10 Questions to Ask Yourself Before Investing

Description

To some people, the thought of investing can be a scary one, whereas to others, it could be a rewarding journey and a way to get rich.

Whatever your thoughts, the fact is that investing is not an easy journey, and definitely not one for the faint-hearted. You need to be intelligent, well-informed, and rational enough when it comes to investing. Be prepared to spend a significant amount of time researching and analyzingâ?¦and yet you might not end up buying it.

On top of all these, you also need to be prepared to take a certain amount of risk. Investing is not simply a matter of buying low and selling high, although those are fundamentals all investors try to bear in mind. But the truth is, how do you know when it is â??low enoughâ?• to buy, and â??high enoughâ?• to sell?

Unless you have insider information, your guess is pretty much the same as mine. There is a certain element of guesswork, luck and timing involved. And thatâ??s the risk that you have to undertake.

Before you get started, here are some questions to ask yourself:

1. How much can I afford to invest?

After deducting your monthly expenses, loan repayments and emergency savings, how much do you have left to invest?

One of my readers previously emailed saying he had saved $5,000 and was looking for advice on what he could invest in. My advice to him was simple â?? donâ??t invest just yet. Save more money before you go in.

You see, with just a few thousand, your investment options are limited.

Example:
Letâ??s presume John is a low-risk taker who cannot afford to lose his $5,000. He prefers to buy an established, blue-chip company that is unlikely to collapse, so he picks DBS.

At DBSâ?? current trading price of $22 today, he would only be able to buy slightly over 200 shares. Even if the price rose to $22.50 by the end of the year, he would only earn $63 in profits (after deducting a conservative $25 brokerage fee for each transaction).

Compare this to if John had $20,000 to invest instead, which would have given him slightly over 900 lots, and thus $400+ in net profits.

The age-old adage of money grows money is indeed true.

2. Do I need the money anytime soon?

Investing generally rewards those who are able to wait out the cyclical swing of the stock market. If youâ??re using almost all of your emergency funds to feed your investments, then when you need money urgently one day, you may find yourself with no choice other than to sell your stocks even if the price is low.

All investors know the best way to make money is to buy low, sell high. But if youâ??re playing with money that you need, youâ??re less likely to be able to wait for such opportune moments.

3. How much time do I have to spend on research?

If you donâ??t have the luxury of time, then you might want to choose passive investment tools such as ETFs or mutual funds which require less active management or monitoring on your part. The stock market might not be the best option for you if youâ??re too busy to really do the groundwork before committing your money.

My broker recently tried to convince me to buy Keppel DC Reit, and when I looked at its prospectus, it did indeed sound extremely appealing. This was from their media statement:

> *â??Keppel DC Reit offers investors a **distribution yield of 6.8%** in Forecast Year 2015 and **7.1% in Projection Year 2016** with a distribution **growth of 4.5%**, driven by built-in rental escalations as well as the renewal or commencement of leases and co-location arrangementsâ?•*


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Hot Stock: Keppel DC Reit most active Singapore Reit, gets outperform call from Credit Suisse

By Angela Tan angelat@sph.com.sg


Keppel DC REIT: First Ever Data Centre REIT To Offer 6.8% Yield

ASPIRE | 08 DECEMBER 2014

By: Mr.IPO

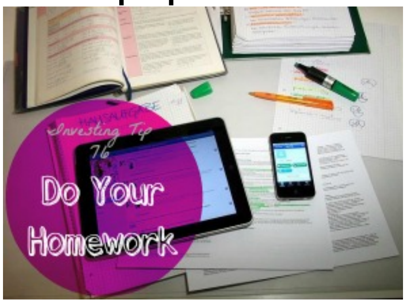
ARTICLES (26)

PROFILE

After spending 2 days of research on this stock, I decided not to buy. Why?
(If youâ??re interested, you may read more about my analysis here.)

So I ended up spending all that time on extensive researchâ?¦only not to buy. And this was only for one stock! Imagine the time you need to spend on the rest.

