THE ELEMENTS

The Key to a Balanced Stock Portfolio

Chris Douthit

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Letter from Chris

At some point, people realize they need to start saving money for the future. This could be in preparation for buying a home, saving for retirement, creating a college fund for their children, or any other possible money-saving scenario. However, holding money in cash is usually not the best investment approach. Money should be invested. Unfortunately, people new to the investing world are often afraid of putting their money at risk or just don't know what to do, so never take the initiative to get started.

The good news is, in today's world, investing is very simple to do. You don't have to have a finance degree to put your money to work in a wise investment. Long gone are the days that you had to rely on a broker to give you solid investment advice and hope that he's working in your best interest.

Today there's an arsenal of tools out there that make investing a fairly straightforward process, something anyone can do with only a reasonable amount of effort. Remember, nobody cares more about your money than you do, so it's up to you to make sure your money grows and outpaces the economy, which is easily attainable with a smart investment approach.

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How to Start Investing

If you don't have a finance degree or are not already working in the industry, then investing in stocks may seem a bit intimidating for a new investor. That's why investment funds and full-service brokers are often the first choices of novice investors.

It makes sense to leave the investing in the hands of the professionals, doesn't it? But what if I tell you that investing on your own can be just as, if not more profitable? You can make your own investment decisions without having to pay high advisory or management fees, and still do just as good, and often, much better.

But before you jump in and invest any money, there are some basic concepts that you must understand:

Company stock is composed of many shares. A share represents partial ownership of the company, in proportion to the total number of shares. The shares will give you voting and dividends privileges depending on the number of shares you own.

You need a broker to act as an intermediary between you and the stock exchange, as you can't invest directly in the market. You don't have to hire the services of a brokerage firm. Nowadays, many online discount brokers allow you to invest on your own for lower fees.

A properly build portfolio is composed of stocks from different industries so that you won't be overexposed to a possible downturn in a single sector. But stocks are expensive, if you can only afford to invest in a couple of companies at the moment, that is fine. Just keep in mind that diversifying becomes more relevant as your portfolio matures, and the capital invested grows.

It's also vital, investing in different types of stocks. In this ebook, we are going to explain the basic concepts behind the different kinds of stocks, the benefits, and risks associated with each, then we are going to give you some tips that will help you use them to their maximum potential.

Calculating Return on Investment

Before we begin, it's essential to understand how you can measure the return on your investment. You can calculate the percentage of profit using this formula:

$$\textbf{ROI=}\ \frac{(\text{Sell Price - Buy Price}) * \text{Shares} + \text{Dividends}}{\text{Buy Price} * \text{Shares}} \times 100$$

For instance, let's suppose that you purchased 100 shares of XYZ company at $25 per share. Eight years later, you were able to sell the shares for $37 each. During the eight years, you obtained $750 ($93.75 per year) in dividends. Your ROI for the trade would be:

$$\textbf{ROI=}\ \frac{(\$37-\$25) * 100 + \$750}{\$25 * 100} \times 100$$

Meaning that the $2500 invested turned into $4400.

You don't have to memorize the formula, as most online brokers automatically calculate the ROI for you. But they often miss to include the fees and dividends in the metric, so knowing how to do the calculation on your own can come in handy.

Now that you understood the basics let's move on to the most relevant types of stock that you should be aware of before you start investing.

Growth Stocks

Growth stocks are the most pursued type of stock in the financial industry.

Those are stocks that have the potential (at least in theory) to appreciate at a faster rate than the market. The best growth stock performers can double or triple the investment over a short period. That's the reason they are so popular between traders.

Naturally, as the potential benefits are higher, the companies' inherent risks are very high as well. The companies, usually, hasn't been proven on the market, are very leveraged, and doesn't pay dividends or aren't profitable yet. For that reason, the stocks are very volatile, but if you are looking for faster growth, that's what you want.

Despite its many disadvantages, investing in those types of stocks can be worth the risk. Companies like Google (GOOG), Facebook (FB), or Microsoft (MSFT) were once considered growth stocks. Now, these companies are worth more than some countries. The investors who trusted these companies from the beginning multiplied their money.

Here are some tips that will help you to find the best growth stocks:

Invest in Disrupting Companies

To magnify your results, you have to invest in companies that have exponential expansion potential. Disrupting companies are looking to create a new category or looking for a better way to do something. Industries like banking have existed for as long as money itself, they sure are a safe investment, but they are not inventing revolutionary ideas any time soon. Instead, betting on new, transcendental industries like biotech, technology, or artificial intelligence are more exciting ideas for a growth stock looking to disrupt an industry.

