INVESTING FROM A TO Z

by Mike Frazier

This book is *dedicated to*

Samantha, Nikki and Brooke

Investing for the future has always been important, but is especially important today. Pensions and other company supplied retirement plans are a thing of the past. The responsibility of saving for retirement falls directly on the individual. The sooner one begins saving and investing, the better chance of success through the power of compounded growth.

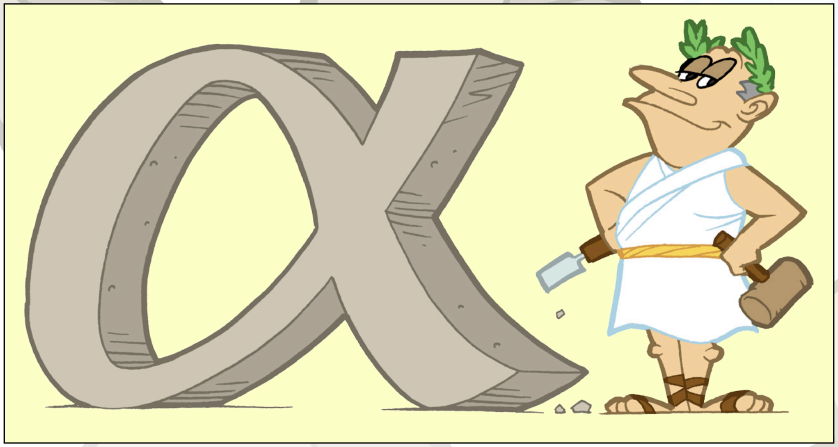
INVESTING FROM A to Z

The advancement of the Internet has made investing easier in some respects, but much more difficult in others. Markets move faster than ever today. In this age of globalization, global markets are intertwined. Commodities, currencies and global trade bind economies from the United States to Asia, Europe and Latin America, and everywhere in between.

There is so much information at our disposal, but it can be quite overwhelming. Not all of it is credible or responsible either. Information travels at the speed of light, but knowledge doesn't. I decided to write this book as a basic primer to make sense of terminology that is spoken in the investment industry, but might not always be understood beyond it. The goal is an inviting educational piece to help build the necessary tools and knowledge to be a successful and responsible investor.

-Mike Frazier

A is for Alpha



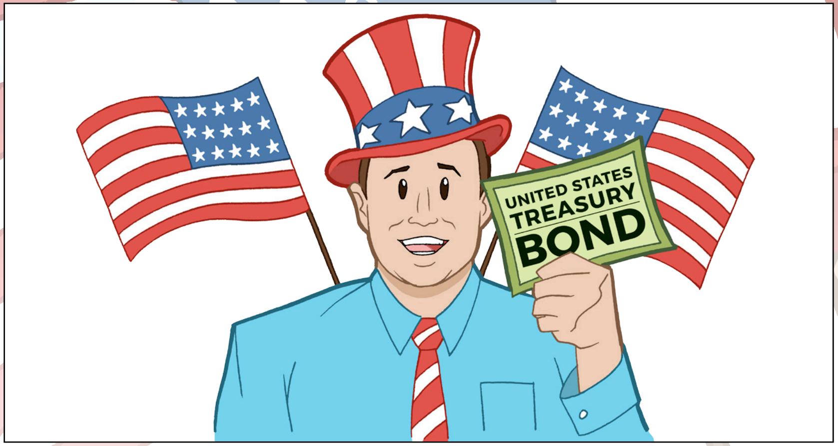
In the investment world, the Greek letter "A" measures the reward potential of a particular investment relative to the risk taken.

The Alpha of an investment is compared to a specific benchmark, like the S&P 500. A positive Alpha of 2.0 would mean the investment is outperforming its benchmark by 2%. A -5.0 alpha means the portfolio is underperforming by 5% quantifiable.

The Alpha can also be viewed as a value that a portfolio manager provides. Logically, you're looking for positive alpha.

Alpha is commonly used with Beta, which measures the volatility in a portfolio and overall risk.

B is for Bonds



While a stock is an equity security, a bond is a debt security. When you buy a bond, the issuer is actually borrowing money from you, and pays you interest until they pay you back in full.

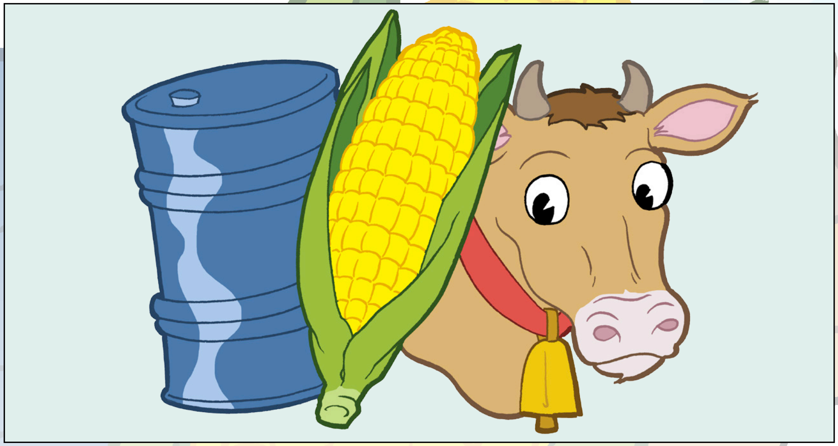
Bonds are referred to as fixed income, because the interest payments are a contractual obligation. The payment is fixed, and generally paid out twice a year until the bond matures.