4. Am I prepared to do the homework necessary before investing?



Jim Rogers estimates that only 2% of investors even read their annual reports. Where do you stand? Are you willing to spend hours and hours learning how to conduct a fundamental analysis or a technical analysis before you purchase any company stock? Do you even know what they mean?

As a short introduction, fundamental analysis involves looking at the characteristics and operating model of the company itself in order to estimate its value, whereas technical analysis looks more at price movements in the market, to understand demand and supply patterns together with market sentiment as they try to predict trends of whether the stock price will go up or down in the future.

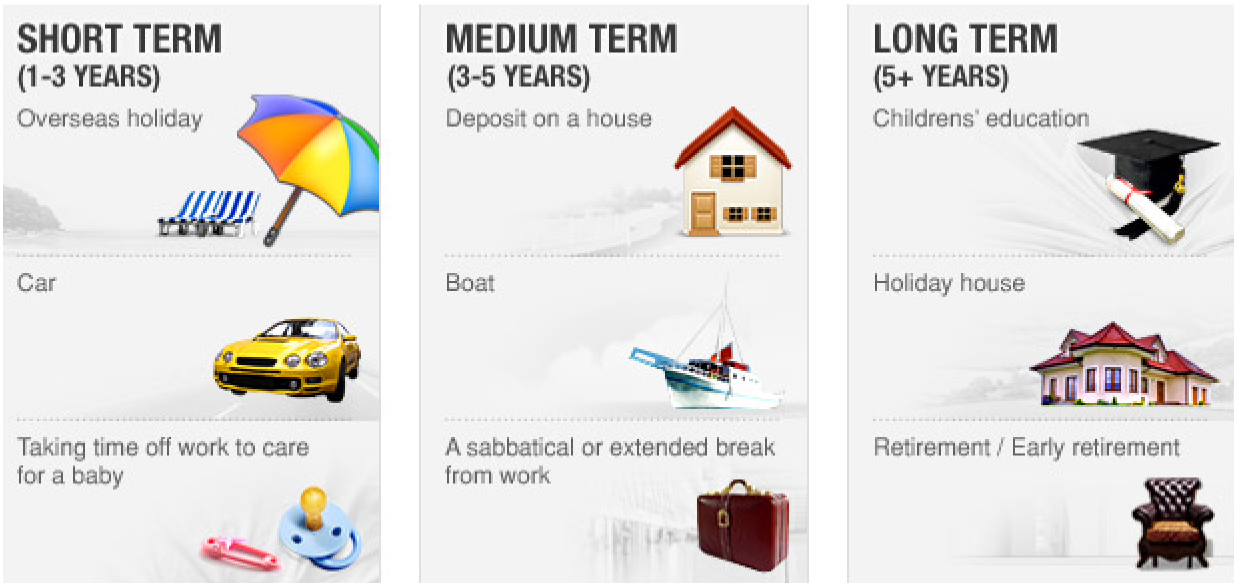
For instance, ask anyone and theyâ??ll tell you the growth of e-commerce is indisputable. But which company will benefit? Will it be Amazon, eBay, Alibaba or JD.com (rising competitor giving Alibaba a run for its money)? Given that JD.com only recently went public and was pretty quiet about it, technical analysts may favour this stock as prices may go up once the public starts noticing them more. On the *other hand, fundamental analysts may prefer to wait longer to see if the company truly is able to manage its competitors and own earnings well.*

5. Do I understand how the investment works?

If youâ??re buying into REITs, do you know how they work, and what are the factors influencing their prices? What about for stocks, ETFs and mutual funds? Do you really know what youâ??re buying into?

If you donâ??t, then either take the time to understand it, or perhaps you might want to consider putting your money with a trusted financial advisor to do the legwork for you instead.

6. What do I hope to achieve through my investments?



Some examples of investment goals. Credits: CIMB Principal.

