Regions Wealth Podcast

Episode 40: Building Generational Wealth: Learning How to Invest

When it comes to creating generational wealth, learning how to invest is key. While it's never too late to start, learning the basics of investing at an early age can help increase financial confidence in adulthood. In this episode of Regions Wealth Podcast, Chief Investment Officer Alan McKnight joins us to discuss the basics of investing for adults, plus how to teach your kids about investing at any age.

Sarah Fister Gale:

Welcome to Regions Wealth Podcast, the podcast that tackles life's challenges with financial experience. I'm your host, Sarah Fister Gale.

According to a recent study, 4 in 10 Americans are not invested in the stock market, with lack of knowledge being the primary deterrent. As we've discussed throughout this series, getting your kids involved at an early age can help ensure they're more financially confident as adults. But while teaching your kids to use a savings account is one thing, teaching them how to invest is quite another.

Joining me remotely is Alan McKnight. He's the Chief Investment Officer at Regions Bank. Alan, thanks for joining us today.

Alan McKnight:

Well, thanks for having me.

Sarah Fister Gale:

Thank you for being here. In this episode of Regions Wealth Podcast, we're continuing our conversation about generational wealth and discussing the basics of investing. While this episode is focused on financial literacy for children, it's *also* going to be a great primer for *adults* who'd like to learn more about investing.

We've taken some frequently asked questions from a bunch of people and developed a character who needs your help. Let's listen.

Georgia:

"Hello there my name is Georgia, and I've got three boys. My oldest, Daniel, just turned sixteen. It's a milestone year, and in my family, the tradition has always been for my parents to gift $5,000 towards the purchase of a car. However, Daniel has always been a big saver, so he asked

grandma and grandpa if they'd open an online trading account for him instead. We all love this idea — unfortunately, none of us know the first thing about investing!

Sarah Fister Gale:

So, Alan, we'll dive into the basics of investing in just a moment. But before we do, I'd like to get your thoughts on this topic. Is it beneficial for children to learn how to invest?

Alan McKnight:

It's definitely beneficial. Anything that can be imparted early on about the benefits of investing will only stand to benefit the children later on. And as our daughter's third grade teacher once told her, practice makes progress, not perfection, and the same holds true for learning how to invest.

Sarah Fister Gale:

I love that, practice makes progress. And so, what does that mean in terms of investing?

Alan McKnight:

It means that the earlier you start, the earlier you're gonna learn the terminology, understanding the basics, the more you can test into that and start to make progress in understanding what you may want to achieve later on in goals and the ability to achieve those goals. But it's never gonna be perfect. It's not as though you start and immediately, you see success and that everything necessarily unfolds the way you've planned.

Sarah Fister Gale:

So in Georgia's story, her son is 16. You talk about your daughter's third grade teacher. Is there a recommended age to start thinking about investing?

Alan McKnight:

As with so many situations with parenting, it comes down to the interest level. There's no set time or age or date when you should start to introduce the concepts. Probably most important is the ability to introduce it in a way that the child can understand and find interest in. I think we've all learned as parents, the more you try to push something that isn't comfortable or interesting, the less chance of success you'll have.

Sarah Fister Gale:

How can parents get their kids engaged, then, in these lessons?

Alan McKnight:

We find the more straightforward they can make it, the better chance of success they'll have. As we all know, it can be a difficult conversation, even for adults. So, try to sit down in a casual setting and do it in a way that hopefully is matched by their interest level. The more you push,

the less interested they may become. For me, it was my grandfather sitting down with me in a lowkey manner. Every morning, he read the newspaper and would inevitably get to the business section and the stock section. He would pull it out, show it to me, add a few anecdotes or examples of what the tickers meant, what companies they were, and try to apply something that made sense to me. As an example, he would talk about Coca-Cola and the stock, and the fact that during the Depression, when he was in college, the only individuals he knew that were able to afford cars, were those who worked at Coca-Cola. So, things like that can make it very real and interesting for a child, rather than something that is very boring, something that may not seem intuitive or logical to them. And so, taking advantage of the situation in a casual setting can be helpful. In addition now, there's so many technological resources that you can bring to bear, rather it be something on a phone, TV. The tools are really unlimited now in terms of teaching, showing, and getting those children engaged.

