Session II: Where to Invest

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Financial Consultant
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Seek the advice of tax and legal advisors

This presentation is designed to provide accurate and authoritative information regarding the subject matter covered. You should understand that Wells Fargo Advisors is not engaged in rendering legal, accounting or tax-preparation services. If tax or legal advice is required, you should seek the services of an appropriate, competent professional.

Wells Fargo Advisors’ view is that investment decisions should be based on investment merit, not solely on tax considerations. However, the effects of taxes are a critical factor in achieving a desired after-tax return on your investment.

The information provided is based on internal and external sources that are considered reliable; however, the accuracy of the information is not guaranteed. You should direct specific questions on taxes as they relate to your situation to your tax advisor.
My Favorite Rules

The first rule of investing is don't lose money; the second rule is - don't forget rule number one.

-Warren Buffet

No one can count your money better than you.”

-Troy E. Bryant

Pay yourself first!
Where to Begin

1. Develop a Plan (6 mos., 1 year, 3 years)
   Where will you be? What will you need?
2. Emergency Fund 6-12 months of Expenses. Start Small: 1-3 months
3. Limit the use of Credit Cards if unable to pay off at the end of each month. Do not buy material item that you do not need on credit!
4. Make a Budget & Use Coupons!
   Stick to the Budget.
Today’s retirement reality

Retirement savings – it’s up to you now

From 1980 to 2010, the changes in employer sponsored retirement plan offerings has changed dramatically.

Mckinsey & Company, 2011
Where to Begin

6. Contribute to your Employer Savings Plan
   *At least up to the full match-this is free money that you don’t want to pass up.

7. Evaluate Living conditions

8. Shop current Insurance(s), loans, and/or bank accounts.

9. Learn to cook!

10. Revisit your plan Annually
Simple interest

Year 1

\[
\frac{1,000 \times 1.05}{1,050}
\]

Year 2

\[
\frac{1,000 \times 1.05}{1,050}
\]

Year 3

\[
\frac{1,000 \times 1.05}{1,050}
\]
Compound interest

Year 1: $1,000 \times 1.05 = $1,050

Year 2: $1,050 \times 1.05 = $1,103

Year 3: $1,103 \times 1.05 = $1,158

Year 4: $1,158 \times 1.05 = $1,216

Year 5: $1,216 \times 1.05 = $1,277
A dollar per day from ages 25 to 65 years old

For illustrative purposes only and not intended to reflect actual performance of any particular investment.
For illustrative purposes only and not intended to reflect actual performance of any particular investment. This is a general investment rule of thumb that assumes the investment’s principal value and rate of return remain constant and that all interest and/or dividends are reinvested annually at the same rate of return.
Past performance is not a guarantee of future results. Diversification does not eliminate the risk of experiencing investment losses. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Risk and return are based on annual data over the period 1970-2015 and are measured by standard deviation and arithmetic mean, respectively. Arithmetic mean is defined as a simple average of returns. Standard deviation is the fluctuation of returns around the arithmetic average return of the investment. The higher the standard deviation, the greater the variability (and thus risk) of the investment returns. Stocks are represented by the Ibbotson Large-Company Stock Index and bonds by the 20-year U.S. government bond.

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Inflation’s powerful effects

One dollar today: $1.00
Five years from now: $0.82
Ten years from now: $0.66
Twenty years from now: $0.44

Assumes a 4% inflation rate.
Why invest in stocks?

- Potential inflation hedge
- Growth potential
- May issue dividends
- Total-return potential
Facts about stock ownership

- Stock investors own shares of a company
- There are a number of ways to invest in stocks:
  - Individually
  - Mutual funds
  - Defined portfolios
  - Variable annuities
  - Private money managers
Dividends

- Portion of company’s profits paid to shareholders
- Income investors choose companies with consistent dividend payments
Yield

\[
\text{Annual cash dividend} \div \text{Current stock price} = \text{Current yield}
\]
Yield

\[
\frac{\text{Annual Cash Dividend}}{\text{Current Stock Price}} = \text{Current Yield}
\]

\[
\frac{\$2}{\$50} = 4\% \text{ Yield}
\]
Earnings per share (EPS)

- Key number in determining a company’s investment value

\[
\text{Net income} \div \text{Common stock outstanding} = \text{EPS}
\]
Payout ratio

- Important number for income investors
- Dividend-to-EPS ratio
Ex-dividend date

- Ex-dividend date means “without the current dividend.”
- If you buy stock after the ex-dividend date, the seller will receive the current dividend.

