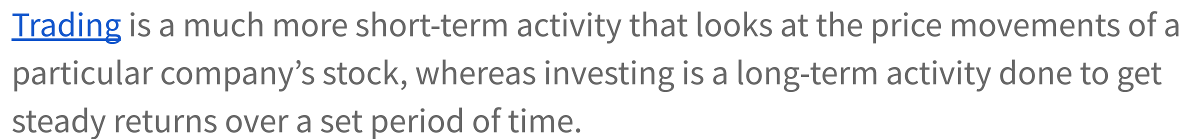
Stock Markets Guides

Author: Nishit Kumar

Stock Investing In-Depth Guide

While most people use stock trading and investing interchangeably, both words mean very different things.



Trading is a much more short-term activity that looks at the price movements of a particular company's stock, whereas investing is a long-term activity done to get steady returns over a set period of time.

Both trading and investing have different requirements, techniques, and tools being used. An understanding of these tools is crucial before you begin investing in the stock market.

What is Stock Investing?

Most people have several sources of income, both primary and secondary.

Primary income usually comes from a job or a business that you run. Secondary income could come from other sources such as rental income from properties you own, freelance income, or money you might earn through a YouTube channel. Whatever your sources of income might be, it is quite likely that at the end of a month, you have quite a bit of money just sitting in your bank account.

"What is the best course of action to follow with regards to this money?" is a question several people ask themselves, and it involves considering several alternatives. However, these can be broken down into 2 main categories, leaving your money in the bank and investing it.

Both these categories have been discussed below.

Leaving Your Money in the Bank

Consider a scenario wherein you have $100 left every week in your bank account after accounting for the taxes you pay and all other expenses.

If you leave your money in your bank account, its value keeps reducing by the year because of something called inflation.

To better understand inflation, you need to understand what purchasing power means. Suppose a bag of apples costs $100, then the purchasing power of this $100 is a bag of apples.

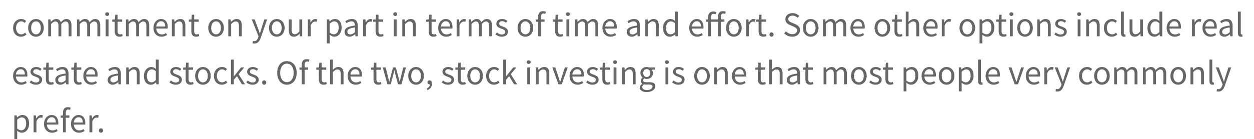
Next year, however, the price of this bag of apples will increase, say to $102. This is because the economy as a whole experiences inflation every year, and there is a systematic increase in prices throughout the market. This means that your $100 in the bank can no longer buy you a bag of apples. Its purchasing power has now gone down.

In summation, while it is a good idea to have some money in your bank account to deal with emergencies and extraordinary expenses, you're losing money in the long term due to inflation.

Investing Your Money

The alternative to not keeping your money in the bank is to invest it.

There are several avenues for you to invest your money. You could choose to do a business on the side and invest your money into that. That would require a large



commitment on your part in terms of time and effort. Some other options include real estate and stocks. Of the two, stock investing is one that most people very commonly prefer.

Stock investing refers to investing your money in various companies that are being publicly traded on the stock market. This is done by identifying companies with high growth potential, investing your money, and then waiting for the company to grow so that your investment grows with it.

There are two ways to profit while investing in stocks: you can profit through dividends and capital appreciation. Dividends refer to your share of the company's profits, which are paid out to all shareholders.

At the same time, the stock price appreciates over time as the company grows, which means that the value of your investment will grow with it, leading to a capital appreciation of your investment.

Stocks vs Real Estate Investing

Two of the most preferred methods of investing are stocks and real estate.

Stock investing has already been explained above as the process of investing in a variety of companies in the stock market. On the other hand, real estate investing refers to buying a piece of real estate and then renting it out to someone else.

There are two sources of income in real estate investing, just like stock investing: you get rental income from the tenants. The value of your property might also increase with time, resulting in capital appreciation. Both real estate and stock investing have their own advantages and disadvantages, which have been discussed below.

