IFB290: Listener Q&A – How Do You Start Investing with $1,000

[This transcript was generated by artificial intelligence. Timestamps are not 100% accurate depending on the platform used for listening].

Dave

0:00

All right, folks, welcome to Investing for Beginners Podcast. Today we have episode 290. We have three great listener questions that we're going to go ahead and answer. And so without any further ado, I will dive into the first one. So this was from Quincy Brown, what advice would you give a new investor who wants to invest $1,000 with an additional $100? Monthly? So Andrew, what are your thoughts on Quincy's? Great question,

Andrew

0:23

you know, I had my answer in mind. And I was going to do the standard kind of template that I always say that people, but I would say, actually, if I was brand new, I would probably take a small piece of that and just buy something that I was familiar with. And then maybe look at the $1,000. And then the $100 monthly later. And the reason for that is because if you've never bought a stock before, it can be kind of intimidating. It's not like a checking account, you put $100 in a checking account, you come back tomorrow, you have $100, in your checking account, you put, let's say, even $5 into a stock tomorrow, it could be down 25 cents.

So I think getting used to that might take a week or two. And so why not just buy something, if you like Apple, yeah, you have an iPhone, buy some apple, or if you find yourself in Microsoft excel every day, if you're fortunate enough to do that 40 hours a week, maybe you buy some Microsoft, and just get used to the process and see just really how easy and simple it is. I would do that first and then look at the $1,000 and $100. Monthly about you.

Dave

1:29

Yeah, that's great advice. I think that's actually I liked that idea, because it kind of encompasses a little bit of the Peter Lynch idea, you know, buy from something that you know, but it also helps you, you know, break the glass on getting investing, because it is scary opening an account can be a little bit overwhelming, it's easy, the platforms make it very simple to do. But it's a little overwhelming and you're realize what you're doing. And it's not a checking account, once you start to open the brokerage account, you realize that this is not a bank account, this is something different. And I know, I did this, and I'm sure you probably did, too, when you buy your first company, your first few companies, you watch them every day all day long.

Yeah, he just you want to see what's happening with Apple and whether it's going up or down or how you're doing with all that. And I think after a while, you kind of get away from that activity. And so I think that's probably kind of a really smart idea to start simple and small like that. And then once you've dangled your feet or gotten your feet wet, then you can start kind of unpacking. So let's say that somebody, let's say a Quincy does this. And so he invest, I don't know 100 or $200, he's got $800 to start investing, then what would be your recommendation,

Andrew

2:42

I feel like you can take two different paths, you could say I'm going to be a little more active here, or I really just want it to be set it and forget it. So if you want a set and forget it and you want to be invested like everybody else, just buy an index fund, which is a basket of the big companies that are in the stock market, and that will give you diversification. So you can't get super hurt from one individual company going under. And that's a great way to start. So you could do an s&p 500 index like spy, I like to recommend that one for some reason, that's easy for me to remember spy spy. And you just buy that, and then you could continue buying that every month, and you don't really have to look at it.

There is a danger there, you do want to understand that the stock market is like a roller coaster. So I would encourage don't just stop there continue the learning journey. The other approach would be to start looking at individual stocks. And you could find a service like what I offer where I offer my advice on what exact stocks I'm picking. And you could just follow that. Or you could start to I guess, roll up your sleeves and start doing picking different stocks yourself.

So maybe if it was, you know, if you knew you're going to do an additional $100 a month, maybe 800 is a lot to take a bite on your first real stock, if you will. Maybe you break that up. So I don't think there's any one

right answer to any of that. But maybe if you have a sense of I know I want to be a little more involved. Or I know I want to trust somebody to do it for me, or I want to just be completely hands off. I think that helps answer the question. And hopefully you can take one of those ideas and run with it.

Dave

4:22

That's great advice. He really goes back to that whole idea of trying to decide what kind of investor you want to be and how active you want to do and all this. Sometimes there's a stigma I've said this before, it's sometimes there's a stigma of you know, you got to be a stock picker, you got to be, you know, an indexer. And you don't you can do both. And there's nothing wrong with you know, building a base using index funds. And then, you know, if you really want to start to learn how the market works and start to investigate individual companies like Apple, for example, that could be your your test run.

