRE)
- Having a nice house in the city
- Owning the Los Angeles Lakers
- Live comfortably without working
- Having a good passive income

f. Prefer not to answer

- 1

What concerns you about investing? *(Select all that apply)*

a. Lack of knowledge about investments

- 1+1+1+1+1+1+1+1 = 8

b. Uncertainty about market conditions

- 1+1+1 = 3

c. Fear of losing money

- 1+1+1+1+1+1+1+1+1+1+1 = 11

d. Difficulty understanding investment products and fees

- +1+1+1 = 3

e. Other (please discuss)

- When buying and selling

f. Prefer not to answer

- 1

How confident are you in making money decisions?

a. Not confident at all

- 0

b. Somewhat confident

- 1+1+1+1+1+1+1+1+1+1+1+1+1+1 = 14

c. Very confident

- 1+1+1+1+1 = 5

Financial Objectives Overview

- Recap: setting measurable goals based on **time horizon** should guide all investment strategies
- **Time horizon**
  - the period an investor expects to hold investments to support a specific financial objective

S.M.A.R.T. Criteria

A financial objective does not exist if it does not satisfy all S.M.A.R.T criteria

S — Specific

Financial objectives should be **clear**, **definite**, and **unambiguous**

M — Measurable

Financial objectives should be **quantifiable** to measure progress towards desired results

A — Attainable

Financial objectives should be **possible to achieve** – stretch goals or stretch financial objectives are o.k.

R — Relevant

Financial objectives should relate to **financial purposes**

T — Time Bound

Financial objectives should have a **defined timeline** with start and target dates

Guide to Develop Financial Objectives

List →

- Make a list of **what matters to you** & what you want from life
- Your list could be practical or fanciful, including your **aspirations**, **dreams**, and **hopes**

→ Categorize →

- Categorize the items in your list. Identify what is…
- within **reach**,
- will **take a bit of time**, or
- what should be part of a **long-term plan**

→ Frame →

- Frame each list item around **S.M.A.R.T. criteria** to create financial objectives
- S.M.A.R.T. criteria can apply to other things too (ex. academics, sports, etc.)

→ Prioritize →

- Prioritize your S.M.A.R.T. financial objectives from **most important to you to least important** to you
- Are the least important items still relevant to you?

→ Develop →

- Develop the **investment strategies** around your S.M.A.R.T. financial objectives
- Investors often have multiple investment strategies

→ Monitor

- **Monitor progress** to the S.M.A.R.T. financial objectives periodically
- Monitoring schedule should be appropriate to each financial objective time bound

When circumstances change or major life events occur

Large Group Exercise

Identify whether this is a good or bad financial objective

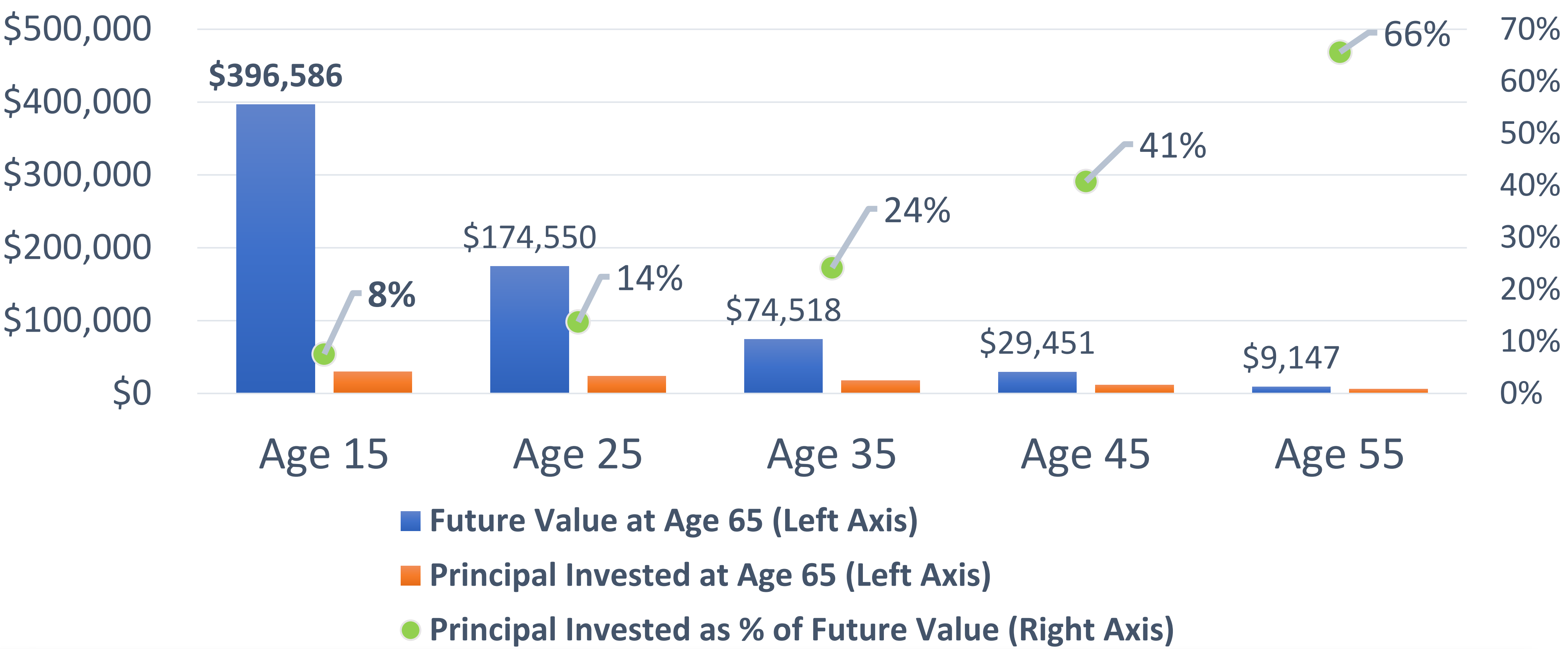
S.M.A.R.T. or not financial objective? I will…