The beauty of bonds is the predictability. You know how much income you'll receive, and you know when you get your money back.

The U.S. Federal Government is a large issuer of bonds, referred to as Treasury Securities. Corporations and Municipalities also frequently issue bonds.

Bonds are generally issued at par value, which is 100. They also mature at par value, but trade actively, and can be priced at a premium and/or discount to par value, depending on interest rates and the issuer's credit quality.

C *is for* Commodities



A commodity is a basic good that can be purchased interchangeably in the open market for consumption and/or investment. Commodities are generally natural resources such as metals, agriculture, and oil.

Commodity trading has been around for centuries, well before currencies were widespread. People would barter with commodities. Due to the seasonality of agricultural commodities, futures contracts helped hedge risks from “Mother Nature”, such as excess freeze or drought. The Chicago Board of Trade is the oldest futures and options exchange, and was established in 1848 to ensure fair market prices existed year-round.

Commodities trade on global exchanges, mostly in the form of futures contracts to buy or sell at a specific price within a specific time-frame. Commodity prices can be quite volatile, and can be driven by economic activity, geo-political events as well as weather. Because of this, trading commodities is speculative in nature. Billions of Dollars are traded in commodities daily.

D *is for* Dividend

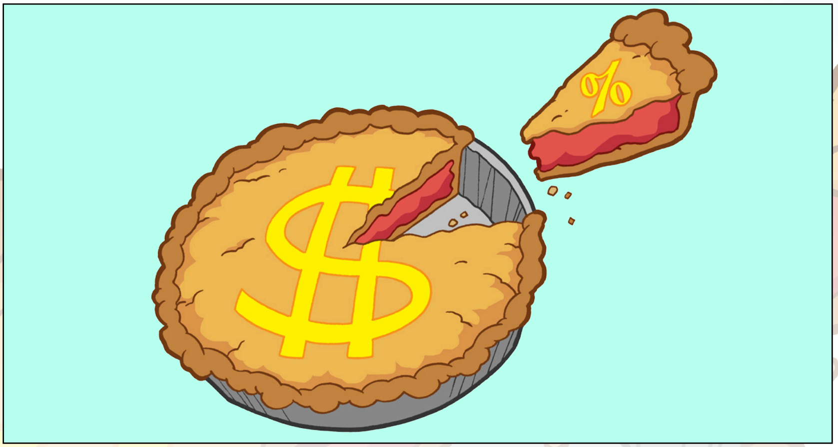
Many investors seek income as well as price appreciation. Income distributions received from stock investments are called dividends. Established and mature companies often pay a portion of their profits back to their shareholders to incentivize them to own the stock. Dividends are usually paid out four times per year and require approval from the company's Board of Directors.

Historically, dividend payments have provided nearly 50% of total stock market returns. Growth stocks generally do not pay dividends.

Importantly, dividends are not fixed. During hard times, stock dividends can get cut. It's important to do your homework on the dividend to make sure it's safe. It's critical that a company earns more than they pay out in dividends.

There are select companies that Wall Street refers to as "Dividend Aristocrats." These firms not only pay dividends, but have also increased the dividend payment every year for a minimum of 25 years.

E *is for* Earnings Per Share *EPS*



The EPS is the key indicator for a company's profitability. It's the portion of company profit allocated to each outstanding share of its common stock.

The EPS is largely considered the most important factor in valuing stock prices. Profits drive stocks.

Growth stocks are expected to see profits increase at a faster rate than more mature value stocks. Because of the faster growth, investors are generally willing to pay more for growth stocks. This can be measured with the Price/Earnings (P/E) ratio.

F *is for* Federal Reserve

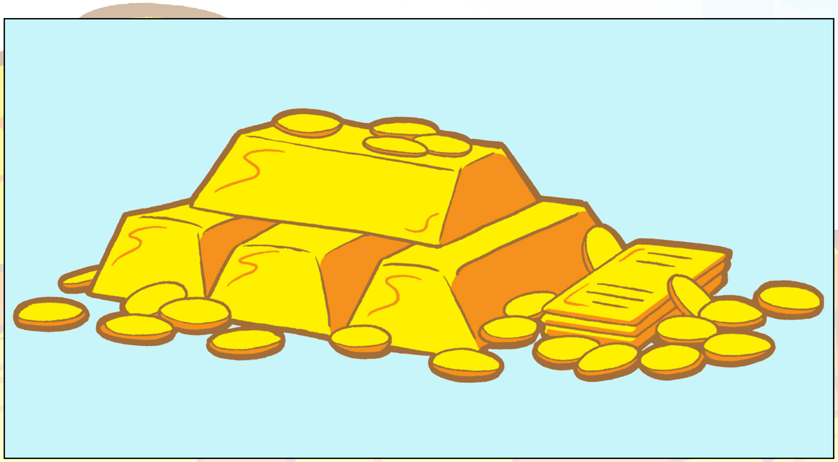
The Federal Reserve, typically referred to as "the Fed," is the gatekeeper of the U.S. economy. It is the bank of the U.S. government and it regulates the nation's financial institutions. It establishes U.S. monetary policy and determines short-term interest rates.