And you could spend some time really kind of trying to analyze it and think about all the principles that we've talked about through the years and use those was as as a guidepost, or a map of this is how you can start to try to analyze a company and look deeper in and determine whether that's really what you want to do. And I think those kinds of ideas too, are probably a little safer. And also will keep you in the market who will hear raise their hand, has bought a kind of going out in the limb and bought something maybe they shouldn't have bought. And they ended up losing all their $1,000 or 800 of the $1,000.

Because they bought at too high of a price that the company tanks, and they get out of the market, and they never invest again. And we don't want anybody to do that. And so I think it's better to like Andrew said, take a smaller bite of something, and then decide what kind of investor you want to be and then work from there. And there's nothing wrong with deciding I want to be an indexer. And then you decide individual stocks are really the way I want to go and vice versa. And so you could really branch into the individual stocks and go, you know, this is more work than I really want to do. And, and become an index, you know, using mutual funds and index funds.

There's nothing wrong with that either. It's the more important part is investing and staying invested and continuing to do it. Because my favorite sprays and water dripping on a stone will make an impression. So if you keep at it, you will end up in a good place at the end. Great advice. All right. So let's move on to the next question. So we have should someone invest in the South African market? Or is investing overseas a better decision and this is from D at NY? G. So Andrew, what are your thoughts on this question? This is kind of interesting,

Andrew

6:40

I guess, to give context, obviously, me and Dave are both in the United States, US citizens. So it's natural for people to want to invest in the own country that they're in. And I know when I first started investing, that's what came absolutely natural to me. And that makes sense. As far as continuing to invest that way. There are a few reasons that I continue to look primarily in the US stock market. And it's because they have the biggest companies, and also one of the biggest GDPs in the world. China would be right up there in GDP, depending on how you're measuring it. But China also has a history of nationalizing foreign investors.

So you can go back to the 1950s, they had some history doing that. So you know, you take China out of the equation, what's left you have the US they have a huge GDP. So that's kind of a GDP, if you're not an econ Master, you know, GDP is just like a way to measure how big the economy is. So it's very helpful in my mind to find the big economies and the big companies, because those have a lot of advantages over small companies. So for example, I wouldn't necessarily want to invest in somebody who's coming up with a new soda product, when I know there's Pepsi or Coca Cola, who could very easily create something that's better. That sounds harsh. If you're in that business, I don't mean to offend you.

But that's, that's just as a generalization. You can kind of use that framework for a lot of different businesses. And so a lot of the businesses that are in the United States have these great advantages. And that's why I primarily invest in the United States. Not to say that there aren't opportunities in South Africa. But admittedly, that's a much smaller economy. And there isn't much us or let's say, people in Europe who are buying stocks are down. There are many reasons. But one would be that. Generally, it's easier for bigger companies to compete against littler ones if they're in the same field. Yeah, have you looked at South Africa at all?

Dave

8:51

I know, I never have admittedly, the really my only exposure to any sort of economics or any sort of not none investment, but much about the South African market is through the wine industry. When I was working in the wine business years ago, I did some research on some of the wines that that came out of South Africa, and they had fantastic products. And they were not as well distributed, or as well known as some other parts of the world.

But they they made some great stuff. But that's really been my only economic exposure to the South African market. And so that's not been some place that I have been drawn to doesn't mean that there aren't great

investments there. But as somebody like Andrew was saying, you know, the home bias is a real and when you when you live in your country, whether it's South Africa or whether it's Australia or whether it's Japan, it's very normal to want to invest in your particular geography because you know, at the best, you may not know the ins and outs of the intricacies of each particular company. But when you live in that country, you are familiar with the code The term you're familiar with the language, the economics, and what's going on the news, the trends, all those things are going to be far more natural to you than when you invest outside of your own country.

And one of the things that I've always struggled with getting somewhat getting over it, but not as much is when you invest in someplace like South Africa, or I'm sorry, South America, like Brazil, for example, where my fiance's from I know the country, somewhat air quotes somewhat, but I don't always understand the differences in the culture between the United States and Brazil. And so sometimes when you are analyzing or thinking about and a potential investment there, and this is not a slam against the country, or the companies by any stretch, but it's different. And so you have to account for that.

And one of the ways you can account for that is trying to build in a margin of safety to hedge your bets against being wrong, because what happens in the Netherlands is going to be different than what happens in New Jersey. And so you have to kind of try to account for that. And that's kind of the way that I look at it. So is it better to invest overseas, I think it really depends on what you're trying to do and where you're trying to go now. Again, US citizen home bias, take this for what it's worth.