<table>
<thead>
<tr>
<th>Monday</th>
<th>Tuesday</th>
<th>Wednesday</th>
<th>Thursday</th>
<th>Friday</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td><strong>Ex-dividend</strong></td>
<td><strong>Bought stock without dividend</strong></td>
<td><strong>Record date</strong></td>
</tr>
</tbody>
</table>
Stock split

- Before split:
  100 shares at $100 = $10,000

- After 4-for-1 split:
  400 shares at $25 = $10,000

- Before reverse split:
  10,000 shares at $1 = $10,000

- After 25-to-1 reverse split:
  400 shares at $25 = $10,000
How to invest in stocks

- Establish goals
- Establish your risk tolerance
- Determine what to buy
Bonds

- You are a lender to the company
- You earn interest on the money you lend
Corporate bonds

- Annual interest and yields

\[
\begin{array}{c}
$1,000 \\
\times 5.50\% \\
\hline
$55
\end{array}
\]

Annual interest
Corporate bonds

- Annual interest and yields

\[ \frac{\$1,000 \times 5.50\%}{\$55} = \frac{\$55}{\$1,030} = 5.34\% \text{ current yield} \]
Bond yields

- Example:
  - 10 years to maturity
  - 5.50% coupon rate
  - Paid $30 premium over par $1,000
  - Callable in five years for $1,000
- 5.11% = yield to maturity
- 4.81% = yield to call
Government bonds

- $5,000 and $10,000 denominations
- Backed by the full faith of the government
- Risks include:
  - Country risk
  - Political risk
  - Inflation risk
  - Interest-rate risk
Tax-free municipal bonds

- Interest is free from federal taxes and sometimes state taxes
- $5,000 denominations
Tax-free municipal bonds

- General obligation
- Revenue
Taxable investment vs. tax-free municipal bonds

### Taxable

- **$10,000**
- x 4.5%
- $450 interest
- x 28%
- $126 taxes

- $ 450
- - 126
- = **$324** after taxes
## Taxable investment vs. tax-free municipal bonds

<table>
<thead>
<tr>
<th>Taxable</th>
<th>Tax-free municipal</th>
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<tbody>
<tr>
<td><strong>$10,000</strong></td>
<td><strong>$10,000</strong></td>
</tr>
<tr>
<td>x 4.5%</td>
<td>x 3.5%</td>
</tr>
<tr>
<td><strong>$450 interest</strong></td>
<td><strong>$350 interest</strong></td>
</tr>
<tr>
<td>x 28%</td>
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</tr>
<tr>
<td><strong>$126 taxes</strong></td>
<td><strong>$98 taxes</strong></td>
</tr>
<tr>
<td><strong>$450</strong></td>
<td><strong>$350</strong></td>
</tr>
<tr>
<td>- 126</td>
<td>- 0</td>
</tr>
<tr>
<td><strong>$324 after taxes</strong></td>
<td><strong>$350 after taxes</strong></td>
</tr>
</tbody>
</table>
Taxable-equivalent yield

\[
\frac{100 \times \text{Tax-exempt yield}}{100\% - \text{Investor’s tax bracket}} = \text{Taxable-equivalent yield}
\]

Example:

\[
\frac{100 \times 3.5\%}{100 - 28\%} = 4.86\%
\]
**Investment-grade-bond ratings**

<table>
<thead>
<tr>
<th></th>
<th>S&amp;P (+ or -)</th>
<th>Moody’s (1, 2 or 3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Superior</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
<tr>
<td>Excellent</td>
<td>AA</td>
<td>Aa</td>
</tr>
<tr>
<td>Favorable</td>
<td>A</td>
<td>A</td>
</tr>
<tr>
<td>Average</td>
<td>BBB</td>
<td>Baa</td>
</tr>
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Mutual fund advantages

- Professional management
- Diversification
- Pooled money
- Liquidity
Mutual fund pricing

- Front-end load
- Back-end load
- No load
- All funds have management fees
Fund families

- Exchange privilege
- Include funds managed to suit various investment risk and return objectives:
  - Growth
  - Income
  - Conservative
  - Aggressive
Taxation of mutual funds

- Dividends — taxed as they occur
- Trading profits — taxed as they occur
- Exchanges — taxed as they occur
Exchange-traded funds (ETFs)

- Index fund
- Track one specific index
- Buy/sell like stocks
- Price set by underlying index
Important disclosures

- Insurance products are offered through our affiliated non-bank insurance agencies.
- Dividends are not guaranteed and are subject to change or elimination.
- Investing in fixed income securities involves certain risks, such as market risk if sold prior to maturity and credit risk, especially if investing in high-yield bonds, which have lower ratings and are subject to greater volatility. All fixed income investments may be worth less than their original cost upon redemption or maturity.
- Yields and market value will fluctuate so that your investment, if sold prior to maturity, may be worth more or less than its original cost.
- Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline of the value of your investment.
- Mutual funds are sold by prospectus. Please consider the investment objectives, risks, charges, and expenses carefully before investing. The prospectus, and, if available, the summary prospectus, which contain this and other information, can be obtained by calling your Financial Advisor. Read the prospectus and, if available, the summary prospectus, carefully before you invest.
- Exchange traded funds (ETFs) seek investment results that, before expenses, generally correspond to the price and yield of a particular index. There is no assurance that the price and yield performance of the index can be fully matched.
- Ibbotson Large-Company Stock Index represents the S&P 90 Index from 1926-1956 and the S&P 500 Index thereafter.
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