15 THINGS

YOU SHOULD KNOW

BEFORE STARTING TO INVEST

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ARE YOU READY TO INVEST?

Investing your money for the first time is a big step. In this guide, our experts will help you get off to the best start.

Low interest rates on cash savings since the financial crisis have meant that many savers have turned to the markets in the hope of achieving a better return.

Investing means taking risks with your money. This is not necessarily a bad thing – more risk could mean better returns – but if you are going to invest you need to be prepared for the fact that you could lose some, or even all, of your savings.

Before you do invest, it's crucial to assess your finances and make sure that you have the necessary safeguards in place.

- **PAY OFF ANY DEBT**

Make sure your debts are under control. The cost of your debt – in interest payments – is likely to outweigh the returns you receive from investments.

Focus on reducing debt to levels that are comfortable to manage or, ideally, pay off all debt before investing.

- **THINK ABOUT RETIREMENT**

It's unlikely that the state pension will be enough to maintain your lifestyle in retirement.

So it's vital that you start saving into a pension as early as possible. Make sure you're contributing to your workplace pension scheme or a private pension before investing any spare cash – pension savers benefit from employer contributions and generous tax breaks.

- **MAKE SURE YOU'VE GOT SAVINGS**

Have you got spare cash to fall back on? Before risking your money, you need some core savings an emergency fund to cover unforeseen events.

The generally accepted rule is to have at least three months' salary in savings before you invest. And make sure that these savings are in a high-rate savings account

FIVE TIPS FOR NEW INVESTORS

If you invest your money, you have much greater potential for growth than you do if you leave your money in a savings account.

In the current economic climate, with interest rates still around record lows, you could be losing out by keeping your money in a savings account because inflation will eat into your returns, meaning you could lose money in real terms.

Investing in the markets could enable you to achieve an inflation-beating return and help you reach your long term financial goals. But it's important to understand that when you invest, you are putting your money at risk.
The greater the risk you take with your money, the greater the potential for growth.

But with this comes an increased chance of losing your money. Before even considering investing your money, you need to be comfortable with the risks involved.

No investment is risk-free, and if you simply can't accept that there are no guarantees and that you could, potentially, lose some of your money, you are not ready to become an investor.

When making financial decisions, it's important to consider the five steps below before you do anything with your money.

- **WHAT ARE YOUR FINANCIAL GOALS ?**

Set clear goals. Are you just looking to grow your money? Or are you looking for a regular income? Is there a set amount that you want your money to grow by or a minimum income that you need?

Having set goals will help you to decide how much risk you need to take to achieve what you want. You may not have a particular reason for investing, but try to ascertain exactly what you want your money to do.

- **WHAT'S YOUR TIME FRAME ?**

Once you know what your goals are, work out how long you need to achieve them. This will give you a clear idea of the kind of rates of return that you'll need from your investments and whether or not your goals are realistic.

Factors such as your age and health are important to consider. If you have short-term goals (less than five years) you should stick to cash savings because, if your investments fall in value, you might not have time to recover your losses before you need the money.

Medium (five to 10 years) and long-term goals (10 years or more) are appropriate for investment, but some investments become less appropriate the older you get. You have less time for your money to recover if it falls in value and, if you're retired, your capacity to earn is diminished.

- **UNDERSTAND YOUR ATTITUDE TO RISK**

Understanding the risks you'll encounter when investing and deciding how much risk you are willing to take is fundamental. You might have a long time frame, and plenty of cash to fall back on, but if you don't think you would sleep at night if the markets became volatile, a high risk approach probably isn't for you.

- **HOW MUCH CAN YOU AFFORD TO INVEST ?**

Be realistic about how much you can afford to invest. Assess all of your liabilities, such as debts, insurance premiums, pension contributions, savings and living costs, to see how much spare cash you have to invest.

Investing works best when you can take a long term view, so stay in cash if you think you might need the money in the next five years.

- **SEEK FINANCIAL ADVICE**

Many investors make their own decisions, without advice. But DIY requires time, knowledge and confidence.

If you take financial advice, you'll be able to talk through all the points raised above and ensure that your investments are tailored exactly to your needs.

LUMP SUM OR REGULAR SAVINGS ?

Should you invest all of your money in one go, or drip feed it into the stock market over time?

This might seem like a purely practical consideration – but it can have a big impact on your returns

Your decisions will invariably depend on your circumstances, but you should also consider your attitude to risk and think about where you are investing your money and why.

If, for example, you're comfortable with the risks and have a strong conviction in your choices, you may want to invest a lump sum.

However, if you don't have a lump sum, or if you're cautious about going all in, you might prefer to adopt a regular savings strategy.

INVESTING A LUMP SUM

Say you have £10,000 to invest. If you invest all of it straight into the stock market, your capital has the greatest potential for growth, as it's immediately fully exposed to the market. The assets in which you invest, be they shares, bonds or units in a fund such as a unit trust, are bought at the same price and you can benefit from any price increases straight away.

The potential downside of investing a lump sum is that you're exposed to potential downward movements in the market. So, if you invested all of your money in the FTSE 100 (the stock market index that tracks share performance of the top 100 companies in the UK), for example, and it dropped by 20%, your investment would follow suit.

Staying invested in the stock market over a long period gives you the opportunity for your money to recover – but this could take a long time and would require a lot of nerve and patience on your part as an investor.

You also have to think about market timing – are you investing at a peak or at a low?
This can be hard for even professional investors to judge.

Regular savings and 'pound cost averaging'

Regular savings offers the opportunity to make market fluctuations work in your favour. The strategy involved is known as 'pound cost averaging.'

Pound cost averaging describes the process of regularly investing the same amount, usually on a monthly basis, to smooth out the impact of the highs and lows of the price of your chosen investment.

The effect of pound cost averaging is that you're buying assets at different prices on a regular basis, rather than buying at just one price. And while riding out the movements of the market, you could also end up better off than if you invested with a lump sum.

Let’s look at this in practice. If you invested a £10,000 lump sum and bought shares valued at £10 each, you'd have 1,000 shares. Now, if you bought £500 worth of shares per month over 18 months (amounting to £10,000 overall), you would buy 50 shares in the first month.

But if the share price went down to £9.50 in the second month, you'd be able to buy 52 shares, as the shares are at a lower price. Therefore, rather than your full £10,000 investment being affected by the drop in share price, only a small proportion of your money drops in value. After 18 months of movement in the share price, it might end back on £10.

If you invested with a lump sum, you'd still have the same amount of money and the same number of shares. But by regularly investing, you may end up with more shares and, consequently, some capital growth, despite the share price ending up the same as when you first started investing.

However, it’s important to remember that you may not necessarily benefit in this way using pound cost averaging. The potential downside of pound cost averaging is that if your investment continuously grows in value, you'll miss out on some of that growth.