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PIMCO EDUCATION

The What, Why and How of Investing

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What is an asset allocation?
Why worry about retirement investing now?
How do I pick an advisor?

Asking questions is the best way to gain understanding, but investors aren't always sure where to find answers.

This small book offers simple, practical responses to some of the most commonly asked questions about investing. It will introduce you to the fundamentals, including investing terms, concepts and strategies.


What?

What is investing?

Investing is the act of committing money now (for example buying shares in a company) with the goal of receiving more money in the future.

What are stocks?

Stocks are a unit of ownership in a company. Companies issue shares of stock to raise money. The initial price of a share is based on a company's estimated worth. After that, the price fluctuates based on supply and demand for the shares by investors.

What are bonds?

Bonds represent a loan or a way to borrow money. A company, state or government issues bonds to raise money. The issuer agrees to pay periodic interest payments for the term of the bond and to pay back the full amount borrowed at the end of the bond's life (called maturity).

What?

What is a portfolio?

An investment portfolio is a collection of investments. An investor can buy a single security (for example a stock or a bond) or they can hold numerous securities in a portfolio.

What is asset allocation?

Asset allocation is how an investor distributes their money between different types of investments, such as stocks, bonds and cash. Asset allocation can help balance a portfolio's risk and return (a strategy known as diversification).

What?

What are mutual funds?

Mutual funds are investments that pool money from many investors to buy securities, such as stocks or bonds. An investor buys a share in the fund (and does not directly own any of the actual securities in the fund). The price of a share (called its net asset value or NAV) is the combined value of all of the securities in the fund divided by the number of shares outstanding. The price fluctuates daily with the changing prices of the securities.

What are exchange-traded funds?

Exchange-traded funds, or ETFs, are investments that pool money from many investors to buy securities, such as stocks or bonds, similar to mutual funds. But, unlike mutual funds, ETFs trade like a common stock on a stock exchange. Because ETFs trade on an exchange, they allow for intraday tradability and offer transparency. The price of an ETF may fluctuate throughout the day as they are bought and sold.

What?

What is a benchmark?

A benchmark is a standard against which to measure investment performance. In most cases, an investment's benchmark is a market index or a combination of indexes. An index tracks the performance of a selected basket of securities, such as all listed stocks or all government bonds. Indexes are unmanaged and an investor cannot invest directly in an index.

What is active management?

Active management is an investment strategy where the manager of the portfolio seeks to select securities and initiate trades with the goal of achieving the investment objective. In contrast, passive management is an investment strategy where the manager typically seeks to buy and hold a portfolio that represents a benchmark in an effort to track benchmark performance.

What?

What return can I expect from my investment?

It is impossible to accurately predict future returns. Over the last 20 years, stocks (as measured by the S&P 500 Index) returned an average of 9.80% per year and bonds (as measured by the Bloomberg U.S. Aggregate Bond Index) returned an average of 3.10% per year.* It is important to note that past performance is no guarantee of future results.

*As of 31 December 2022.

What is risk tolerance?

All investments carry some degree of risk. These risks include the chance that an investor will lose the money they invested. Investors generally require more return potential to take on more risk. Each investor must determine how much risk they are comfortable with – their risk tolerance level.

What is volatility?

The price of a security (such as a share of stock and a bond) goes up and down based on supply and demand pressures from investors. Volatility measures how much a security's price typically fluctuates.


Why?

Why invest?

Investing can help individuals reach their financial goals. Individuals may invest to increase their wealth (called capital appreciation), generate income or maintain the money they have (capital preservation).

Why not keep my money in cash?

Individuals are sometimes tempted to keep the bulk of savings as cash or in other short-term investments (such as CDs and money markets) to reduce their risk levels. But, these investments typically offer the lowest return potential, making it difficult to reach financial goals.

Why?

Why work with financial professional?

The financial markets are increasingly complex. Individuals may not have the time or interest in staying on top of changing conditions and actively managing a portfolio. A financial advisor can offer these individuals important benefits, including helping to develop custom investment plans, recommending specific investments, and monitoring markets and portfolio performance.

Why?

Why diversify my portfolio?

