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INVESTMENT PARTNERS

Investor Basics

Overview of investing

NZX Firm

INTRODUCTORY GUIDE

Investor Basics

Overview of investing

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Topic 1: Introduction to investing

1.1 What is investing?

Investing is all about placing your money in assets that you anticipate will generate a profit, and therefore provide an income stream (from interest and dividends) and also possibly some capital growth (an improvement in the value of your original investment).

Investing vs saving

People who are accumulating money in the bank are 'savers' while those who are using their savings to buy investment assets like shares are 'investors'.

1.2 Why invest?

Investing means something different to everybody. The goal might be to maintain your standard of living in retirement or provide an ongoing income stream to be able to pay off your mortgage. Everyone has different objectives, and therefore needs to have a plan to achieve those goals.

There are two key elements to investing:

Income and capital growth

People invest to receive an income stream through dividends or interest and/or invest to achieve capital growth, which occurs when the value of your original investment increases.

In order to achieve your objectives, the value of your investments must rise at least in line with inflation, which is really just a measure of how much prices of goods and services are rising. Therefore, in order for you to retain the value of your investment it needs to at least deliver returns matching or ideally exceeding inflation. Topic 6 will cover inflation in more detail.

1.3 How to invest?

There are many opinions around this topic with four main investment options available, commonly known as asset classes.

1 Shares (equities/stocks)

2 Property

3 Cash

4 Fixed Income/Interest

1 Shares (equities/stocks)

Companies come in all shapes and sizes, from small 'one-person bands' like a lawn-mowing business, a shop or courier service through to large enterprises.

There are two types of companies; private (such as a family farm or family run business) or public. Public companies are businesses, which are owned by a number of investors such as Air New Zealand.

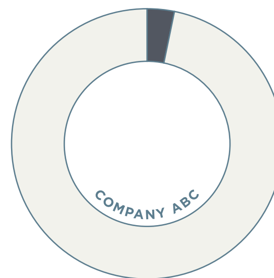
People who invest in these companies are called shareholders. In return for investing in the company, shareholders can receive dividends and other income from the profits that the company may generate each year. Investors also share in any increased value of a company the more successful it becomes (capital growth).

When you buy a share in a company you are effectively becoming a part owner and have a stake in that company. You will thereby have an interest in the company's assets (i.e. the land and buildings they own) and you will also be entitled to vote at company meetings and on the appointment of directors.

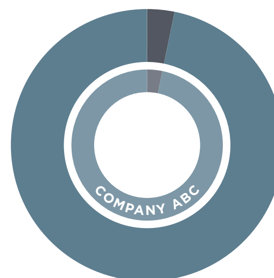
Share price examples

Investor owns

100,000 shares
$5.20 price per share
$520,000 total value



Investor owns **5%**



Public companies may be bought and sold through a stock market exchange and are in that case called listed companies. Investors can also invest in unlisted companies. These are usually smaller companies not listed on an exchange. They are therefore not regulated in the same way and are less liquid. Liquidity is a term which refers to how easily and quickly you can sell your investments.

2 Property

There are many different types of property you can invest in. You can buy a farm, a residential rental property, an industrial factory, a shop or an office. Your return will come from the rent paid by your tenants, along with any profit made if you sell the property for more than you paid for it.

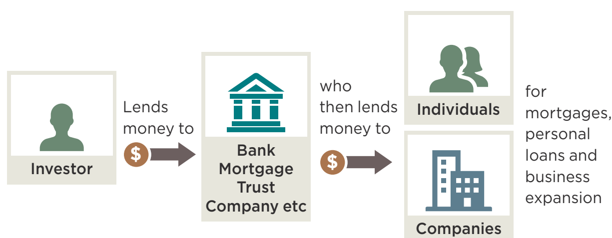
Another way of investing in property is to purchase a share in a property company. Property investments, which can be bought and sold via a stock market exchange, are known as listed property vehicles (LPV). A LPV pools the money of many investors so that they can purchase a range of property investments at a higher value which individual investors otherwise may not have access to. Since the listed property can be easily bought and sold through a stock market exchange, this makes this type of asset more liquid than other types of property, such as investments within the residential real estate market. Those that invest via LPV also don't have the difficulty of managing rates, insurances, maintenance and tenants etc.

3 Cash

Cash can be a physical holding of notes and coins although we also define on-call accounts and term deposits of less than 90 days as cash.

4 Fixed income/interest

If you don't own or part own companies or property, the alternative is to lend your money. When you put your money in a cash account or on term deposit with a bank you are effectively lending the bank money. In return they pay you interest, and then lend your money to someone who might need a mortgage, who they generally charge a higher interest rate.



Other examples of investments where you are lending directly to other entities include bonds issued by corporate issuers or the government. These types of 'lending' investments are commonly referred to as 'fixed income' or 'bonds' and the rate of interest, or income you receive is often at a fixed rate for a set period of time.

More information on fixed income investments is provided in Topic 3.

1.4 Asset allocation and diversification

A key consideration when building your investment portfolio is having the appropriate asset allocation and diversification.

Asset allocation describes how much money you have invested in each of the main investment asset classes: - those being; cash, property, fixed interest and shares (otherwise known as stocks or equities).

Diversification is all about reducing risk by investing in different areas and investments.

You will have heard the mantra 'don't have all your eggs in one basket'. There are many examples that illustrate this message, but one that comes to mind is the investor who had 2 rental properties, on the same street in the same city. With heavy rainfall, both houses slipped down a steep hill, and the investment went with it.

Diversification provides peace of mind that if one or two of your investments are performing poorly, you have others which may do better and provide a return. Essentially – it should smooth the returns you receive and spreads the risk.

More information on asset allocation and diversification is provided in Topic 7.