Assignments

Financial Plan Assignments

Open your copy of your Investment Plan Investment Plan Example Template (LT05A). Make sure you understand the terminology related to investment plans. I will discuss many aspects of this plan in upcoming sections.

First, you will not have only one portfolio for your investments; you will likely have many portfolios, all of which are important parts of your Investment Plan. Review your goals and objectives. What are you trying to accomplish individually and as a family through investing? With your investments, what are you trying to accomplish? Think through your general investment guidelines in Section IIA for both Stage 1 and Stage 2, and fill in those sections.

Using Expected Return Simulation and Benchmarks (LT27) , input your stock and bond allocations from your work you have done in the previous section.

There are four different asset classes for equities or stocks that I have data for. Large-cap stocks are the largest and biggest companies, generally with market capitalization (or shares outstanding multiplied by share price) of over $10 billion dollars.

Small-cap stocks have market capitalization generally between $250 million and $2 billion dollars. International stocks are those registered on exchanges outside the United States. And emerging markets are stocks of companies listed outside the U.S. and outside the major developed markets.

In bonds and cash, there are two different asset classes. Treasury bonds are long-term government securities, which are government debt with maturities generally one year or more. Treasury bills are government debt with maturities less than one year.

Real Estate Investment Trusts (REITs) are neither stocks nor bonds but have components of both.

Using the dropdown boxes in Expected Return Simulation and Benchmarks (LT27), try to come up with a preliminary target asset allocation. This is not your final target but just a preliminary pass.

Second, determine your investment constraints. When will you need money from your investments and why? Now is a good time to think about these needs. Fill out the constraints on Section II.B.1-4. on liquidity, time horizon, taxes, and unique needs. Your average and marginal tax rates should also be added and will come from your section on Tax Planning.

Finally, determine your policies. I recommend you make a first pass at your policies and then refine them as you learn more about investments. Major policies include:

> **III.A.1. Acceptable asset classes:** Decide now what you will invest in and what you will not invest in. I recommend against asset classes where you have no discernible

advantage.

III.A.2. Total assets: What is the maximum amount you will invest in any single asset? Remember the principle of diversification.

III.A.3. Short selling or buying on margin: Decide if you will use debt to invest. I recommend against it. Do not invest with borrowed money.

III.A.4 Unacceptable asset classes: What asset classes will you not invest in? Make the decision now. I recommend against foreign currencies, options, futures, derivatives, and collectibles and other

III.B.1-2. Investment benchmarks: Determine your investment benchmarks for each of your asset classes. I strongly recommend a minimum of four asset classes, so you will have at least four investment benchmarks. Suggestions for benchmarks for the various asset classes can be found in Expected Return Simulation and Benchmarks (LT27).

III.C.1-2. Asset allocation strategy: Determine your target and minimum and maximum allocations for your two different stages.

III.D.1. Investment strategy: Determine how you will invest. Will it be mutual funds or individual stocks? I strongly recommend mutual funds, at least initially, when your assets are few.

III.E. Funding strategy: Determine your funding strategy. How will you save money for investing and saving? What is your goal to save each week or each month? How will you keep your priorities in order?

III.F.1. New investments strategy: What is the maximum amount you will invest in new investments? I recommend not investing more than 5 to 10 percent in any new investment (except for broad-based mutual funds with more than 50+ assets).

III.F.2. Investments in company stock: Think about the maximum you will have in your retirement fund in investments of your company's stock. I recommend no more than about 10 percent due to diversification concerns.

III.F.3. Unlisted investments: Finally, what is the maximum amount you will include in unlisted investments, i.e., investments that are not listed on a recognized stock exchange? While I recommend you not invest in assets that are not listed, it is your choice.