1. retire with $1 million or more in my retirement accounts
2. invest 15% of my gross earned income from age 23 towards my age 65+ post retirement financial needs
3. be rich by the age of 25
4. have paid off 100% of my student loans within 10 years of college graduation
5. be the CEO of a company in the S&P 500
6. own 1 positive cashflow investment property by the time I am age 25
7. own a yacht
8. pay off my credit card in full every month, without exceptions

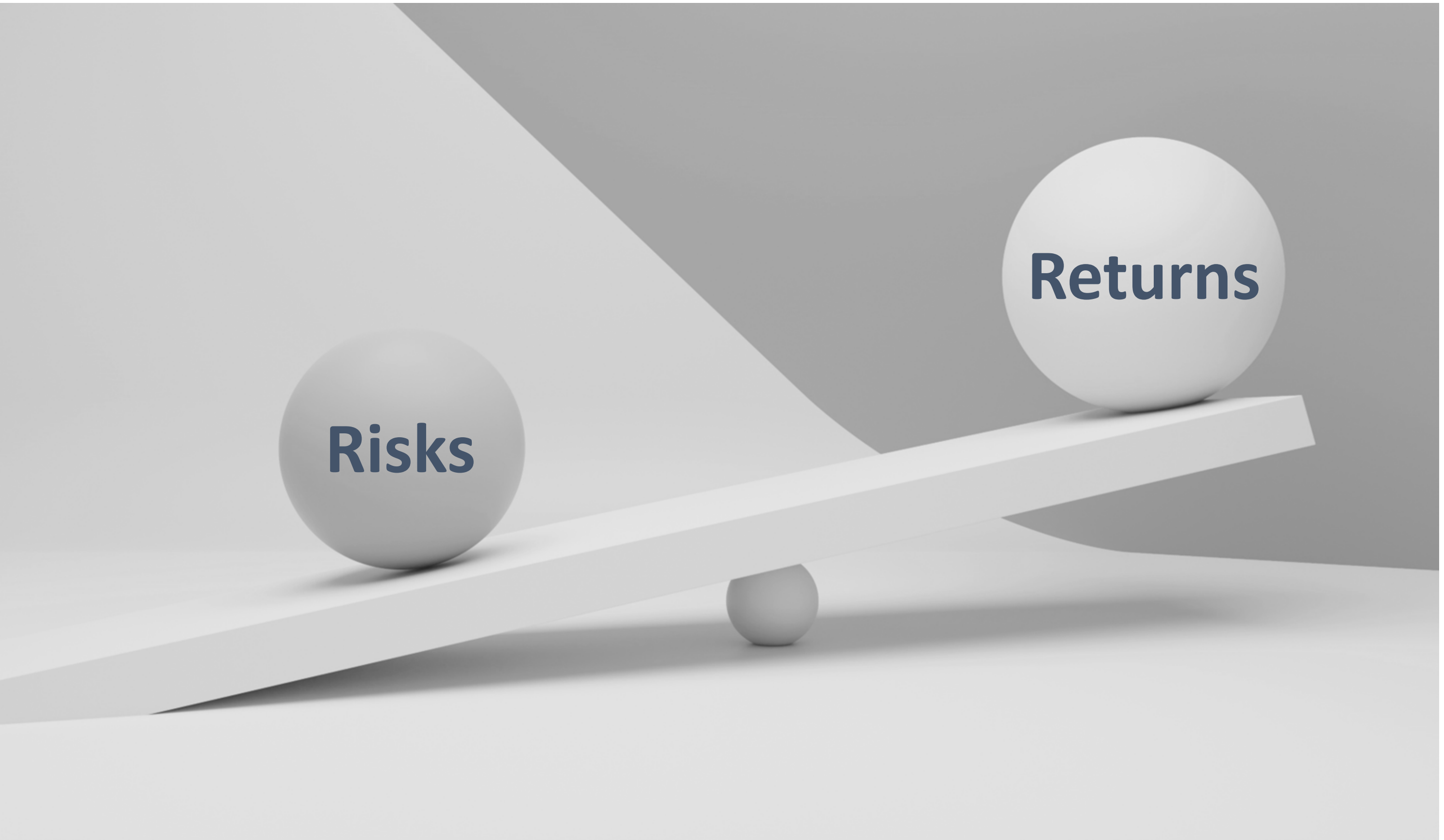
S.M.A.R.T. or not financial objective? I will…

