

THE **A** **B C** 'S OF

INVESTMENT

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The "ABC's" of Investment

According to the Cambridge dictionary definition¹, investment is “the act of putting money, effort, time, etc. into something to make a profit or get an advantage, or the money, effort, time”. It can be a daunting topic as there are some people who are fearful of investment because they associate investment to be being risky, difficult, confusing, time consuming and emotionally draining.

A recent Straits Times article² reported that “US stocks plunge into bear market as recession worries grow”. The recent volatile market and market selloff due to inflation news, rising interest rate, recession worries and global uncertain situation have caused some concerns for some investors as well. This article hopes to share the “ABC's” of investment framework for one can improve their financial literacy to overcome the fear investment, as well as for one to consider in their investing journey to help them make better investment decisions and planning.

A- Analysis of own situation and goals & objectives

Everyone is unique and each has different situation, concerns, goals, and objective when it comes to investment. The first step of this framework is to have an analysis of own situation (risk profile, time horizon, resources etc), as well as goals and objectives of our investment. It will be good to determine the objectives of investment: whether it is for wealth preservation to keep pace or beat inflation; tapping into power of compounding to accumulate more wealth and grow money faster; planning for a particular goal like retirement planning or children's education; or investing for capital gains or dividends. By understanding the objectives and goals of investment, it helps an individual to be more focused and less distracted by external factors.

After knowing the objectives and goals of investment, the next step will be understanding their risk appetite and time horizon. One needs to understand the risk appetite and the the risk return trade off (whereby a higher risk level of risk is associated with potentially higher return), before eventually investing into something that is in line with their risk profile and suitable to meet their goals and objectives. Different people have different interpretation of time horizon as well, and this will affect the strategy and investment that they choose.

Given a longer time horizon, one can tap into the power of compounding to compound their investment returns and achieve better outcome and results through their investment. It is important for one to know that investment is essentially different from trading or speculation too.

B- Budgeting

The next step in this framework would be budgeting. Budgeting is an important process in planning, and it helps people make better financial decisions; prepare for emergencies and stay focused on long-term financial goals. One should first look at their assets, liabilities, income, expenses, cashflow; and allocate budget for their investment. According to MoneySense³, one should ensure that they have “enough money for daily expenses and other expected expenditure”; “enough cash for emergencies” and “basic health and life insurance policies in place” before doing their investment. This is to ensure that one is ready for investment. In Singapore, there are a few sources of funds for investment. These include cash, the Central Provident Fund (CPF) and Supplementary Retirement Scheme (SRS) funds.

C- Construction of portfolio with the buying of assets **(asset allocation)**

With the allocation of budget, the next step in this framework would be the construction of portfolio with the buying of assets. According to Investopedia⁴, “asset allocation is an investment strategy that aims to balance risk and reward by apportioning a portfolio's assets according to an individual's goals, risk tolerance, and investment horizon”. Depending on one's risk profile, one can buy assets that are in line with their risk profile to meet their investment goals.

These assets can be equities, bonds, properties, cash, unit trust and etc. For the accredited investors⁵, they may be looking at alternative assets classes like private equity, hedge funds or private debt etc. As the popular idioms put it: “do not put your eggs in one basket”. The same applies for investment as well, and it is good for one to have a diversified portfolio. Different assets classes/instruments perform differently at different time.

With a well-diversified portfolio, it helps investors to reduce overall risk and volatility in their investment; as well as to smoothen out the returns in the long run.

There are also many different investment strategies and approaches that one can use for their investment when it comes to portfolio construction and asset allocation, depending on each individual profile and risk appetite.

Some of these strategies and approaches includes value investing, growth investing, contrarian investing, momentum investing, dollar cost averaging, arbitrage and etc.

Regardless of what asset allocation or which investment strategies and approaches that one chooses, the most important thing is for one to understand how these asset allocation, investment strategies and approaches works for them; and being comfortable with these decisions.

D- Do due diligence & have regular reviews

During the portfolio construction process, one should do their due diligence before buying that particular asset/product for investment. Due diligence is “defined as an investigation of a potential investment (such as a stock) or product to confirm all facts” ⁶. By doing due diligence, one should be able to make an informed decision whether to buy or avoid that particular asset or product for their investment. With the rise of scams, it will be also good for investor to be wary and careful about investment scams. The “too good to be true” litmus test and checking out if the service provider or companies being listed on the MAS investor alert list will be helpful for one to avoid potential scams.

