Allianz

practice #02

Future Workout Deep Dive

#02 Investment 101

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Intro

You're ready to manage the now. But what about the future? In this session, we cover the basics from the question of what is investing to introducing the topic of risk tolerance. And for those who feel more confident and want to get beyond the basics of investing, we provide an introduction to diversification and how to invest sustainably.

So wherever you're at, one thing's for sure: The earlier you start in life, the better prepared you will be for managing your finances.

Knowing you've invested in your financial future off the field means you can focus even more on delivering on the field, according to Olympic Champion in Javelin, Thomas Röhler.

So, what is investing?

Put simply, investing is buying into something you think will increase in value over time. But as you'd expect, this chance to grow also comes with risks.

As you hear repeatedly in the investment world, there are no guarantees, and you could get back less than you invest. In the worst case, you could even lose everything you invested. Therefore, before taking any important decisions about your savings, we would always recommend to consult an expert for advice.

If there are risks, why bother then?

Putting your money into a savings account with a bank is the simplest form of investing. However, in the current economic scenario with inflation at a higher rate than the interest on a savings account, you run the risk of actually losing money. Through a broader, more diversified investing, you can give yourself the chance of getting a better return while minimizing the risks mentioned.

Getting started

When it comes to investing, the start can feel overwhelming. One thing that helps is being aware of your current and future financial responsibilities and having clear goals in mind.

- Are you looking to finance a couple of gap months between the end of your sports career and the time your post-sports career takes of?
- Or perhaps you'd like to save for a longer-term goal, say financing your retirement in 40 years from now?

Knowing your timeframe makes a big difference in the choice of your investment strategy. Some investment opportunities are more appropriate to finance your short-term goals, others might help more to contribute to your long-term goals. Additionally, the risk of different types of investments can vary. Being clear on your goals will help you decide which level of risk you're comfortable with.