1. retire with $1 million or more in my retirement accounts **[Not time bound. When is retirement expected?]**
2. invest 15% of my gross earned income from age 23 towards my age 65+ post retirement financial needs
3. be rich by the age of 25 **[Not measurable. How is rich quantified? May also not be attainable, depending on the measure. Is it attainable by age 25?]**
4. have paid off 100% of my student loans within 10 years of college graduation
5. be the CEO of a company in the S&P 500 **[Not relevant. Not time bound.]**
6. own 1 positive cashflow investment property by the time I am age 25
7. own a yacht **[Not time bound. Own a yacht by when?]**
8. pay off my credit card in full every month, without exceptions **[May not be attainable. Paying off a credit card in full every month is advisable, but emergencies do arise. Including the clause "without exception," leaves this likely to fail over a long period.]**

Invest **$50 per month** starting at various ages **until age 65** in a portfolio earning **8% annual returns**, compounded monthly



Bottom line: For long-term investing, starting young helps because of the effect of earnings on earnings.



Recap Risk and Return Tradeoffs

- **Risk** means the potential to **lose principal** on investments
- **Returns** mean the **financial gains** on investments
- Equities, such as stocks, *generally* provide opportunities for **higher returns,** but carry **heavier risks**
- Fixed income, such as bonds, *generally* carry **lighter risk**, but provide opportunities for **lower returns**


?
What factors do you think might affect the risk of principal losses on investments?

Investment Risks: Two categories

Manageable Risk

- technically this is known as **idiosyncratic risk**
- risks related to an **individual** security or **very specific group** of securities
- **Example**: The U.S. government implements windfall profit taxes on oil companies. What might this do to oil company stocks?
- You can do something about it