After the portfolio has been constructed, it is important for one to do regular reviews.

With regular review, it allows one to track and measure the performance of their investment; to decide on whether there is a need to do rebalancing in their portfolio; cashing out and exiting on certain investments if they are overpriced; starting new investment into new areas that they want, so as to ensure that their investments are still in line with their financial goals and objectives.

CONCLUSION

I hope the “ABC's” points above provide a useful framework for you to understand about investment and are helpful in your investment journey. However, this article should only serve as a guide, and should not be taken as investment advice. Investment is an extensive and broad topic which entails more details that are beyond the scope of this article. It will be good for individual to take ownership by getting educated to learn more about investment through lessons or information and materials from trusted websites like MoneySense and those others by financial institution. It will also be good that one can look for and work with a trusted and competent practitioner for this investment planning and discussion; so as to help them make better investment decision each time. With this, I wish you every success in your investment and HUAT ar!



ABOUT THE AUTHOR

Tan Seng Chuan is a licensed financial practitioner and an active member of IFPAS. He holds the ChFC®/S, CLU®/S, IBFA, AEPP® designations, and the HNW certification.

NOTES:

- 1- [HTTPS://DICTIONARY.CAMBRIDGE.ORG/Dictionary/ENGLISH/INVESTMENT](https://dictionary.cambridge.org/dictionary/english/investment)
- 2- [HTTPS://WWW.STRAITSTIMES.COM/BUSINESS/COMPANIES-MARKETS/SP-500-SINKS-39-ENDING-IN-BEAR-MARKET-AMID-INFLATION-WORRIES](https://www.straitstimes.com/business/companies-markets/sp-500-sinks-39-ending-in-bear-market-amid-inflation-worries)
- 3- [HTTPS://WWW.MONEYSENSE.GOV.SG/ARTICLES/2018/10/WHAT-IS-INVESTING](https://www.moneysense.gov.sg/articles/2018/10/what-is-investing)
- 4- [HTTPS://WWW.INVESTOPEDIA.COM/TERMS/A/ASSETALLOCATION.ASP](https://www.investopedia.com/terms/a/assetallocation.asp)
- 5- [HTTPS://WWW.MAS.GOV.SG/-/MEDIA/MAS/News-AND-PUBLICATIONS/CONSULTATION-PAPERS/ANNEX-4--PART-III--NONRETAIL-INVESTOR-LEGIS-AMDmts.PDF](https://www.mas.gov.sg/-/media/MAS/News-and-Publications/Consultation-Papers/Annex-4--Part-III--Nonretail-Investor-Legis-AMDmts.pdf)

ACCREDITED INVESTOR MEANS AN INDIVIDUAL —

(A) WHOSE NET PERSONAL ASSETS EXCEED IN VALUE THE MINIMUM AMOUNT OF \$2 MILLION (OR ITS EQUIVALENT IN A FOREIGN CURRENCY) OR SUCH OTHER AMOUNT AS THE AUTHORITY MAY PRESCRIBE IN PLACE OF THE FIRST AMOUNT, AND IN DETERMINING WHETHER AN INDIVIDUAL'S NET PERSONAL ASSETS EXCEEDS THE MINIMUM AMOUNT, THE ESTIMATED FAIR MARKET VALUE OF AN INDIVIDUAL'S PRIMARY RESIDENCE LESS ANY OUTSTANDING AMOUNTS IN RESPECT OF ANY CREDIT FACILITY GRANTED TO THE INDIVIDUAL OR ANY OTHER PERSON THAT IS SECURED BY THAT RESIDENCE, SHALL NOT ACCOUNT FOR MORE THAN \$1 MILLION (OR ITS EQUIVALENT IN A FOREIGN CURRENCY) OF THE MINIMUM AMOUNT; OR

(B) WHOSE INCOME IN THE PRECEDING 12 MONTHS IS NOT LESS THAN \$300,000 (OR ITS EQUIVALENT IN A FOREIGN CURRENCY) OR SUCH OTHER AMOUNT AS THE AUTHORITY MAY PRESCRIBE IN PLACE OF THE FIRST AMOUNT

- 6- [HTTPS://WWW.INVESTOPEDIA.COM/ARTICLES/STOCKS/08/DUE-DILIGENCE.ASP](https://www.investopedia.com/articles/stocks/08/due-diligence.asp)