7. How long do I plan to invest?

The turnaround time for your investments is important, as it will influence the types of tools you choose and the stocks you buy. Many investments require time to grow, and if locking up your money for 10 â?? 20 years sound uncomfortable to you, then you might want to consider something that can generate returns in a shorter time frame.

Value investing, which Warren Buffet predominantly practices, is one such tool that requires patience and time. It operates on the principle that there are under-valued companies out there, and thus patience is a key attribute for value investors to wait for the market to recognize the companyâ??s value which theyâ??ve been ignoring. Even if you spot a great value stock today, you typically need to hold on to it for at least a few years before the price goes up significantly for you to make a profit.

8. How much do I expect to earn on my investments?

Is this figure realistic? How much time would you need to reach this level of earnings?

If you go in with $5,000 and expect to have $10,000 by the end of the year (a 100% return), I would say youâ??re either crazy, blessed with tons of luck, or have some valuable insider information.

Most investors are happy enough if they can generate a 5% to 7% returns on their investments yearly. My goal is to get above that. What about you?

9. What are the costs to buy, hold and sell the investment?

Trading	Investing
Short-term	Long-term
Price	Value
Technicals	Fundamentals
Volatility	Risk
P/L	Goals
Borrow	Save
Want	Need
Noise	Signal

Useful comparison table I took off Google. Credits do not belong to me.
If youâ??re frequently buying and selling, donâ??t forget to factor in your brokerage fees when you calculate your costs. Many people forget about this when they calculate their nett profit / losses. Will you also be paying taxes on the money you earn? All these are â??invisible costsâ?• that some of us miss out on.

Do also note the differences between trading and investing. Investors tend to buy/sell less frequently than traders, and would therefore incur less transaction costs as well. The downside is, itâ??ll take longer to see returns as well.

10. Am I prepared to lose my money if Iâ??m wrong?

At the end of the day, investing carries a certain amount of risk. Even if you do your homework thoroughly, thereâ??s no guarantee that youâ??ll make a profit on your investment, because in a way, youâ??re betting on the future.

The most any of us can really hope for is to make an educated guess on future price and earnings based on current track records and solid fundamentals. Even good businesses can fail, whereas what seemed like a risky business can rise to fame quickly. Take a look at these 2 case studies.

Case Study 1: The decline of Laura Ashley

Most females are familiar with Laura Ashley, the much-loved English fashion brand. Its romantic, sweetheart clothing appealed to many women in the 1970s, and the business grew quickly to a major retailer with over 500 shops worldwide.

But in the 1980s, fashion changed. As more women entered the workforce, practical and professional attire became the preferred choice over Laura Ashleyâ??s sweet pieces. At the same time, fashion houses started moving production offshore and some even outsourced it entirely to cheaper countries like China and Thailand. Laura Ashley, however, continued to pursue its sweetheart designs which were now outdated, and the expensive manufacturing processes that served them well since they started. Today, while the brand is still around, they are no longer as popular as before.

Case Study 2: Las Vegas Sands

Las Vegas Sands (which owns casinos) stock price declined drastically from 2008 to mid-2009 when the company was facing a liquidity crisis and various lawsuits. It fell to a historical $1.77 in 2009 where the crisis was so severe that the company was in danger of going bankrupt, because they lacked funds to continue its multibillion-dollar ongoing and planned construction projects in Macau, Singapore and the U.S.

Would you have dared to invest in the company at that time? Many thought the company would go bust on its own or driven bankrupt by the lawsuits they faced.

But if you had taken a gamble on them then, you would have made almost **fifty times return** by now! Your 10k could be half a million today (in just 6 years)!

As you can see, there really is no guarantee when it comes to investing.

So the question is, are you willing to take the risk? Are you prepared to lose your money if youâ??re wrong on your judgment?
(If your answer is no, you might want to consider other alternatives. Keep a look out for my upcoming post on â??types of investment products for different personalitiesâ?• soon!)

With love,
Budget Babe
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1. Investing
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3. Stocks