Established in 1913, the Fed is an independent government institution, although Congress does maintain oversight authority.

The Fed is run by a Board of Governors which consists of seven Presidential appointees. The Fed watches over the world's largest economy and is, therefore, one of the world's most powerful organizations.

The Fed Chair is considered one of the most powerful individuals in global finance. Paul Volcker, Alan Greenspan and Ben Bernanke became household names during their tenure. In 2014, Janet Yellen was confirmed to lead the Federal Reserve, making her the first female Fed Chair.

G *is for* Gold

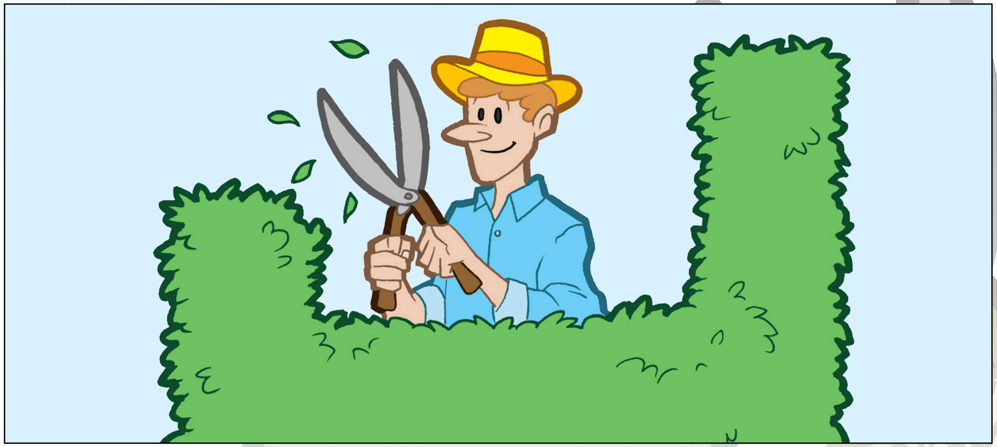


Gold is one of the oldest investment assets in the world. It has been a valuable and highly sought after precious metal for centuries, used for jewelry as well as currency. Gold was first used as money in Asia Minor.

Because Gold was widely accepted as a form of currency, it became a monetary system known as the Gold Standard. Foreign currencies were priced against units of Gold and were exchanged. The Spanish Gold Doubloon was widely used in trade in the 18th century.

In recent years, Gold has been viewed as an investment that will do well with inflation. It's also coveted because of its universal value and mistrust of government currency manipulation. Most countries maintain a vast supply of Gold reserves. The U.S. maintains the majority of its Gold reserves at Fort Knox.

H *is for* Hedge



A hedge is an investment made to protect assets or help offset losses in a primary investment. It's often viewed in the investment community like an insurance policy.

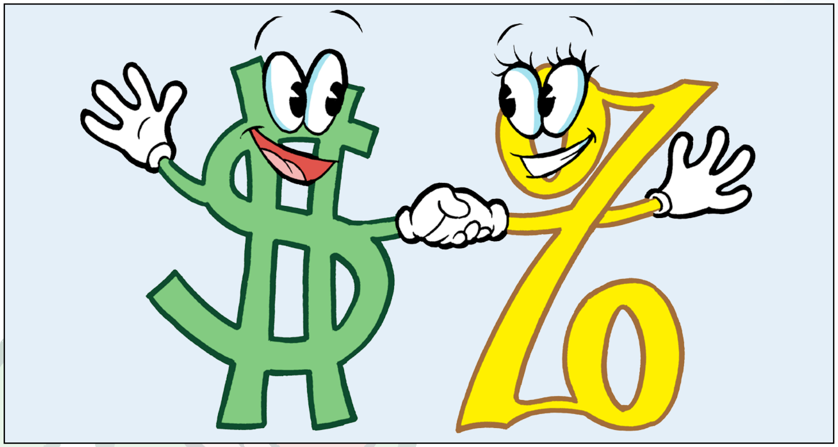
Investors usually hedge a position or portfolio when they have large gains or a substantial position and they're not sure about the near-term price direction and seek downside protection.

Shorting is a type of hedge, which can be done with stocks, commodities and other securities. Shorting a stock consists of borrowing shares of stock and simultaneously selling the shares with the plan to buy them back at a lower price and keep the spread. Short-sellers make money when Markets decline.

Farmers have hedged crops for centuries to help protect them from a drought or other supply issues. The Chinese were believed to create Rice Futures over 6,000 years ago.