Starting early

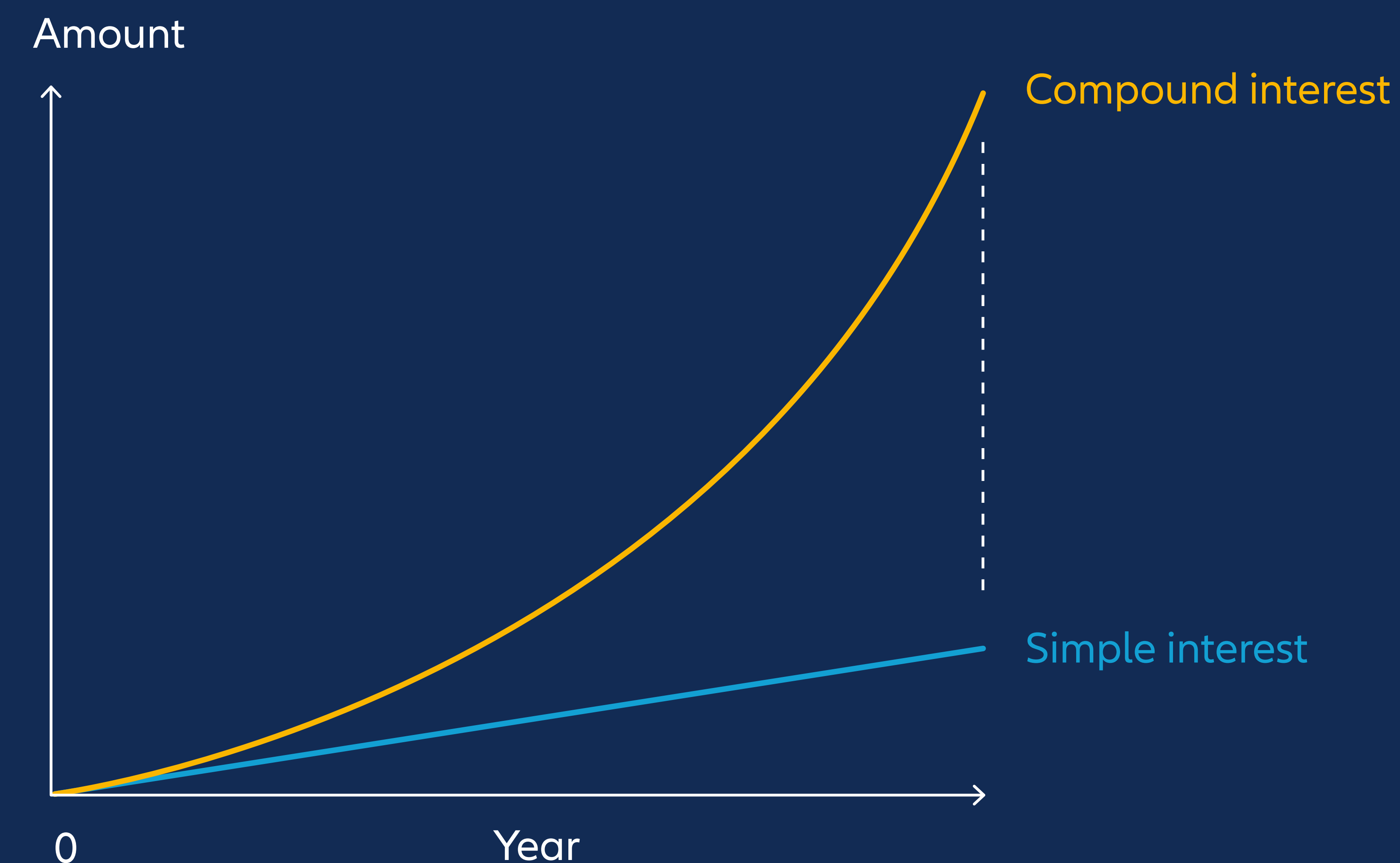
The earlier you start in life, the better. Why? Even just a small amount per month accumulates over time and works towards your long-term goals. With compound interest (which will be explained below), you will receive a greater rate of return over time, as your accumulated investment increases.

Stay **patient**

When it comes to compound interest, patience pays off. Compound interest is effectively the interest you receive on your investment and interest of the past. This ultimately leads to an exponential growth of your initial investment.

The power of compounding

Compound interest versus simple interest



Stay **patient**

So, the earlier you start investing and the longer you invest for, the more likely you are to see a benefit over time. This is where even starting with small amounts can make a difference over time.

Let’s look at an example:

If you had € 1.000 in a savings account and the interest rate was 2% per year, compounded annually, how much would you have after 5 years?

a) More than € 1.100
b) Exactly € 1.100
c) Less than € 1.100

Click to see the answer

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Know your risks

One topic that is closely connected to any form of investment is risk. When we talk about risk, we predominantly see two aspects:

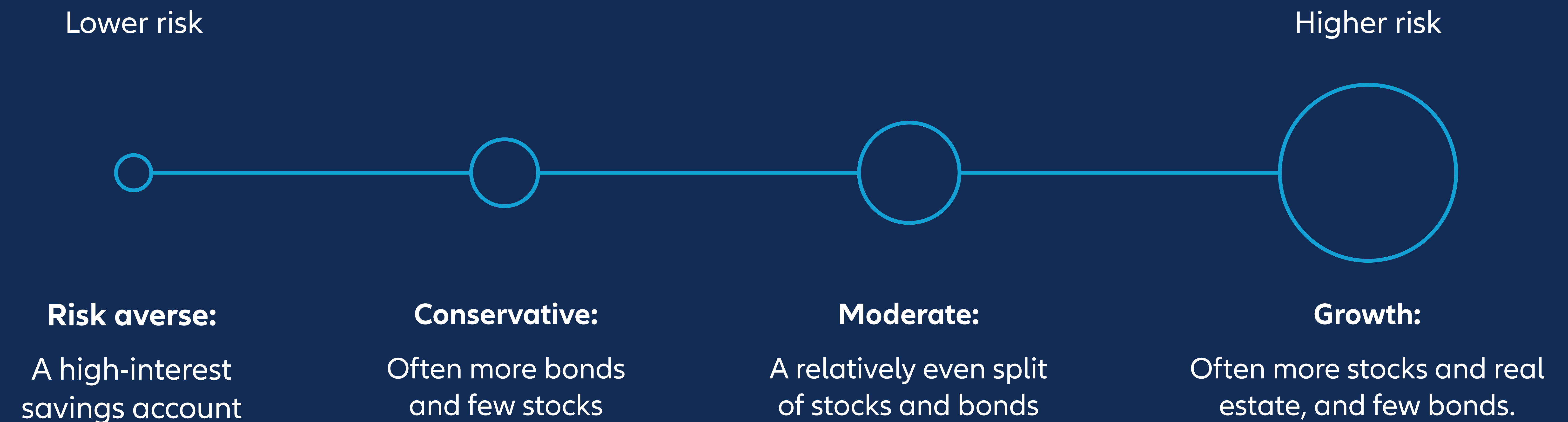
1. Your risk tolerance

Once you've decided to invest, you'll almost always be asked to check your risk tolerance. You should only take risks you're comfortable with. Determining your risk appetite can be rather tricky. It is not only about how much you'd be prepared to lose, worst case. It's also the ability to withstand market turns and the inability to predict what's ahead. In other words: how high is your comfort level with uncertainty.

Know your risks

Try our investment personality test:

Take the right financial risks
Your goals, timelines, and risk tolerance will help you decide



Source: Wealthsimple. For illustration purposes only. Not intended as investment advice.
Actual rates of return may vary. Illustrative returns do not account for taxes or other expenses.

Know your risks

2. Your risk capacity
Your risk capacity, or how much investment risk you are able to afford, is determined by your individual financial situation. Risk capacity is more flexible and changes depending on your personal and financial goals—and your timeline for achieving them.

If you have your own business, kids approaching college or elderly parents who depend on you financially, you may be less likely to comfortably ride out a weak market (given your constant income needs) than if you're single and not holding any major financial obligations.

In addition, an unplanned financial shock—like job loss, an accident that comes with expensive medical bills, or a windfall by e.g. winning a major competition and receiving a large price sum —can also affect your investment decisions by altering the amount of risk you're able to afford.

Diversify

Putting all your eggs in one basket is seldom a good idea. **Mix it up.** Be aware of the challenges that could hit you – not only on the financial markets but also on the personal side.

Generally speaking, by diversifying you can reduce your investment risk. You can diversify your investments across different types of asset classes (stocks, bonds, real estate), industries, or parts of the world. If one part of your portfolio doesn't do so well, you haven't lost it all and some parts of your portfolio might even mitigate the losses of another part. Through diversifying you can also mitigate the liquidity risk since some investments can be transferred to cash easier than others.

Put your eggs in different baskets

Diversifying your investments means you can minimize risk and maximize rewards

Inflation linked bonds

Defensive stocks

Nominal bonds

Real estate

Growth stocks

Source: Wealthsimple. For illustration purposes only.

Diversify

It's also good to be aware of our own **overconfidence**. Naturally, we look for the best in life and the best possible outcome. But do check the rational side of your brain before plunging into your dream investment opportunity.

Additionally, we should be aware of loss aversion. This refers to a phenomenon where a real or potential loss is perceived by individuals as psychologically or emotionally more severe than an equivalent gain. For example, the pain of losing $100 is often far greater than the joy gained in finding the same amount.

Diversify

Here's a quick example of some investment projections:

You can invest in two projects.

- Project A: 10% or 6% return, with either outcome equally likely.
- Project B: 12% or 4% return, with either outcome equally likely.