Diversification is an investment strategy that helps spread out risk exposures by investing a portfolio across different asset classes. In this way, if any single investment or asset class does badly others might compensate by performing well, potentially smoothing returns overall.

Why start investing early?

Time can be a big advantage in investing. An investor who starts early and invests consistently can accumulate more assets. In addition, the longer time frame may allow an investor to better ride out volatility and to potentially realize the benefits of compounding. Compounding is when earnings on an investment are reinvested in the investment, potentially generating additional earnings.

Why?

Why is consistency important?

Market conditions change. Security prices go up and down. Investors may be tempted to try and time when to buy and sell investments, but history shows that creating a plan and sticking with it is most often a smarter strategy.

Why?

Why worry about retirement now?

People are living longer, meaning many individuals may spend decades in retirement. Financing those years will require sufficient retirement savings. The sooner an individual starts investing for retirement the better, especially if the investments can be done within a retirement account (such as an IRA or a 401(k) available to investors in the U.S.). There are restrictions, but many contributions to a retirement account are tax deferred in the U.S. until they are withdrawn in retirement.

Why?


How?

How do I get started?

The first step is decide how involved an individual wants to be in selecting and managing their investments, or if they'd rather work with a financial advisor. In either case, an individual will need to identify their investment goal (what you need the money for, such as financing a child's college education or retirement), their investment timeframe (how long until you need the money) and their risk tolerance. With that information the investor (and their advisor if they have one) can develop an investment plan.

How?

How much do I need to start investing?

An individual should be able to cover their necessary expenses and have some money set aside for an emergency before investing. Any money after that can be invested. Beginning investors may want to consider investing 10% of their income (including contributions to a retirement account).

How?

How can I grow my invested assets?

Investors primarily interested in growing their assets are likely pursuing a capital appreciation strategy. Capital appreciation is an increase in the price or value of an investment. Stocks have historically provided the best opportunity for capital appreciation over time, but bonds can also offer appreciation potential. There are no guarantees that the value of stock or bond investments will appreciate and in fact they can lose value.

How?

How can I preserve my money?

Investors primarily interested in maintaining the principle value of their money are pursuing a capital preservation strategy. Historically less risky investments such as CDs, money market accounts, and interest bearing bank accounts can maintain their value, but offer low return potential. For an increased risk, bonds can offer return potential that will help investors keep pace with inflation and move towards financial goals. All investments involve risk and there are no guarantees that bonds or any other investment will deliver a positive return or that they will not lose money.

How?

How can I generate income?

Investors interested in income may consider several strategies, including dividend-paying stocks, bonds and short-term investments. Selecting the appropriate strategy will depend on an individual's situation, including the amount of income needed, their investment time frame and their risk tolerance.

How?

How do I balance short- and long-term goals?

Most individuals are investing for more than one goal. These can include longer-term goals such as accumulating assets for retirement and more immediate goals such as generating income to supplement earnings. Investors may be tempted to prioritize short-term goals, but it is important to take advantage of time to achieve long term goals. A professional financial advisor can be helpful in balancing these goals and selecting appropriate investments to pursue both.

How?

How do I manage volatility?

Investors who are uncomfortable with volatility can adopt one or more strategies that may help reduce it. These include focusing on less volatile types of securities (such as certain types of bonds) and diversifying money across investments. There is no guarantee that any of these strategies will reduce or eliminate volatility.

How?

How often should I check and/or change my investments?

Scrutinizing every fluctuation in the market or in the value of an investment can create a lot of anxiety. Investors may instead want to set a schedule to review performance and make any adjustments. It is important to keep in mind, however, that a disciplined approach to a long-term investment strategy may yield the best results.

How?

How do I choose an advisor?

Investors looking for a financial advisor will want to ensure that they do their due diligence. Make sure the individual is licensed and that he or she has references. Ask about their investment philosophy, their services, their fee structure and their availability. Beyond that, selecting a financial professional should be a very personal process.

How?

How can I learn more about investing?

There is no end of available information on investing, from educational content to current analysis. The challenge is finding a reliable, relatable source. Individuals who would like to continue their education journey with PIMCO can visit pimco.com/resources/education.

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