Hedges are a valuable tool in managing risk. A hedge provides protection but also limits maximum returns.

I *is for* Interest Rates



Interest is a cost paid by a borrower of assets to the owner as a form of compensation for the use of the assets. It is most commonly the price paid for the use of borrowed money.

Interest rates are a part of our daily lives. We see them with mortgages, car payments and credit cards. Paying attention to interest rates is critical to personal finance.

The rates of interest fluctuate with economic conditions and inflation. Interest rates have significant influence on investments, particularly in stocks, bonds and housing. Interest rates are effectively the price of money.

J *is for* Junk Bond

A bond that is below investment grade is commonly referred to as a Junk Bond. It's also known as High Yield. Junk Bonds are rated BB or lower.

Junk Bonds pay higher interest than safer, investment grade bonds, because they come with additional risk. Investors purchase the bonds seeking higher returns. Junk Bonds act more like growth stocks than investment grade bonds. Individuals need to be very careful when considering Junk Bonds. Yield seeking can be a dangerous proposition.

K *is for* Knowledge

Investing can be very challenging. Success requires a great deal of homework and experience. Investors learn something new every day. The stock market is a discounting mechanism, which anticipates events and prices them in advance. The phrase, “buy the rumor, sell the news” is often accurate.

Investing can be quite humbling. Information has become so abundant today and travels at the speed of light on the web. The problem is, knowledge doesn’t.

Markets move very quickly, and economic globalization has tethered the U.S. stock and bond markets to markets overseas. It’s a global world. Knowledge comes with experience.

One of the greatest challenges for long-term investors is to deal with shorter-term issues. Understanding the various issues that move markets is critical to long-term success. It requires hard work and discipline. Knowledge is king.

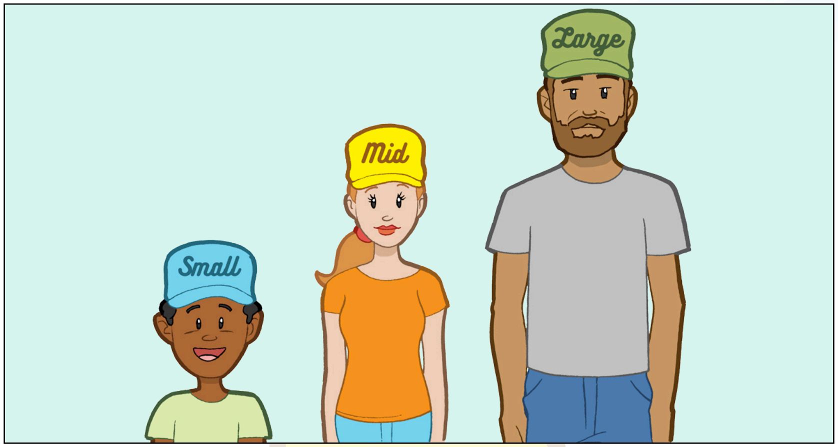
L *is for* Liquidity

Liquidity is the degree in which an investment can easily be bought or sold and converted to cash quickly, without having a significant influence on the asset price.

A liquid investment, like a stock, can generally be transacted efficiently on an exchange. Large cap stocks are considered very liquid as they trade in heavy volume, well over 1 million shares per day.

An illiquid investment generally does not transact quickly or easily and doesn't have a large market of buyers and sellers. Many smaller company stocks are less liquid. Real Estate is considered illiquid because it generally takes weeks to complete a transaction.

M *is for* Market Capitalization



The Market Capitalization or "Market Cap" is the true and total market value of a company or institution. Market Capitalization is calculated by multiplying the stock price by the total shares outstanding.

Large Cap stocks refer to companies that are valued at $10 Billion and over. Mid Cap stocks are generally $2 Billion - $10 Billion. Small Cap stocks are under $2 Billion in value.

The S&P 500 index is a composite of the 500 largest U.S. companies by market cap. The majority of the S&P 500 companies are Large Cap stocks, but the index does have some Mid Caps and Small Caps. All 30 stocks in the Dow Jones Industrial Average are Large Caps.

N *is for* New York Stock Exchange

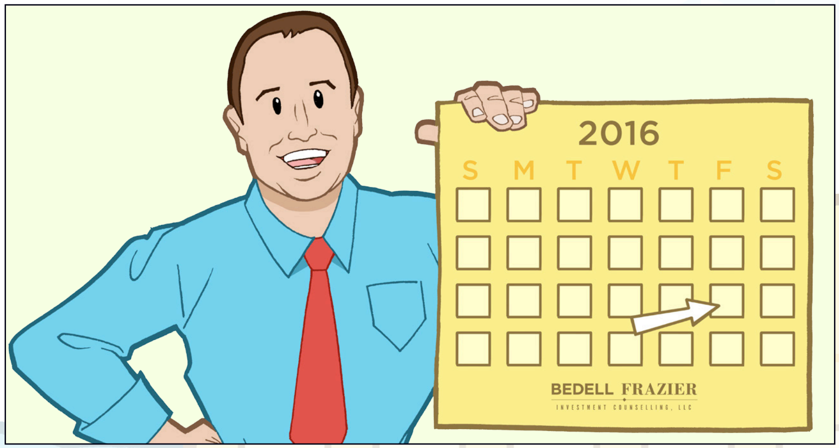
The New York Stock Exchange (NYSE) is the largest stock exchange in the world. It resides at 11 Wall Street in New York City, at the corner of Wall and Broad.