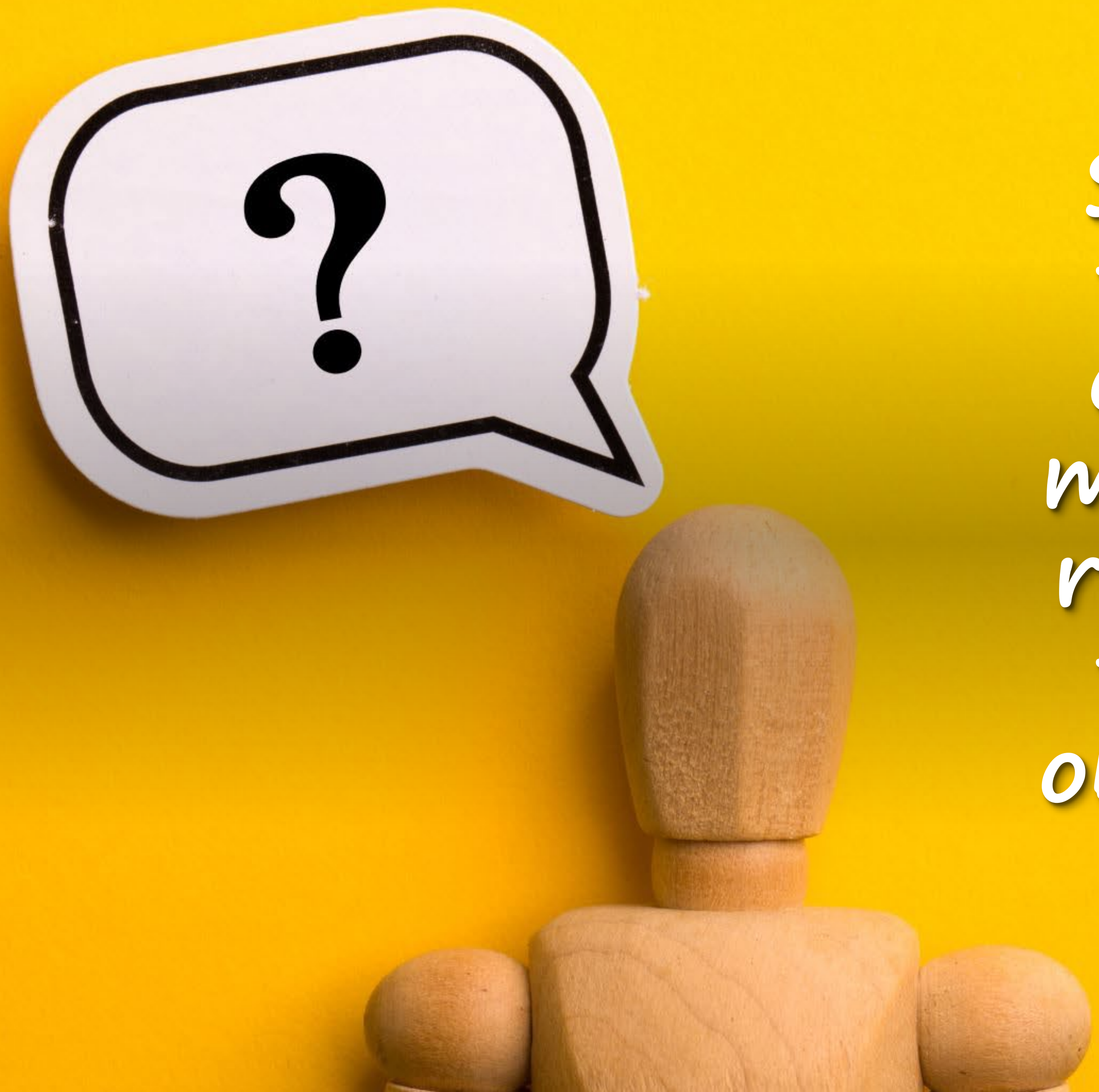
Unmanageable Risk

- technically this is known as **systematic risk** or **market risk**
- risks related to **all** securities or **many groups** of securities
- **Example**: A 10-mile-wide asteroid strikes the earth. What does this mean for humanity, let alone the financial markets?
- You cannot do anything about it

Risk Tolerance

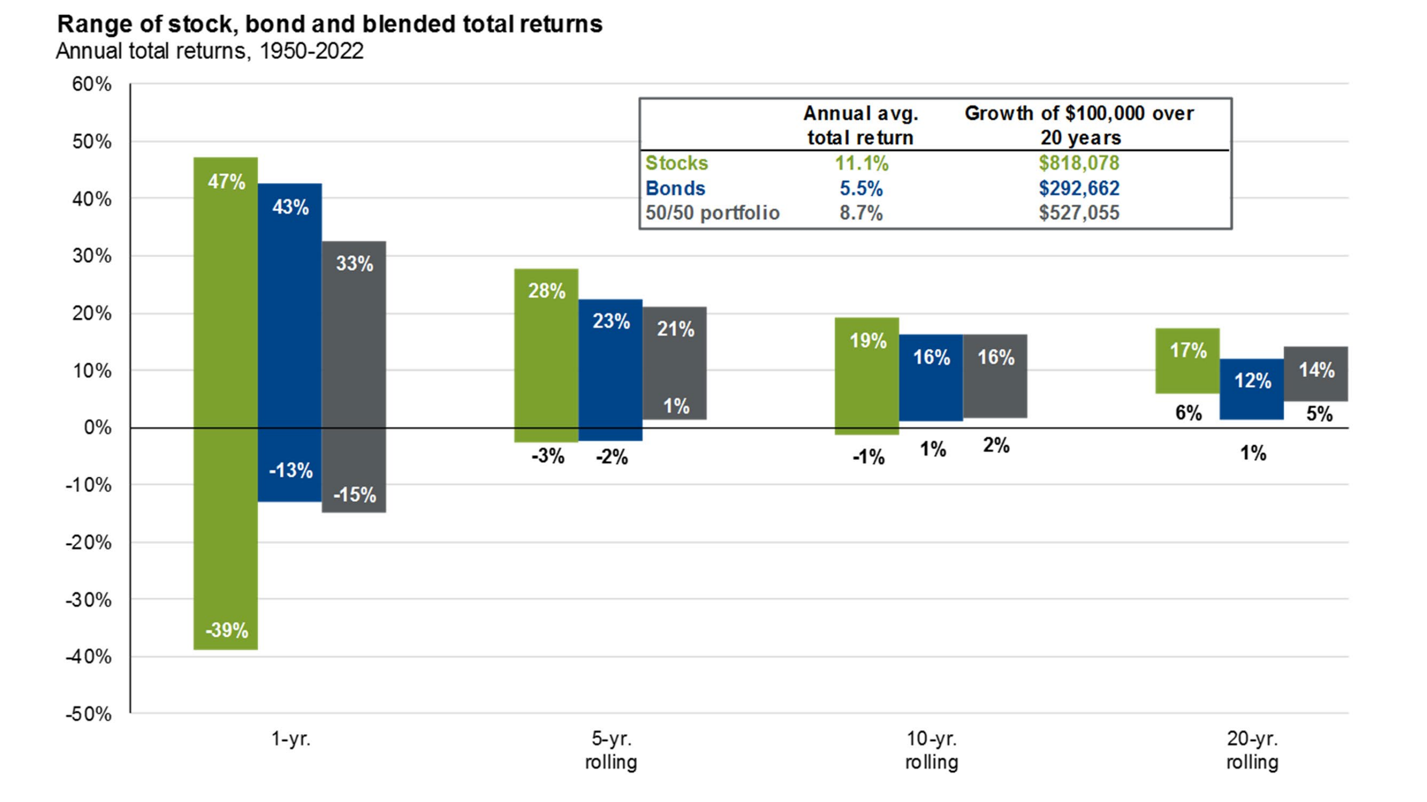
The degree of **principal loss** an investor is **willing to endure**, given the **volatility** in the value of an investment.