Compared to Project B, Project A has...

a) Higher return and lower risk
b) Same average return and lower risk
c) Lower return and higher risk

Click to see the answer

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Invest sustainably

When it comes to investing, you can also think sustainably.

That includes for example caring for our planet.

Thus, when looking to achieve a return on your investment, you can also consider the environmental, social and governance (ESG) factors involved. For example, at Allianz, we drive positive outcomes and embed sustainability in our core business processes to manage risks and capture opportunities. We exclude certain sectors, companies and sovereigns from our businesses e.g. companies involved in coal-based business models.

Why not ask your bank or insurer which sustainability initiatives they're supporting?

So that's some basic guidance on how to start. But what could you actually invest in?

Possible investment opportunities

We've covered a bit the what and the why, so now it's time to explore some potential approaches to investment. All of the following financial investments together might build a basis for your financial portfolio.

As previously mentioned, a saving account is a simple form of an investment. But there are many more possibilities ("asset classes") you can use to build a diversified financial portfolio:

Cash

This very basic form of investment (as in a classic savings account) is considered to be rather low-risk, as the probability of losing your money is low. However, this low risk is bought by lower returns than other asset classes and a potential devaluation of your money because of inflation.

Bonds

A bond is an investment that pays a fixed income. Basically, you lend money to a company and, in return, they pay you back a fixed amount until the maturity date, which is the date when the money you originally invested is paid back to you.
Government bonds and corporate bonds are the most common types of fixed income products. The government or company will pay you interest for the life of the loan, with rates depending on inflation and the perceived risk of the loan (e.g. that the company you invested in won't pay back the loan).

Stocks / Equities

Trading stocks involves buying and selling shares in publicly-traded companies. When someone buys shares of a company, they effectively become a small part-owner of that company and have some claim on its assets and earnings, in the form of dividends and/or capital appreciation. The other way to make money from stocks is that you sell the shares at a higher price than you paid for them.
But the market can change. Share prices have been known to go up and down and some companies can even go bankrupt - so you could even lose your investment.

Funds

A mutual fund pools money from different investors in one large pot. The fund manager takes advantage of the larger amount of money in this pool he is able to invest and distributes the money in different types of assets including stocks, bonds, commodities, and / or real estate. This is in line with the concept of diversification, as mentioned earlier in this module.

Exchange -traded funds (ETFs)

ETFs, which are a subset of funds, will track a particular index, sector, commodity, or other assets. But unlike mutual funds, ETFs can be purchased or sold on a stock exchange the same way that a regular stock can since they only copy an already existing fund.

Real Estate

Real estate is considered to be its own asset class. One of the key ways investors can make money in real estate is to become a landlord. A couple of the big barriers here are the comparatively high amount you need to start your investment, as well as the liquidity of your money while being tied down for a long period of time. But if you have the means to invest in real estate, it might be a great way to secure your future long-term.

Additional fees

When building your investment strategy you should also be aware of the investing costs (e.g. expense ratios, market costs, custodian fees, advisory fees, commissions...). These costs vary across the market and it's important to research those costs in advance, so that you minimize investment costs and maximize your gains.

Three takeaways

So there you have it. Investment 101. As with all of this, start by thinking about your current situation and your future needs. And remember the following:

- Identify your risk tolerance and be aware of the risks associated with investing.
- If you believe in your portfolio, be prepared to commit, understanding your timeframe and potential liabilities.
- Diversification is a key feature of any well-established portfolio and will allow you to best manage potential hits.

Next up...

Insurance Intervals

We get it. You get to week three, having yawned your way through personal finances and investment, and then we hit you with insurance.

But as any good sportsperson knows, having teammates who've got your back and coaches who prepare you every step of the way can make all the difference to how you deliver on the pitch.

And it's the same with insurance. So get ready for both the sprints and the recoveries by knowing you're covered for exactly what you need. No more, no less.

Next up...

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Intervals