The origin of the NYSE is traced to the "Buttonwood Agreement" between 24 stockbrokers in 1792. The agreement was signed on Wall Street under a Buttonwood tree.

The NYSE is nicknamed the "Big Board".

All stock transactions used to be made on the exchange floor with market makers. Today, the vast majority of trading volume is conducted electronically. Approximately 10% of daily stock trades take place on the exchange floor today.

O *is for* Option



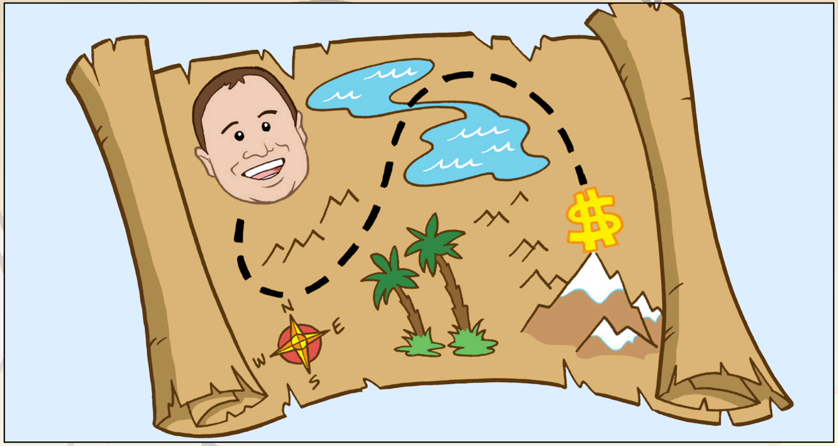
An Option is a derivative security whose value is derived from an underlying security, commonly a stock.

Options are contracts between a buyer and a seller, which give the buyer the right to either buy or sell a particular security at a specified price on or before a specified date.

Puts and Calls are the most common forms of options. A call option allows the buyer to purchase a security. A put option allows the buyer to sell a security. Some option strategies can be very risky while others are very defensive.

Options are traded regularly on various exchanges and expire on the 3rd Friday of every month.

P *is for* Plan



A wise man once said, "if you don't know where you're going, any road will take you there."

Responsible investing requires a well thought out plan. The first step is to identify goals. Are you investing for income or growth? Is this money for retirement or maybe college for your kids or grandkids? You cannot invest money intelligently until you establish the plan. The plan will then drive the investment philosophy and strategies. The plan will determine what type of investments are appropriate and how much risk can be taken.

Time is a significant component of the investment plan and strategy. Investors with a longer time horizon can generally afford to take more risk than those with short-term needs.

Q is for Quantitative Easing

Quantitative easing is a monetary policy tool in which a central bank purchases securities from the Market with the intention to lower interest rates and increase the money supply. Quantitative easing increases the supply of money by injecting capital into the financial system. The goal is to promote lending and growth investments. Quantitative easing is often considered when short-term interest rates are at or near zero, and does not involve the printing of new notes.

Quantitative easing was a popular strategy by central banks around the globe to help fight the Great Recession, which was created by the Financial Crisis in 2008.

R *is for* Real Estate Investment Trust

A Real Estate Investment Trust, commonly referred to as a "REIT," is a security that sells like a stock on the major exchanges and invests in real estate directly, either through properties or mortgages. A REIT is required to distribute at least 90% of its income to investors.

REITs were created in the United States when President Eisenhower signed into law the REIT Act that was contained in the Cigar Excise Tax Extension of 1960.

S is for Stock

A common stock is a security that represents ownership in a company. Stock owners are shareholders, and have voting rights. Companies issue stock to raise money. Common stock holders are at the bottom of the ownership hierarchy of a company.

Historically, stock owners received paper stock certificates as proof of ownership. Today, stock owner information is kept electronically and stocks are held in “Street name” at brokerage houses in place of a hard copy of the stock certificate. Most U.S. common stocks trade on exchanges, like the NYSE and NASDAQ.

Preferred stock has senior rights to common stock. Preferred stock dividends are paid out before common stock dividends. A Preferred stock is generally viewed as an income security.

The Dutch East India Company is believed to be the first company to issue stock to the public in 1602.