Stock Investing Pros and Cons

One of the biggest advantages of stock investing is that it does not require huge amounts of capital.

You can usually get started with a small amount and then gradually scale up. It is also easier for you to buy several different stocks to diversify your investments and reduce your potential downside. Stocks are highly liquid, meaning it is straightforward to sell off your shares in the stock exchange for cash if you suddenly need cash in hand.

All these advantages make stock investing a desirable option for most beginner investors.

However, stock investing has some disadvantages too. Stocks are often more volatile than real estate, which means that the value of your investment can fluctuate a lot very often.

All investors in the market are not rational, and the high liquidity of the stocks means that it is very easy to panic sell, which means that you'll end up taking a huge loss.

There are also numerous taxes associated with selling shares, called the capital gains tax.

Real Estate Pros and Cons

Just like stock investing, real estate has its own set of advantages and disadvantages that make it a popular option for investors.

One of the biggest advantages is that it is a constant source of fixed passive income in the form of rent, which is an attractive supplement to your own primary income. It offers the possibility of leverage, which means that you can buy a property for much more money than you currently have in hand by getting a mortgage.

Real estate has several disadvantages. The biggest one is that real estate is a very illiquid investment, which means that you will not be able to sell it if you need cash urgently easily. It also requires a lot more work than stock investing does, as there are maintenance costs to be paid for the property regularly, along with the hassle of finding a tenant for your property.

There are significant transaction costs involved with the purchase and sale of real estate, unlike with stocks where you only have to pay a minimal fee or commission to buy and sell stocks.

How to Start Stock Investing

If you're looking to start investing in stocks, there are several steps that you need to take to get started on the journey.

These steps include deciding what type of investor you wish to be, finding a broker, setting the parameters of your investing behavior, and learning how to analyze stocks. Each of these steps has been discussed below.

Identifying What Type of Investor You Want to be

There are two types of investors: active and passive.

An active investor chooses their stock through research and fundamental analysis, finds out everything there is to know about the company, and invests their money. Once this is done, the investor then constantly monitors their investment to see if the company is continuing to prosper as well as they thought it would.

If a change in the company shifts its fundamentals, they take out their money from the stock and invest it elsewhere. They are very hands-on investors, and becoming this type of investor requires a lot of research, technical knowledge, and time on your part.

The other kind of investor is a passive investor. They do not need to do their research, as they rely on experts doing it for them.

Such investors invest in mutual funds, a portfolio of stocks that an expert manages in return for a fee. Some investors even choose to invest in index funds, a portfolio of stocks with something in common.

For example, the S&P 500 is an index fund that comprises the 500 largest companies being traded in the USA. When you invest your money in an index fund, a proportion of your capital is allotted to each company that comprises the index. Passive investors do not have to constantly monitor their investments, requiring specialized technical knowledge or a large time commitment.

Finding the Right Broker

The next step you need to take as a stock investor is finding the right broker for yourself.

Finding the right broker is a research-intensive task, as there are several things you need to be mindful of:

- Is there a minimum investment or account balance that you have to maintain?
- What is the commission that the broker charges per trade? While this is not a huge concern if you're only making a few trades, it is still best to go for the broker who charges the lowest commissions.
- Is there a minimum activity level that you have to maintain? Most brokers levy a charge unless you make a certain number of trades every month, so knowing this is important.
- What countries/exchanges can you trade on? Most brokers offer the ability to trade both the NYSE and the NASDAQ and European exchanges such as London Stock Exchange. The more options you have, the better.

Trade on our award winning trading platform[1]

A faster, clearer and smarter way to trade. Seize your opportunities with a cutting-edge platform built around your needs.

Create demo account

Create live account

It would help if you found a broker for yourself that satisfies all your requirements and parameters, which means that the next step is to set your investment parameters.