A company that comes to mind is Netflix (NFLX). Their main competitor Blockbuster, the once-dominant player in the home movie industry, failed to see the future and was taken out by the new disrupting content providing company, Netflix. However, it is even worse than that. In 2000 Reed Hastings, one of the founders of Netflix, met with the CEO of Blockbuster John Antioco and the rest of the Blockbuster decision-making team to discuss a partnership. As the story goes, Hastings was told no, basically being laughed out of the room.

The fact is, John Antioco could not see the future, clearly, this was the worst decision he could have made. Blockbuster never stood a chance, by having thousands of retail locations and much higher costs, it could not compete on price scale with Netflix. Throughout the next ten years, Blockbuster was slowly taken out by the very company they laughed at, only to officially go out of business in 2010. Today, Netflix has a market cap of over $190 billion.

Buy Stocks that can Beat the Benchmark

All companies' annual report growth forecasts look amazing. But, are the projections translating into sales and stock performance? Analyzing the historical stock prices is always essential as it tells you the market's enthusiasm for the company.

Timing the Market

Experimenting with market timing early on can be a good idea. It is challenging, as even veteran investors struggle with that strategy. But over time, you can learn to trade actively, be aggressive, and get ahead of trends.

Patience

Stock prices will not move immediately in your favor; in a lot of situations, they will even work against you. You have to be patient, stick to your decisions, and let your strategy time to pay off. There's a famous saying in the industry that goes „time in the market beats timing the market."

Choosing the right growth stock is difficult, you might lose money in the process, but finding that diamond in the rough company can make all the effort worth it.

You may take this example as inspiration: Jeff Bezos was one of Google's first investors. After Google's IPO, Bezos turned his $250,000 investment into 3.3 million shares of Google. He allegedly sold his position some time ago, but if he had held his stake to this date, his investment would be worth over $4.8 billion. Did Jeff sell to early? It just depends on what he moved his money in... Something tells me he did okay.

Dividend Stocks

Investing in stocks with the expectation that is going to appreciate is speculative. Even if the company is increasing its sales and improving its net asset value, that won't necessarily reflect in the value of the shares.

Companies that pay dividends are less speculative. It's a sign that the enterprise has been able to establish its business model in the market.

When a company obtains profits from its business activity, it can either reinvest the money or distribute the benefits between its shareholders. The dividend yield is the metric that is used to calculate the annual dividend that a company pays. For example, a company trading at $50 with a dividend yield of 3%, means that the company pays $1.5 in dividends per shear a year.

Dividend stocks are the safest alternative of stock types. A company that declares dividends is an organization that has reached maturity in its industry and has secured a fixed customer base. That's because only the companies that can afford to pay benefits are businesses that make enough money to save, reinvest, and share the extra rewards.

As dividend companies are already big and well-established, you can't assume they will grow rapidly and exponentially. What you can expect from them is steady and reliable expansion. Companies that pay dividends concentrate their efforts in incrementing profitability instead of augmenting their market cap. Thus, those types of companies attract long-term investors; therefore, they tend to appreciate slowly over time.

There's a common misconception regarding dividends and share prices. Non-financial people often believe that when a company declares a dividend, the stock prices stay the same. But in reality, their stock price drops in proportion to the gains distributed, as they cannot create money from nothing. But that's another topic, download our dividend book for more details on how dividends stocks work.

AT&T (T), Johnson & Johnson (JNJ), and ExxonMobil (XOM) are some examples of companies that pay dividends—having 6.26%, 2.75%, and 6.36% dividend yield respectively. As you can see, they are all stable businesses that have a loyal customer base and don't rely on economic performance to obtain profits.

When it comes to dividend stocks, there are two major strategies that you can follow. You can take the dividends and use the money for your expenses or other projects. Many people use the dividends of their stocks to live-off or use it as a retirement method. Of course, you'll need to invest a considerable amount to receive decent returns. But, with that approach, you won't be entitled to a fixed dividend, as the stock appreciates over time, the profits will increase accordingly.

You can also use the dividends to reinvest the money and get a more significant stake in the company. You can set most online brokers to collect the dividends and purchase more stocks when you have enough money. That strategy is potent for long-term investors as it can multiply their capital without having to spend much time keeping track of the positions.

Value Stocks

When a company goes through a public relations crisis, suffers from bad media, or launches a controversial product, people often overly-punishes that company's stock price. Buying when everyone is selling is counterintuitive and hard to do, but that is the basic principle behind these types of stocks.

If a stock undergoes a sharp decline in value despite its stable financial situation, it is being undervalued. It can be an excellent opportunity to purchase a stake in the company at a discount.

Here are some tips that will help you identify a value stock:

Solid Financial Situation:

A company that can stay profitable and expands its business despite taking a hit in stock's price performance is a clear indicator of a value stock. The market penalizes poor brand image management, but sooner than later, the people will forget what all the buzz was about. If the company can maintain or improve its finances, the share price will eventually go up.