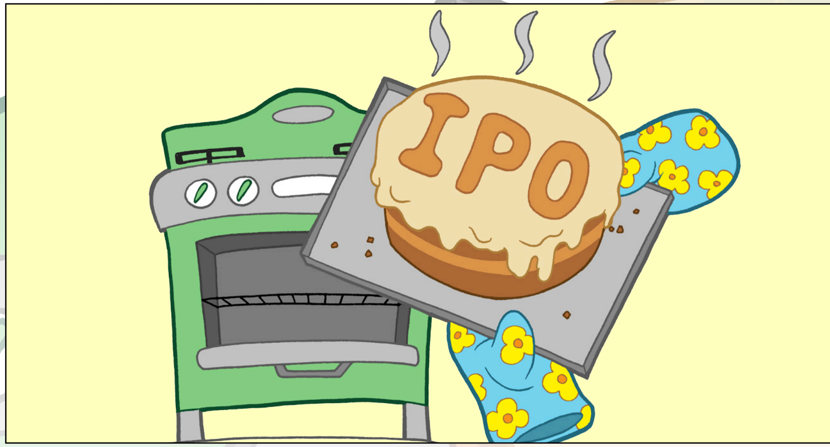
T *is for* Trade

A trade is a financial transaction. Trading is the purest form of capitalism. Buyers and sellers are matched to negotiate a fair and acceptable market value for a particular security.

A standard stock transaction settles three days after the trade, otherwise known as T+3.

The U.S. Stock Market is open for trade weekdays from 9:30am to 4pm, Eastern Time. Trading does exist pre-market open and post-market close, but they are not nearly as active so securities aren't as liquid.

U is for Underwriter



An underwriter is a company, usually an investment bank, which guarantees the purchase of an issuing company's stock. The underwriter administers the process of a company doing an Initial Public Offering or "IPO."

The underwriter performs valuation measures and due diligence in order to help determine a fair market value for the stock. The underwriters are the ones that bring an IPO to life.

There are generally a number of underwriters that participate in IPO's; in this case they are called a Syndicate. The Syndicate are like the cooks in the kitchen that collaborate to bring a company public.

The Syndicate actually purchases the stock at the determined IPO price and then sells it to the public. In essence, they're the middlemen.

When investors buy an IPO, they're actually buying the shares directly from the underwriters.

V *is for* Valuation

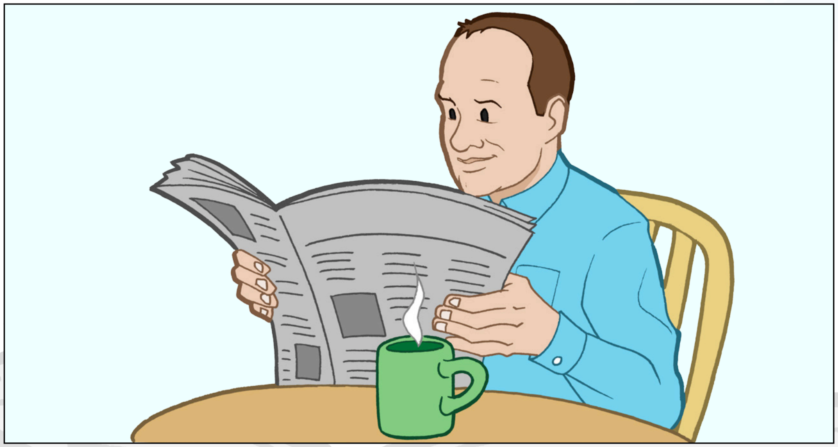
Valuation is the process in determining a fair market price for an asset. There are many valuation metrics used to value a security. One of the most common is the Price/Earnings (P/E) Ratio.

Other measurements to value stocks are Price to Book Value, Price to Sales, Earnings yield, cash-flow yield, and Earnings Before Interest Taxes Depreciation and Amortization (EBITDA), among others.

The S&P 500, the barometer for the U.S. Stock Market, has historically traded around 15X forward year earnings. During the Dot.com bubble in 2000, the S&P 500 traded above 30X earnings, the most expensive it had ever been. Conversely, the S&P 500 has traded below 10X earnings a few times at the end of Bear Markets.

Importantly, the Dollar price of a stock does not reflect whether it is expensive, cheap or fairly valued. There are many stocks that trade well above $100 that are considered cheap, while others that trade below $10 can be very expensive.

W *is for* Wall Street Journal

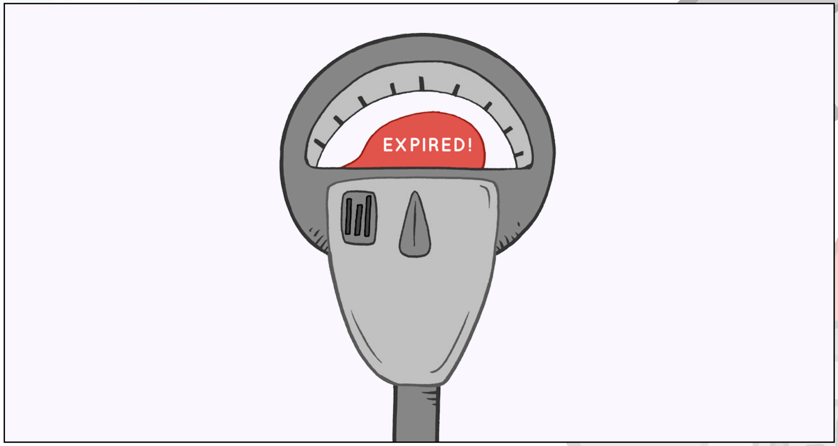


The Wall Street Journal is the standard in financial journalism. The daily newspaper covers global stories pertaining to finance, economics and politics, among others. Before the advancement of the internet, the WSJ was a primary source for stock quotes and other market data. The WSJ is the largest U.S. newspaper in circulation.