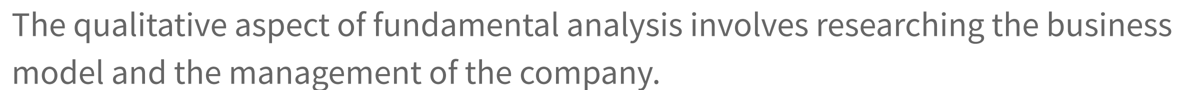
Setting Parameters

This is a large and comprehensive step and includes various other smaller questions that you need to answer before moving ahead. The primary parameters that you need to set are in terms of:

1. Capital: How much capital are you willing to invest in the market? Are you going to invest on a lump-sum basis or in incremental amounts every month? The answer to this question will affect the type of broker you can get and influence your investment strategy as a whole.
2. Time horizon: What is your time horizon for the investments? How long will you hold your positions? Your time horizon is a significant factor as it enables you to narrow down opportunities.
3. Type of stocks: What type of stocks are you planning to buy? Are you only going to buy high-dividend stocks? Are you only investing in a particular sector, exchange, or set of companies? Picking a selection of stocks is important as it will allow you to focus your research and efforts on a limited set of companies, and then you can devote your time to analyzing them.
4. Diversification: How much of your capital are you going to invest in each stock? It is important to ensure that you don't put all your eggs in one basket and that your portfolio is diversified enough to insulate you against risks as much as possible.
5. Risk profile: How much risk are you willing to take on? Will you invest in riskier investments, or are you going to play it safe? This also narrows down your pool of opportunities and is a significant factor in determining the returns you will earn.

Learning Fundamental Analysis

If you wish to be an active investor, you need to begin learning how to analyze stocks. This is done through a fundamental analysis process, which helps you identify undervalued companies and offer good investment opportunities. Fundamental analysis has two parts: qualitative and quantitative.



The qualitative aspect of fundamental analysis involves researching the business model and the management of the company.

If a company's business model is stable and relevant in the future, it is a good company to invest in. Similarly, the kind of leadership that a firm has, or the quality of its senior management, is a major factor in deciding whether or not the company will be successful and reach its full potential.

The quantitative aspect of fundamental analysis involves studying the financial statements of the company in comparison with its competitors. This is done by using financial and accounting ratios to compare how the company has been performing in the past and forecast its future performance.

The company's ideal share price can be calculated using this, and this is then compared to the current share price of the company to identify whether the company's shares are undervalued.

Technical analysis is also often used in conjunction with fundamental analysis to analyze short-term price changes in the stock to identify the optimal entry opportunity for the stock. This involves using trading charts and statistical indicators to study historical patterns in the stock price and extrapolate future price movements.

Dividend Stock Investing

As mentioned earlier, dividends are a share of the profits that a company pays out to its shareholders.

Usually, companies only pay out a fraction of their profits as dividends, and the rest is then used to finance the company's future operations. Companies also try to achieve stable dividends. They only increase the dividends they payout when they are sure that they will consistently pay higher dividends in the future.

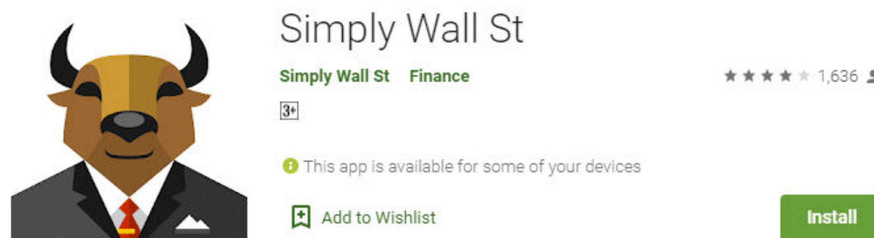
Dividend stock investing is the policy of investing in stocks that have high dividend yields. The dividend yield of a share can be calculated by dividing the dividend paid by the share price.