Valuation Multiples:

Learning how to interpret and use valuation multiples is imperative to invest in value stocks successfully. Valuation multiples are simple ratios that can help you to evaluate stock price relative to the company's financials quickly. The most relevant multiples are:

- Price to Earnings: Share Price / Earnings Per Share
- Price to Book Value: Share Price / Book Value Per Share
- Price to Cash Flow: Share Price / Operating Cash Flow Per Share
- Price to Dividends: Dividend Per Share / Share Price = Dividend Yield
- Price to Sales: Share Price / Sales Per Share
- PEG: (P/E) Ratio / Earnings Growth Rate

Regardless of a company's promising financial indicators, value investing still equates to market timing and speculation. If you purchase a stock too soon or too late, your gains will be hindered, and predicting when the stock will hit its very bottom is nearly impossible.

Still, investing in stocks that are underpriced and paying attention to the multiples is a goods discipline to have whatever strategy you decide to follow. As Warren Buffet himself said: „It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."

Emerging Markets Stocks

The US is the financial epicenter of the world. NYSE and NASDAQ are the biggest stocks-exchanges both in volume and market capitalization. While its massive size brings security to investors, it cripples its growth (percentage-wise).

Developing countries' financial industries can offer faster growth than mature economies.
That is due to the essence of developing countries' economies. Developing nations' economies grow faster than developed countries; thus, they have the potential to reach a mature nation status. Analogously, stocks from those kinds of nations rise quicker and have the possibility of achieving a multinational level. But, similarly to growth stocks, higher appreciation chances, carries higher risks.

India and China are, by far, the most promising examples. China, while they are slowly reaching the GDP of the USA, they still have a long way to go, as they have over four times the population of the US. India took 271 million people out of poverty between 2006 and 2017; they already are the fifth economy in the world and have a population similar to China.

Countries like Brazil, Turkey, Mexico, South Africa, and Saudi Arabia are also good investing options; those markets are more speculative but have a reliable financial infrastructure. Opportunities are plentiful for investors who are willing to step outside their comfort zone.

In the way that developing countries stocks can offer up to double- or triple-digit growth, they also come with their fair share of risks. Developing nations often face corruption, currency instability, poor transparency, and significant government participation in the economy.

Those reasons are enough for some people to avoid investing in emerging economies. But for the investors who are willing to take the expose, returns can be gratifying.

Advice for a Successful Investing Career

Becoming a successful trader is more complicated than just saving some money and selecting a handful of stocks. There are no get rich quick tricks in this business, accomplishing stable returns takes patience and dedication. Perhaps, these tips can help you to prosper in the industry:

Realize that Ups and Downs are Part of the Industry

No one has a perfect investing career. Having losses from time to time is perfectly normal; the objective is the long-term. Learn from your mistakes, adapt your strategy, and stay patient.

Analyze the Value of the Stock

As we stated before, evaluating the price of a stock relative to its finances is an excellent habit. Undervalued stocks have a lot of room for growth. Overvalued stocks while they are hot and fancy, they are the first to fall when speculative bubbles pop.

For Growth Stocks

It is better to invest in growth stocks when the market is bullish. As companies are expanding, they rely on sales increases and reaching new customers. In a contracted economy, they struggle, and their stock suffers.

Don’t Listen to the News

Emotional investing is the doom of all traders. Ignoring the news, and being continually checking your stocks, will save you a lot of stress, and will give your investment time to grow.

Diversify your Portfolio with Options or Other Assets Classes

Regardless of your strategy, diversifying is crucial. Always invest in different industries and different types of stocks. As you mature as an investor, you can expand into commodities, fixed income, or options. Don't try to run before you walk, but once you feel comfortable enough, mixing options with stock gives traders a lot of advantages. Some of the main ones include:

1. The ability to diversify an already existing stock portfolio
2. Generate additional income off of stocks you already own without adding risk
3. Allow you to make more money using less capital
4. The ability to implement the right strategy for any given market condition, bull, bear, or neutral markets.

Sells your Stocks When:

1. When a bullish company starts to lose interest from investors
2. When the stock underperforms the market for three months straight
3. When a company radically reduces its profits
4. When you lose 20% of your investment.

Avoid Falling in Love with a Company

We all have invested in a company that we love and that we want to support. But we are not on the business for charity if the company underperforms avoid feeling attached to it.

Why You Should Make Your Own Investment Decisions

Now you know what you need to start making your investments in stocks. Maybe you find it overwhelming, and you're still wondering if you should hire a financial advisor or not. Let us convince you why you should make your own investment decisions.

Nobody Cares More About Your Money Than You.

This statement is self-explanatory; everybody is pursuing their interests, especially in this business. An advisor can choose to chase the route that is more profitable to go for the path that is more profitable to him.

You can Spend Your Money in Stocks Instead of Fees.