But if I think about a lot of my friends that are in the investing community via Twitter, whether they're in Europe, or whether they're in Southeast Asia, or whether they're in Canada, a lot of them invest in the United States, because it's the largest GDP, it's the largest economy in the world. And they have some of the better the best businesses in the world. And they're great investments, Berkshire, Hathaway, Google, Microsoft visa, you know, the list goes on and on. And so that's why a lot of people choose to invest there. But I think to Andrew's point, if you're looking at a smaller company in your network or your home, Herve, I think it's easier to analyze that company than it would be in another in another country, because you don't understand some of those things that I was discussing. And we also haven't really talked about the accounting is different.

The accounting in the United States is different than the rest of the world is not hugely different, but it is different. And sometimes there can be some shady Enos that goes on outside the United States. And without pointing fingers, China, you know, there are some companies that they don't get regulated as well as maybe they do in the United States. And so again, that's something I'm not saying, don't invest in China, that's not for me personally.

But if you're going to do that kind of thing, you have to think about the downside, and what are the potential risks and you have to factor that into your investment? If you don't, then you're going to be caught surprised. And I think that's why I have chosen to primarily invest in United States. But I am looking at Brazil, and I do have some investments in Canada and Europe. And I guess one in Taiwan, don't need to think too hard about what company that is. But anyway, so you know, I have learned to try to branch out but I'm still more focused on the home bias. What about you?

Andrew

13:09

Yeah, I would say that was a really great answer. By the way, that was a lot of good information. I would say that. This is like a dynamic thing. And I think it's going to change over the decades, maybe. I mean, hopefully, for the US, I'm in the US. So I hope that things don't change too much, because businesses here are good. But for example, in the 1980s, the Japanese companies were really I mean, not only was their stock market really good, but those businesses were really, really good. They brought what's called Six, six sigma manufacturing.

And they just had the ultimate and they still do, but the ultimate quality and the products they would create. That's why you saw a lot of their cars come over here and still do well. But for a while that was the stock market to be in. You can listen to our episodes we did with Eric slynn Way back in the archives, if you want to hear a couple horror stories of how that can go the other way. But the point is, is that these things are fluid, they're they change over time.

So if you're picking stocks, you want to be cognizant of how these factors are. So I think it's a really, really good question. And I think it should be considered. And I'm glad this listener brought it up. The only other thing I would add, which is depending on if you're in a retirement account, it might be a little bit different than if you're in a regular taxable brokerage account. But there are also every country is different in taxes. And the US has tax treaties with some countries but not with other ones.

So for example, if the US had, I don't know, South Africa because those companies have not come up on my screens. They don't meet my criteria for one reason or the other. But let's pretend that there is no tax treaty with South Africa, then you would get taxed as a you, if you were in the US, you would get taxed from the IRS plus you would get tax from the South African authorities. If you are investing in a country where there is a tax treaty, you probably will only get taxed one or the other, or you could get taxed on both. And then the IRS is going to give you a refund because of the tax treaty.

So that's another thing to keep in mind when it comes to investments, because if you make 12% on your money per year, but you're paying 30% in taxes, and then 20% in taxes, it doesn't take a mathematician to realize that you're not actually growing as much as if you had paid no taxes or local taxes. So those are all factors. And hopefully that additional information is helpful. Yeah, gotta love taxes,

Dave

15:51

right?

Andrew

15:52

Yeah. All right.

Dave

15:54

So next question we have is how do you identify the risks in business with high payout ratios, but also high growth like PepsiCo? And this is from Luke. So this is a great question to

Andrew

16:05

do you want to give a brief overview for beginners what the payout ratio is and what he's referring to their Yeah.

Dave

16:13

So for those in the unknown, so here's the download. To use a phrase from my generation, a payout ratio is the ratio that a company is comparing what a company will pay out, most people refer to this as dividends. But you can also include share buybacks as well. But let's just stick with dividends. Right now. It's a comparison of the dividends that a company pays out to the earnings, or the bottom line, or the net income that a company earns for the year. Now, PepsiCo is one of the dividend aristocrats they've been paying a dividend for a very long time. And so this is something that dividend investors follow very closely.