Sarah Fister Gale:

That's a really good point. Most of us don't look at newspapers every morning anymore, but it sounds like there's lots of apps that could replicate that same sort of experience.

Alan McKnight:

There are, and they're so much more intuitive because they've really thought of younger investors at the starting point, rather than something that may have been intuitive to a 50-year-old, a 60-year-old. They're thinking of, how do we get a 10-year-old, a 20-year-old, engaged and involved? And so, the technological capabilities there are so much higher. They have similar tools that can make that more real and involved for the child.

Sarah Fister Gale:

That's great advice. So let's pause here for a moment and listen to the second part of Georgia's question.

Georgia:

My dad did a bit of research and read a few reviews before choosing a pretty well-known online trading platform. So now that Daniel's account is funded and ready to use, he's eager to get started. He's looking to me for guidance and is asking me a ton of questions about investing. Unfortunately, I haven't the faintest idea how to help him! While I do invest a portion of my earnings, I work with an investment advisor who just sort of handles everything for me. Daniel keeps asking me about things like cryptocurrency and… well… this is embarrassing to admit, but I don't even really understand the difference between a stock and a bond, much less what a cryptocurrency is. I honestly don't know where to begin. Do you have any words of wisdom or some resources that can help me help him?"

Sarah Fister Gale:

Let's start with the basics. What is investing and how does it work?

Alan McKnight:

The goal of investing is to generate a return that's above and beyond what you might be able to generate by keeping your money in a piggy bank on your dresser or in a savings account. For a new investor, it would typically occur via an investment in either a mutual fund, a diversified portfolio of stocks, bonds, or both. Or, via single stocks or bonds. If you invest with stocks or bonds, historically, it's going to increase more than a savings account, but it can also go down more so as well. And, in fact, individual stocks can go down, even when the market is going up. It's important to understand the risks. It can up or down, and understand that there's a high risk, a potential for a potential for high reward.

Sarah Fister Gale:

So, Georgia admitted that she didn't even know the difference between a stock and a bond. So, can you explain that to us?

Alan McKnight:

I can, and it's a common question. We throw these terms around so easily and in a nonchalant manner. But for many individuals, it's not that intuitive and they may not have heard of it before. So, with stocks, you own a share of a company, versus a bond, you're loaning money to a company or a government entity. Stocks may or may not pay a dividend, which is a payment made to their shareholders, while the majority of bonds pay a fixed interest over time. Ultimately, with stocks, the goal is for the value of the share purchase to appreciate over time, while the bonds you received, fixed interest payment, plus, and this critical, the bond's principal payment, which is the dollar amount that appears on the face of the bond. This is the amount that the issuing corporation must pay to the bond holders on the date that the bond matures, comes due. We love the example of Will Rogers, who summed it up best when he talked about bonds and he said, "I'm not so much interested in return on my money as I am in the return of my money." When you invest in a stock or bond, you're investing with the expectation of different returns and different risks.

Sarah Fister Gale:

How do you know whether you should be investing in a stock or a bond? Or, should you invest in both?

Alan McKnight:

The critical element there is understanding your risk objective, understanding how much risk you're willing to bear to generate the return that is needed, and really trying to bridge the gap between what is required and what is possible. So, with a requirement, understanding what

percentage would you want in a safer investment, such as bonds, versus a higher risk investment, such as stocks. And then, working with an investment advisor to understand, what is the appropriate allocation between the two to achieve what is required. Now, if you wanna achieve what is possible, that may mean that you have to take on more risk, but at least you understand what that trade-off will be.

Sarah Fister Gale:

That's a useful explanation. So, Alan, what are some other key terms that new investors should be familiar with?

Alan McKnight:

Probably the first term that everyone hears and therefore is useful to discuss would be markets. So, the term markets is used quite a bit to refer to the stock market. Now, most folks would think about it as the US stock market, or the S&P 500. But it really means the entire global stock market. And, in fact, when you talk about markets, that also can include the bond market, so purchases of bonds, sales of bonds, the purchase and sale of commodities, like oil, gas, gold, platinum. It's a vast set of investments, so don't assume, necessarily, that it's gonna be one specific vehicle or security. The other would be a share. So, a share is a partial ownership of a company. Every shareholder owns a portion of that company, large or small. And it can be everything from a company the size of a large computer manufacturer, down to a private ownership or share in a family restaurant, for example.

