

Lesson 1: The Difference Between Investment & Speculation

Investing promotes the safety of **principal** at an **adequate return**.

- **Principal**: Say you invest \$1000 in the company Apple. This \$1000 is referred to as your principal. Is it the amount of money that you are initially investing.
- **Adequate Return**: You should not seek a large return on your money e.g. 50% return within a short time frame. Rather you should seek a safe return e.g. 5-10% over time.

Whenever you are **speculating**, you are NOT doing either of these two things:

- You are not protecting your principle (\$1000)
- You are not going after a safe return

Types of investors:

- **Defensive investors** look for marginal and safe returns. There is a high probability that these investors will receive such returns in the future.
- **Aggressive investors** seek large returns over a short period of time. They do not really consider the risks. Therefore there is a low probability that this type of investing strategy will reap the expected returns.

Here is an example:

Defensive Investor

	Principal	Return	New Value
Stock 1	\$1000	+5%	\$1050
Stock 2	\$1000	-2%	\$980
Stock 3	\$1000	12%	\$1120
Stock 4	\$1000	20%	\$1200

Say the defensive investor invested \$1000 each into 4 different companies (stocks). This investor chose stocks that were likely to generate small, safe and steady returns. After a period of 1 year, the total earned was **\$4,350**, which is an **8.75%** return.

Aggressive Investor

	Principal	Return	New Value
Stock 1	\$1000	-60%	\$400
Stock 2	\$1000	60%	\$1600
Stock 3	\$1000	5%	\$1050
Stock 4	\$1000	3%	\$1030

Say the aggressive investor invested \$1000 each into 4 different stocks. This investor chose stocks, which he thought, would have a high return. However these stocks ended up having a low probability of such returns for various reasons. After a period of 1 year, the total earned was **\$4,080**, which is only a **2.00%** return.

Rhetorical Question Summary:

- What is meant by the term 'principal'?

- What is meant by an 'adequate return'?

- Which type of investor has the higher probability of better returns in the long term?