

“... focus on learning as much as you can, by reading and also by actively investing some of your own money!”



Stocks, Bonds & Mutual Funds:

What's the Difference?

“It's all greek to me!” You may be frustrated because you feel that way about investing in securities. It all seems so complicated and you fear that you might do the wrong thing and loose a whole lot of money! Hopefully, this article will help you to get a very basic grasp of stocks, bonds and mutual funds, three of the main types of securities that people buy and how they make money from them.

A privately owned corporation changes into a publicly owned corporation in order to raise money or capital. It raises this capital by either issuing stocks or bonds on the public markets.

A STOCK GIVES YOU OWNERSHIP IN A CORPORATION

When a corporation raises money by issuing stock, it is essentially selling shares or portions of the company to the buyer. When you buy a share, you own a part of that company. And if the company is well managed and earns a substantial profit, the value of the stock increases – company earnings drive stock prices up. When the stock has a greater value, people are anxious to get a piece of the action and the greater the demand for a stock, the higher the stock price to the new buyer.

When the price of a stock increases and is worth more than you initially paid, that elevated difference is your profit, or appreciation. You gain tangible appreciation when you sell stock for more than its original price. In other words, you make money when the company's stock price goes up through appreciation and you sell the shares.

Another way you can make money from stocks is through dividends. When a company makes a profit, they may decide to share some of these profits with their shareholders. They do this by paying out a portion of their profits for each share of stock you own in the company. Usually the dividends are paid quarterly: every 3 months.

A BOND MAKES YOU A LENDER TO A CORPORATION OR GOVERNMENT ENTITY

When you buy a bond issued by either a corporation or a government entity (like a municipality or state), you are loaning money to the issuer. In exchange, the issuer pays you an agreed upon percentage of interest on your loan, and returns your loan at an agreed upon time or maturity date.

When you buy a bond, you are not buying a share of the company – you are not getting ownership. You earn money by receiving an annual interest on your principal, which is the amount of money you originally paid on the bond.

MUTUAL FUNDS HELP YOU TO DIVERSIFY YOUR INVESTMENTS & TAKE ADVANTAGE OF PROFESSIONAL EXPERTISE

When you buy mutual funds, you are pooling your money with other investors to buy securities. You and other people with a common investment goal hire an investment manager and he/she does all the driving. For a small fee, the investment manager invests your money for you and for others like you in a variety of securities that might include a mixture of both stocks and bonds.

Two key advantages of mutual funds are professional management and diversification.

When you buy mutual funds, you have a profession fund manager who is well versed in investing making the buy/sell decisions for each security – they do this with the benefit of many analysts and strategists. In other words, you don't have to be an expert to invest, you just have to know one.

In addition, when you buy mutual funds, you are diversified over many companies. A mutual fund may own as many as 100 companies in its portfolio – this means you can own dozens of securities, which would normally be too expensive to purchase individually. The advantage of diversification is that you can mitigate the risk you take on when owning an individual stock. With an individual stock, when the company's value goes down, all your shares go down. With a mutual fund, when the value of a stock in the portfolio goes down, there is a good chance that another stock in the same portfolio is going up and therefore balancing the impact of the devalued stock.

THE MILLIONAIRE ATTITUDE

Investing in securities is not a disease (though it can become like an addiction when you really begin to have fun) so you should not avoid it like the plague. The main obstacle to investing is a lack of knowledge, so focus on learning as much as you can, both by reading about the securities market, but also by actively taking part in the fun by investing some of your own money!