You don't need to waste money on advisory fees. Of course, your time is also valuable, but having more money to spend on stocks by making your own decisions is usually worth more than „professional advising."

Online Platforms Allow Anyone to Invest on Their Own.

Gone are the times when you needed to be very wealthy and sign a contract with a brokerage firm to invest in the stock market. Online brokers bring you all the tools necessary to evaluate stocks and manage your portfolio on your own.

All Financial Advisors are Different

Financial advisors are expensive, especially experienced ones. But no matter the credentials of the professional, they will still make mistakes. Most fund managers fail to beat the benchmark. You might as well make your own mistakes, get experience, and become an accomplished investor over time.

There are a lot of people in this industry who claim to know what they are doing, but trust me, they do not! I will tell you a little story. When I was a senior in college studying finance, I was interning at a small brokerage house, I would say about half the people who worked there knew what they were doing and the other half was just good at BS. One day when I showed up to work, one of the brokers asked me if I had any opinions on any stocks. I pitched him my idea, the guy then spent the rest of the day calling his clients pitching my idea to them… I do remember the stock turned out to be a winner, as he bought me lunch two weeks later. However, a professional investment advisor should've never been pitching an idea he heard from an intern.

Investing by Your Own is Fun

Investing in stocks, similarly to other challenging activities is though when you fail, but brings great satisfaction and a sense of self-worth when you succeed. Once you get confidence, you may want to try riskier strategies and different instruments. With time, you'll feel that even the losses help you to learn!

Learning how to Invest in Stocks will be Valuable for Your Entire Lifetime.

You don't need to quit your job to invest successfully; it's wiser to use investing as a secondary source of income when you start. If you ever lose your jobs or your business fail, you can rely back on your investments to help you bounce back. Unlike learning to play the guitar, investing will be appreciated and help you to support your family.

You can use Your Trading Skills as Credentials

People have respect for those who can manage money. Investing is a very desired skill; with practice, you can market your knowledge to other people, and leverage your experience for future jobs or businesses.

Conclusion

Selecting a broker, and going through the dozens of stocks available in the market is scary at first. But today, there are a lot of free, up-to-date information sources and educational tools that can help you with your task.

Solid research is the key to investing, there is no substitute. Do your homework, understand your numbers, have a balanced portfolio with diversified asset classes, and over time you will smash average market returns.

Like anything of value in life, it takes a lot of effort to get it going, but once you are on track, you'll be wondering why you haven't started earlier!

For those who want to fast-track their success, be sure to access our free training videos and our research center at https://OptionStrategiesInsider.com. Here we not only show users the proper way to invest but the investment strategies that make the most sense and how to get the most out of every investment dollar.

Letters and Testimonials

"I have been on a mission to learn options, it started a few years ago when I bought a book off Amazon, but soon found it to be too confusing to continue. Then about six months ago I watched one of your competitors' courses and it wasn't much better, it was just a lot of talk and words on the screen. I then somehow found Option Strategies Insider, and am I glad I did. You did an excellent job of taking a complicated topic and making it easy for anyone to understand. Amazing presentation, I am so glad I found your site."

— Harold B.

"You guys are doing a great job since I started following you. Before that I had been trying to trade options in a totally different way and in the process, only winning about half of my trades. Your membership has shown me how to attack the market in the most efficient way. Thank you guys!"

— Danny M.

"I used to trade stocks and options for a hobby when I was younger. However, with how heavy my workload is, along with making time for the family, I just don't have the time to do market research like I once did. Your ability to find trades that make a lot of sense and then laying it out in an easy to understand research report has immense value. I am up significantly since joining your Ultra membership. Without a doubt, I can confirm signing up with you guys is one of the best financial decisions I have made. I highly recommend your service!"

— Hazi G.

"I closed your recommendations of SPX yesterday and AZO today for nice profits and could not be happier with the research and the recommendations you guys have provided. Your option trading skills are second to none, having this site on my side make option trading a lot more fun."

— Jason M.

"Learning how to trade options property can lead to more wealth than any other form of investment. I am not going to tell you it's easy, because it's not. But once learned, you will have a viable skill that can lead to great wealth that no one can take away from you.

The best part about options is that it never changes, unlike other online businesses that get disrupted or cease to exist over time, options trading knowledge is a viable skill that can be applied forever. Once you have the skill it's yours to use for your entire life!

This is why I am such a proponent for learning how to trade options the right way from the start."

— Chris Douthit - OptionStrategiesInsider.com Founder

Chris Douthit

Chris has a long history with options and an extensive education in finance. Holding an MBA and multiple finance degrees, Chris has put in the time and effort to learning the market fundamentals. As a professional trader for TFM, Spear, Leads & Kellogg and Goldman Sachs, Chris was fortunate to be trained by the top companies in the world and to work alongside some of the best options traders in the business.

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