The Wall Street Journal first went to print in 1889. The daily newspaper was created by journalists Charles Dow and Edward Jones. Dow and Jones first wrote a daily market summary called the “Customers’ Afternoon Letter”. The duo went on to create the Dow Jones news wire service and the Dow Jones Industrial Average (DJIA); the first stock index for the New York Stock Exchange.

The Wall Street Journal is one of the most recognizable and respected periodicals.

X is for eXpiration

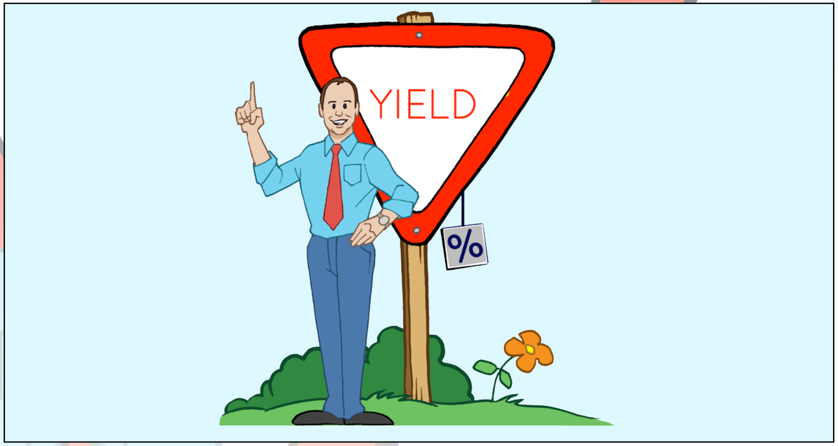


When an investor buys an option, the contract gives them the right -- but not the obligation -- to buy or sell the asset at a pre-determined price, within a defined period of time.

If the investor chooses not to exercise that right, the option expires and becomes worthless and the investor loses the money paid to purchase the option.

Option contracts typically cease trading on the 3rd Friday of every month with the actual expiration on the following day: Saturday.

Y *is for* Yield



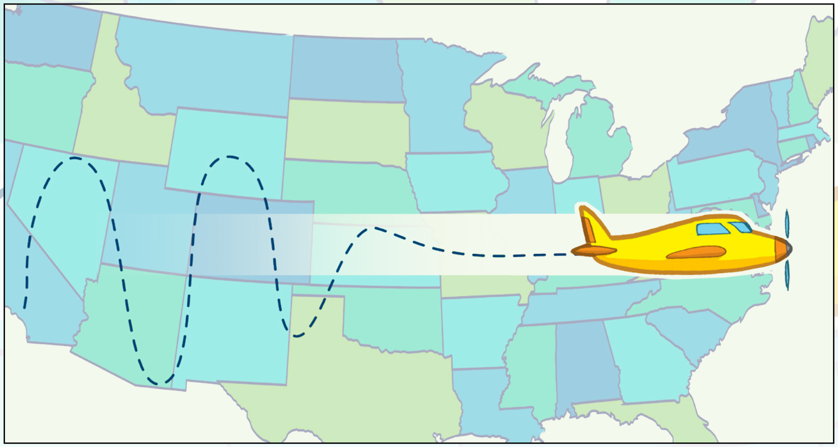
Yield is the percentage of income returned from an investment, usually shown in annualized terms.

A stock dividend yield shows the percentage of income received relative to the current market price of the security.

Yields fluctuate regularly as security prices change. The yield is a mathematical relationship between the annual income and the security price. A stock trading at $25, which pays shareholders $1 dividend, is yielding 4%.

Bond yields often refer to the interest payment relative to current market value or purchase price. They are commonly called Current Yield or Yield to Maturity.