Different types of investments are suitable for different levels of risk tolerance.



Should shorter term financial objectives take more risk or less risk than longer term financial objectives? Why?

Time, Diversification, and the Volatility of Returns



Historical returns by holding period for stocks, bonds, & 50/50 portfolio, rebalanced annually, over different time horizons. The bars show the highest and lowest return during each of the time periods (1-year, 5-year rolling, 10-year rolling, & 20-year rolling).

Source: Bloomberg, FactSet, Federal Reserve, Robert Shiller, Strategas/Ibbotson, J.P. Morgan Asset Management. Returns shown are based on calendar year returns from 1950 to 2021. Stocks represent the S&P 500 Shiller Composite and Bonds represent Strategas/Ibbotson for periods from 1950 to 2010 and Bloomberg Aggregate thereafter. Growth of $100,000 is based on annual average total returns from 1950 to 2022. Guide to the Markets – U.S. Data are as of January 31, 2023.

Financial Objectives & Risk Tolerance

Individual and Large Group Exercise

List three of your personal aspirations or dreams:

a. ___________

b. ___________

c. ___________

Reframe the three items above into **S.M.A.R.T. financial objectives** that could help you attain each of your personal aspirations or dreams:

a. ___________

b. ___________

c. ___________

On a scale of 1 to 7, how comfortable are you with the possibility of losing money in the short-term to potentially earn a higher return over the long-term?

1. Not at all comfortable
2.
3.
4. Neutral
5.
6.
7. Extremely Comfortable

You invest $1,000 toward a financial objective that has a 5-year time horizon. How would you feel if your investment lost 10% after 1-year, decreasing in value to $900?

a. I would be very concerned and consider selling my investment.

b. I would be concerned but would not consider selling my investment.

c. I would be slightly concerned but would not consider selling my investment.

d. I would not be concerned and would not consider selling my investment.

After 1 more year your $900 investment loses 10% more in value, decreasing in value to $810. How would you feel?

a. I would be very concerned and consider selling my investment.

b. I would be concerned but would not consider selling my investment.

c. I would be slightly concerned but would not consider selling my investment.

d. I would not be concerned and would not consider selling my investment.

Coming Up on Investments – Deep Dives Into…

1. Introduction,
2. Financial Objectives,
3. **Managing Risk**
4. Equities (Stocks),
5. Fixed Income (Bonds),
6. Mutual Funds & ETFs, &
7. Putting it All Together.

Key Takeaways

- All financial objectives should be framed into S.M.A.R.T. criteria
- A risk of principal loss is inherent in every investment, so it is important to understand your personal risk tolerance
- Risks impacting a single-security or specific group of securities are manageable, whereas risks impacting all or many groups of securities are unmanageable