And basically, what it is, is a ratio between the dividends that they pay out and the net income or the earnings that the company generates. And generally, the higher the number, the better the dividend is. But it also means that it could be more at risk. And so those are, those are kind of the, I guess, the factors when you're thinking about a payout ratio. So does that help answer that question?

Andrew

17:19

Yeah, I think it does. Okay. I miss anything? No. Okay.

Dave

17:24

All right. So when we look at a company like PepsiCo, then how do we balance the payout ratio, a high one, and growth? How do you kind of balance that out?

Andrew

17:34

Yeah, it's tough, right? Because, by definition, if a stock has a high payout ratio, they have less profits to invest in themselves. And so that makes it very hard for them to grow unless there are other reasons for their growth that don't need as much investment. So the there's always trade offs, you know, we love to say it depends. But in reality, there's always trade offs. So the trade off is if there's a higher payout ratio, the yield you're getting, which is the dividend income you receive, when you buy the stock, is probably going to be much higher.

But that also depends on what the price of the stock is. So that's the plus side having the higher payout ratio, the negative side is what you just are, I guess, what I just said, is the idea that you don't have as much money to reinvest in the business to have future growth. So in my mind, it's really case by case and it is a balancing act. And, you know, the good thing about dividends is it keeps managers from being a little too spendy on their profits, and maybe wasting it on ambitious projects. But the downside is, again, the reduced growth potential.

So I kind of see as a balancing act, I also see it as it depends on the business. So I'll give an example. And every time I've given an example of a company, my portfolio, the next three to six months has been awful for it. So I apologize for you, if you have this company in your portfolio, I have paychecks in the portfolio. And they used to have an even higher payout ratio. But if I look at the payout ratio through the late 2010s, it was

always around 80%. And so you think about, they only leave 20% of their profits to put back in their business and do other things. But if you think about what paychecks does, basically, they are a paycheck processor.

So you know, if you have a small business, and you have three employees and you want to pay them and you don't want to deal with all the paperwork, administration and taxes, blah, blah, blah, you can just use paychecks and they can give those paychecks out and make it really simple. So for them, they kind of naturally grow. If I'm a business, hopefully I'm hiring people every year. So if I hire three, four or five, six people, that's more money, the paychecks every new hire, then so that particular business doesn't need a whole lot to have future growth. But they're also not probably going to grow like 20% a year, because there's only so many small businesses out there in the United States. So that's kind of where I'm not too worried about the high payout ratio, because it makes sense with their business model.

But you could have another business where maybe they haven't grown at all, you know, maybe their revenues are flat, or they're actually declining. And yet they have a payout ratio at 80%, then you might start to think, hey, maybe they should not pay as much of a dividend so we can actually get the growth train running again. So I think it really depends, it is a balancing act. But that's how I would look at the risks of a high payout ratio versus the potential rewards from a high payout ratio.

Dave

20:48

Yeah, that's all great stuff. And I think I love the way you kind of explain that and talk about kind of where the company is, and what they're trying to do, it all comes down to this as part of the capital allocation for the CEO. And this is where we can, from the outside judge how well we think the company is allocating its money, because when they're giving us a dividend, that is now becomes our money. But we can decide whether we think that that is a good decision to pay us so much.

When the business is a either doing well or not doing well. And there's always trade offs, you give us 80% of their earnings that like Andrew said, There's only 20% left to reinvest. Well, if they have lots of opportunities to, to reinvest, and they choose to give us a big payout ratio, and they come across an opportunity, they either have to pass, or they have to do something like take on debt or issue equity, which may or may not be in the best interest of the business.

And so this is really where it comes down to the capital allocation skills of the particular CEO. That's our CFO who's running the company. And you can judge how well they do or don't. And the other part about dividends, which is NB challenging, is that once a company starts paying them, the stock market hates it

when they cut it, or they stop paying it, that's usually very, very bad for the stock price. And you know, as investors, we never want to see that.

So once a company starts paying a dividend, they have to think about how they want to balance that out with the other things that they may or may not try to do. And some of it too, it's going to come down to the maturity of the business and where it is. And it's kind of evolution of a cycle of a business, like Coca Cola, doesn't have as many opportunities to reinvest, as, let's say, paychecks does, for example, because maybe they're not as far your paychecks isn't as far along in their evolution on the scale for businesses. So maybe coke has a different mentality.