Sarah Fister Gale:

Alan, what about earnings and interest rate and volatility? Are those terms that investors need to understand?

Alan McKnight:

They are, they're critical terms. And on earnings, think of it as what a company can generate via their core business. So, a company sells a product, they have certain costs associated with that product, whether it be cost of labor, the cost of the inputs that are associated with it. Ultimately, what is left over are the earnings for that company. From those earnings, the company can either pass those along to their investors via dividends, or they can keep them and reinvest them in the business. But the trajectory of those earnings are really what the market is most interested in. So, are those earnings going up? Are they going down? Are they stable? How can we quantify what they may be in the future?

Interest rates are another key term. Interest rates characterize what a company or a country has to pay as a fixed amount to their bond holders. So, in the example of a treasury bond, the US government has to pay a certain amount of money to be able to borrow money, and investors are willing to pay that certain amount or receive that certain amount from the US government. And then, finally, volatility. So, how an asset moves up or down over time,

whether that's a stock or a bond, or gold, the market wants to know, how much is it going to go up? How much could it go down? And the volatility is the way in which that asset moves over time.

Sarah Fister Gale:

So, Georgia also talked about cryptocurrency, and that ironically is something that my kids have been asking about. In layman's terms, what is cryptocurrency and how does investing in crypto differ from traditional investing?

Alan McKnight:

It's a great question and one that we hear a lot, including one that I hear from my own children. So, at its core, and for this discussion, it's a store of value, similar to owning a dollar or a euro, or a yen. You're merely utilizing a different type of currency for purchases of goods or services. It provides a level of independence from those currencies, though, because it's not associated with any one country. What we recommend is that investors really understand the benefits and the risks of owning that type of currency. And since they're so new, they're easy to create, and therefore, there are a host of different types of cryptocurrencies, all that have various nuances and associations. And therefore, we really try to focus on those that have the highest number of dollars invested in them, as well as the most liquidity, or the ability to actually review, what are they worth and what can you actually do with them. The challenge with cryptocurrencies today is that it all depends on who you ask what they are and what they can achieve, and it's a bit of the wild west in terms of how they're utilized. So, as we sit here today and think about cryptocurrencies, and the hosts of different kinds of cryptocurrencies, we counsel that understanding what they're meant to do, understanding their liquidity features, and even understanding what you had hoped to achieve by holding them, is the most important focus for any investor.

Sarah Fister Gale:

One of the things that's come up in recent discussions around cryptocurrency is non-fungible tokens. Can you explain how that is different from investing in cryptocurrency? And is that something investors should be paying attention to?

Alan McKnight:

They should definitely be paying attention. And I think for NFTs, or non-fungible tokens, the key consideration is, what is the asset really worth? And would you own that asset in a different sphere? So, as an example, whether that be a painting or a trading card, understanding what it means exactly and whether or not you wanna own those. I think the challenge for us is ascribing a value to NFTs, because at the end of the day, it's only worth as much as someone else would purchase it from you for, and determining that amount is very difficult today.

Sarah Fister Gale:

So, it's like a digital collectible.

Alan McKnight:

It is, exactly. And therefore, like every collectible, it's only as valuable as what it can trade for on any given market on any given day. It doesn't mean that there's not value there, but with the limited history of NFTs, it's harder to understand, what will it be worth a year from now or five years from now, 10 years from now, versus, say, common held beliefs around what a stock may be worth or what a bond may be worth.

Sarah Fister Gale:

That's a really helpful way of explaining it, Alan. We've already covered *a lot*, so let's pause for a moment and listen to the last portion of Georgia's story.

GEORGIA:
"Of course, my other two boys want to do everything their big brother is doing, so now they're all excited about investing. Jordan is 9 and Braxton is 11. I want to support their interest, but it just feels WAY too early for them to start actually investing. What can I do to educate them and keep them excited about money management?"

Sarah Fister Gale:

Is there any way that parents can teach their children how to invest at an early age? Maybe even before they have money to invest?

Alan McKnight:

They can, and we like to break it down into a few different categories. So, childhood years, your teenage years, college years, and then finally, new graduates. In the childhood years, it's all about initiating the idea of investing, starting with chores or small jobs where the child can earn money and start to appreciate the process of earning money, and then growing it over time. For example, if you earn $10 babysitting, if I were to save that money, to invest that money, could I actually have $11 at year end? It's the idea of compound interest with the idea that you can grow your wealth over time. Your dollars can actually grow without you having to actually put more in, and it's to your benefit. So, it's framing up the idea of earning, saving, and investing for the childhood years.