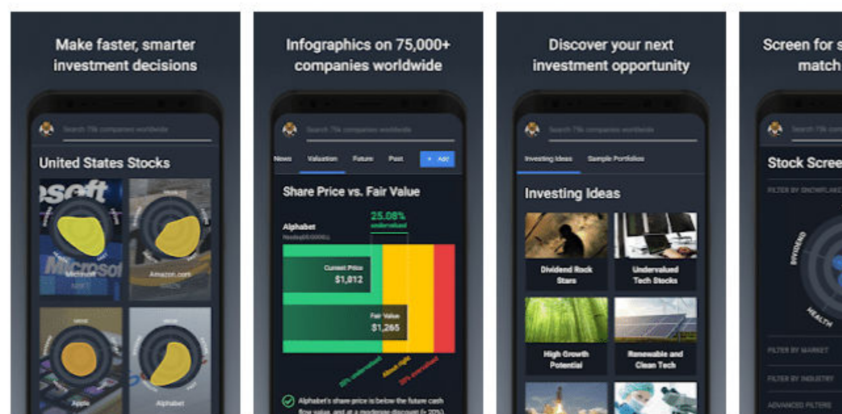
For example, if a company pays $1 of dividends on a $5 share, then the dividend yield is 1/5 or 20%. Dividend investing is an attractive option for investors since it offers them passive income every quarter when the firm declares its results. At the same time, dividends can also be reinvested into the same company's stock to grow your capital even further.

Stock Investing Apps

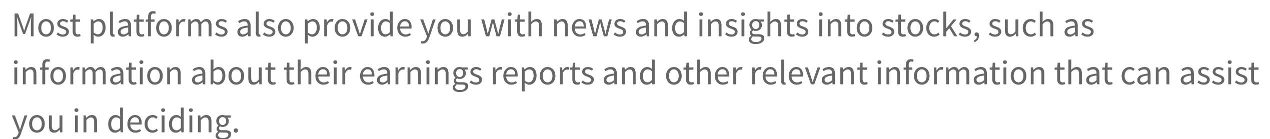
There are numerous apps that you can use to invest in the stock market.

Most brokers these days have their own apps, which have many features that will enable you to invest in the market.





Trading apps offer real-time prices from the exchange, the ability to view your profits and losses at any given point in the day, and a list of all the possible stocks and derivatives you can trade.



Most platforms also provide you with news and insights into stocks, such as information about their earnings reports and other relevant information that can assist you in deciding.

Investing apps allow you to view and analyze charts of stock prices through statistical tools such as Moving Average indicators, Bollinger Bands, and the RSI.

You can also add your own lines and tools to charts, which will allow you to analyze the chart and identify patterns in a much more effective manner. Some investing platforms also allow you to use leverage to invest, even though that is most commonly used for trading.

If you are investing with leverage, you can invest in a stock with more capital than you actually have, which gives you greater buying power in the market. For example, if you have a 10:1 leverage, you can buy stocks worth $100 using only $10 of your own capital. However, it is dangerous to trade on leverage, as any sudden volatility in the stock price could wipe out your account.

Penny Stock Investing

Penny stocks are a form of high-risk, high-reward investment available to investors who are more risk-friendly and willing to research.

A penny stock is a security that has a small market cap, low share price, and is not listed directly on any major stock exchange. According to the Securities and Exchange Commission, any stock priced at lower than $5 and not listed on a national exchange is a penny stock.

These stocks can be bought and sold through specialized brokers and are listed on pink sheets. They usually belong to up-and-coming companies that are not yet big enough to get listed on the stock exchange. Since these companies are not established yet, there is always a chance that they will go under, which causes the high-risk factor.

In addition to this, there is also a lack of any information or reporting requirements placed on companies with penny stocks.

For example, any company listed on a national stock exchange must comply with certain requirements and provide information to its investors. It also has to declare its quarterly and annual results promptly, through which anyone can see how the company has performed. There are no such requirements with penny stocks, and any available information is usually not from credible sources.

Penny stocks are also commonly used to scam gullible investors, so if you invest in them, make sure you do your research.

Lastly

If you have savings, keeping them in the bank is definitely a bad idea because you will lose money due to inflation.

The two next-best alternatives are to invest your savings into real estate or stocks. Both have their own pros and cons, but stocks offer a better investment avenue if you do not have a large amount of capital and wish to keep your investments liquid.

Stocks also offer a form of passive income in the form of dividends, which are paid out quarterly or yearly by the company as your share of their profits as a shareholder.

If you do not wish to research yourself and invest, you can also become a passive investor and use someone else's expertise.

However, being an active investor gives you much more control and the possibility of earning higher returns. While there is definitely a lot of work involved in learning how to analyze a stock and identify undervalued companies, the reward, in the end, will definitely be worth it.