And though but those are all things that when you analyze the company, you'll kind of realize and they can help you determine whether it's good or not good. But it all comes down to the capital, capital allocation skills of the business. And that's why it's really important to really analyze this part of it and study it and determine whether, you know, if they're spending all their money in dividends and buybacks, and they have nothing left for growth, then like Andrew was saying, at some point that's it's going to give, and that may or may not be the best thing for the investors.

Andrew

23:33

So do you have any examples of any companies with a low payout ratio that do a great job of reinvesting their profits for future growth?

Dave

23:41

Yes, the first one that springs to mind is visa. So visa is paying out a blistering 19% of their payout of their earnings in a dividend. And so that leaves them 81% That they can reinvest in the company to do other things. And so they've been paying a dividend for a very long time, but it's not a big part of their capital allocation. The majority of it, they either use for buybacks, or they use it to reinvest in the business.

And that's a really good, I think, example of a company. Another great one that kind of springs to mind would be Apple, Apple's yield, or their payout ratio is pretty low, compared to what they could pay out because they got a lot of cash and they got a lot of cash on the balance sheet. So if they wanted to pay out a really big dividend, they could do it for sure. It's a Cash Generation Machine. But Tim Cook has chosen wisely

think to not to pay a dividend, which is great to give back to the shareholders. But I think he's also wisely holding back to use that cash or to build on a business what once what springs to mind for you,

Andrew

24:45

a man and taken all the good ones here. I mean, an easy one is Microsoft. They also have the last couple of years their payout ratio has been below 30%. And they're obviously investing I mean, it's technology Jeez, it's tricky because it can be like this never ending rat race to reinvest. But they have done a good job of finding projects. So that really paid off for them. The cloud being one of those and being the infrastructure of the internet, that's been super, super high growth for them.

And so Satya definitely seems like he knows what he's doing. And the numbers bear that out. So I know they're investing in like 5g stuff. And I mean, you could probably, we could be here all day long, just talking about the things we're investing in. So there's a lot of great businesses that do a lot of great reinvesting. But it is you do have to be careful, because a lot of businesses also waste it.

So it's good, I think to have that. I liked the way was it, Luke? Yeah. Yeah, I like the way Luke kind of approached it from a risk basis, because I think as investors, that doesn't always come naturally. But that's a good way to think about stocks is what's the downside trade off here? And if you can overcome that, then hey, this might be a great idea. Yeah, exactly.

Dave

26:01

All right. So we we got this great commentary from Stacey, I wanted to share with everybody. So hi, I've made all the mistakes that you have both mentioned. I want to thank you for sharing all your knowledge. I heard that you have a newsletter. Where can I subscribe to that? This is from Stacey. So Andrew, would you like to take that out?

Andrew

26:19

Yeah, you can just go on our website investing for beginners.com. We have a Products tab, you can click on there and the newsletter is right there future that the top you can't miss it. I do want to shout out all these questions came from Spotify, they have this cool new feature where you can write in. And so shout out to all you guys. Thanks for engaging with us. And hopefully we can answer more questions like these in the future

because these were all awesome. And last thing, no questions too stupid, because we always forget what it's like to be a beginner. So if you're an absolute beginner, please write in. I mean, our show is called Investing for beginners after all. So continue to write in and thanks for all the support and hopefully we'll talk to you all next week.

Dave

27:00

Perfect. All right. Okay, so that's gonna wrap up our show for this week. Don't forget to subscribe to the show on your preferred podcast app if you enjoyed our little show. If you would kindly consider giving us a review it greatly helps the show. And don't forget to browse the incredible materials we've created for you at E investing for beginners.com. Lastly, you continue growing your knowledge as an investing for beginners insider with insights and educational tips delivered right to your inbox for free sign up today. And with that, I'll go ahead and sign us off you guys go out there and invest with a margin of safety emphasis on the safety. Have a great week, and we'll talk to you all next week.

We hope you enjoyed this content. Seven steps to understanding the stock market shows you precisely how to break down the numbers in an engaging and readable way with real-life examples. Get access today@stockmarketpdf.com until next time have a prosperous day. The information contained just for general information and educational purposes. Only it is not intended as a substitute for legal, commercial, and or financial advice from a licensed professional review, our full disclaimer@einvestingforbeginners.com.