Z *is for* Zero-Coupon Bond

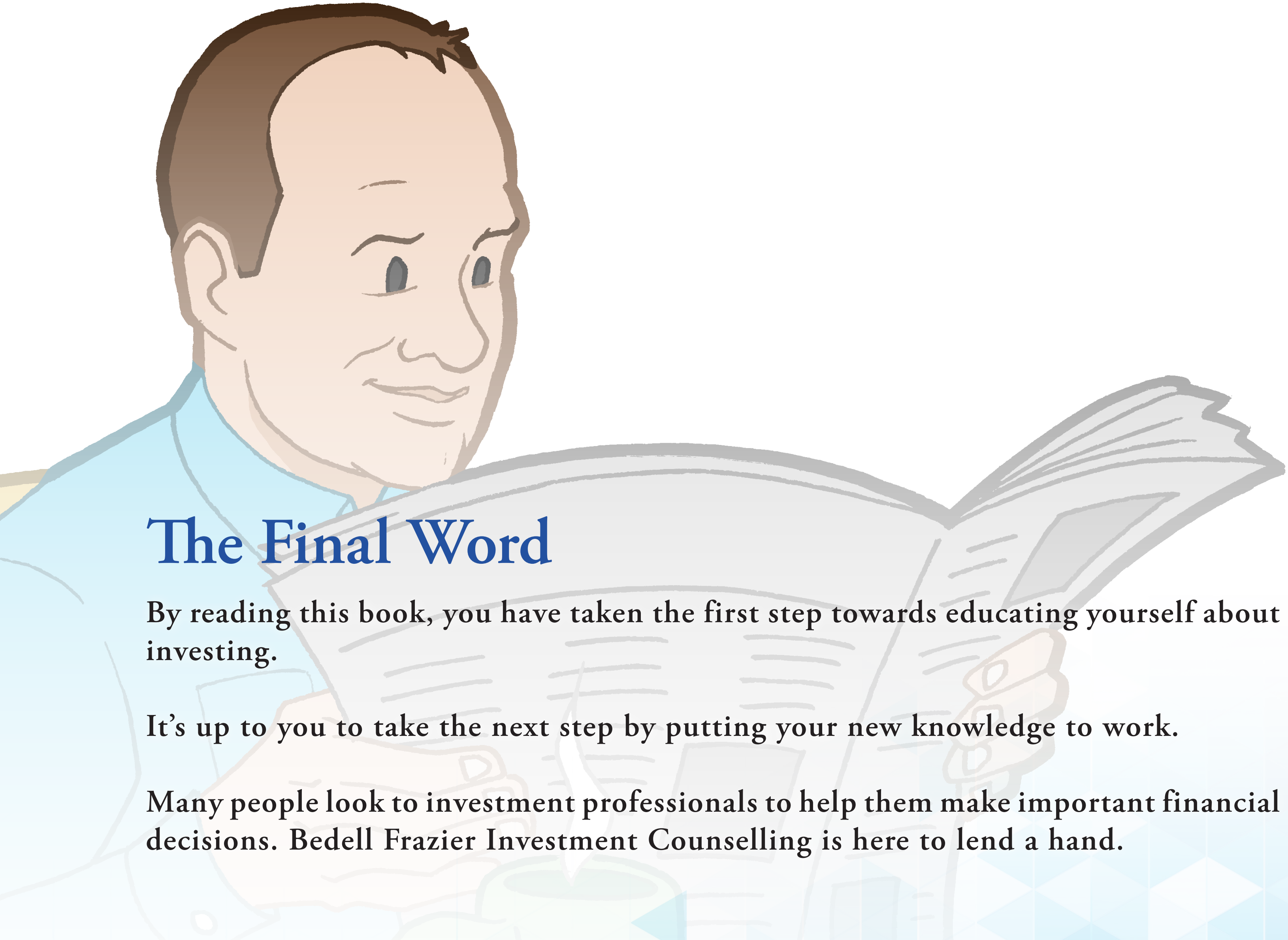


A zero-coupon bond is issued at a discount to par value, and matures at par value. The bond is designed to pay out upon maturity. There is no annual interest payment made.

An investor would purchase a zero-coupon bond when they don't need annual income but are looking for a predictable and substantial payment at a future date.

Zero-coupon bonds are strategic investments for retirement and education planning. Maturity dates can coincide with an expected need of cash.

Like an airplane, which can experience midflight turbulence, but is generally on autopilot until it reaches its destination, a zero-coupon bond can experience volatility with interest rate fluctuation, but the closer the bond gets to maturity, the more it is locked into its par value final destination.



The Final Word

By reading this book, you have taken the first step towards educating yourself about investing.

It's up to you to take the next step by putting your new knowledge to work.

Many people look to investment professionals to help them make important financial decisions. Bedell Frazier Investment Counselling is here to lend a hand.

Mike Frazier

Mike is the President of Bedell Frazier Investment Counselling, LLC. He is the chief executive of the firm, and runs the daily operation in addition to managing client portfolios and oversees investment strategies. Mike has over 20 years of industry experience, and has been with the company since 2002. Mike became a partner in 2004. In 2011, the company changed its name from Bedell Investment Counselling to Bedell Frazier.

Mike began his professional career in the media industry with CNN & Turner Broadcasting in Atlanta. It was at CNN where he was exposed to global issues, including economics, politics and geo-politics at the professional level. He entered the investment business in 1998 with SG Cowen on the institutional equity side. He earned his B.A. from the University of California at Berkeley where he majored in History and played rugby. Always a student of the Market, Mike continued his education in the evenings taking courses in securities analysis, modern portfolio theory and financial planning at UC Berkeley extension.

Mike and his wife Shelley are the proud parents of three daughters; Samantha, Nikki and Brooke. An avid sports fan, Mike also coaches youth softball and soccer.

For more information about

Bedell Frazier Investment Counselling, LLC

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www.bedellinvest.com


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INVESTING FROM A TO Z

by Mike Frazier