Sarah Fister Gale:

I love that. And what about the teenage years?

Alan McKnight:

As you transition into the teenage years, it's more about technology, education. Not inundating the children with information, but really showcasing how they can create an

investment portfolio, the ways that saving dollars can benefit them over the long-term and impart wealth to them via a part-time job or birthday money being applied to an investment account, and that they can continue to grow that wealth over time, even if they're not adding more money in. That's a critical component. And as I mentioned earlier, technology is such a huge advantage now because there are a host of different products that can both showcase what an investor could do with money, so model it out, show and forecast what the money could earn, which is always important for a teenager. And then, finally, understanding whether via family investment advisor or via self-directed platforms, how they could achieve those goals.

As you transition into college, the child will hopefully have a budget, understand that they now have ownership over the money. So, therefore, they will need to really focus on, what can savings do, and earnings. It's not just this esoteric idea of what earning and saving will do. It's very real and palpable as they have to spend money in their college years. How can they offset that with savings and investing, and then over time, understanding what independence in that regard can do for you, with regard to post-grad life and the knowledge and understanding of how to invest. It's much more real during the college years, but we also think it's the most critical time period because it will then allow them to bridge the gap into becoming a graduate, where one of the greatest challenges is trying to manage a budget on your own. There's not a safety net any longer. So, they're responsible for their budget, for spending, for saving. They're inundated with new ideas and topics if they're at a job, so what is a 401K? What is an IRA? How do I fund it? How much do I fund?

And this is really the opportunity to get them on the right path if they haven't done as much during the childhood, teenage, and college years. The new graduate really needs to spend time and understand how they could ultimately reach their goals, because it may seem like a distant future of retirement at age 65 or 70, but it's very real. And what we've found, with a host of different academic studies, is that the earlier they start the investing process, the higher probability of success in retirement, however many years later that may be.

Sarah Fister Gale:

I like the way you broke that down. So, Alan, when you think about new investors, whether they're teenagers or new grads, what are some common mistakes they make?

Alan McKnight:

One of the primary mistakes that new investors make is putting all of their eggs in one basket, or in this case, all of their money in one basket. So, they've heard from someone and they've read something, they've seen something on a host of social media platforms, and they think, wow, this is a real quick and easy way to make money, I can't lose, and therefore, I'm gonna put all of my money in it because I want the excitement, as well as the reward of what is perceived to be very low-risk. But sadly, in many cases, they're high risks. They put it all in one thing, and then it goes down. Well, once it's gone down, in many cases, they don't want to,

then, try it again. They feel like they've been burned by it, they feel like it was, in some way, stacked against them. So, if you can start by showcasing the value of a diversified portfolio, of having a host of different assets in the portfolio about understanding risk tolerance, hopefully there will be a counter balance to the idea of putting all of your money on one single investment and hoping that it goes up. Investors don't think enough about the broader macro, sort of, investing principles. They get caught up in the shiny and new, and in many cases, that then sours them on investing over the longer term.

Sarah Fister Gale:

So, Alan, in episode 17 of this podcast, you and I talked a lot about the importance of determining risk tolerance. How do you do that when you're so young?

Alan McKnight:

It is every bit as important to understand risk tolerance at an early age. Albeit, it can be a little bit more of a difficult conversation because it's not necessarily as clear cut for an early and individual investor. So, starting the risk tolerance conversation comes down to, how much risk are you willing to bear? And understanding that regardless of the goal that you'd like to achieve, you will have to take on a modicum of risk to achieve that goal. And the educational aspect of that is understanding that you can lose money. There's certain investments where that's a very, very low likelihood, but there are others where it's a high likelihood, and how do you build out a diversified portfolio that hopefully maps your risk tolerance and understanding of risk with the portfolio that you're creating.

The critical element in discussing a diversified portfolio is understanding that certain types of securities, whether they be bonds, stocks, or even cash, help to smooth the path and help to ensure that sometimes, certain aspects of a portfolio may go up and sometimes they may go down. And so, you need to have a ballast in those portfolios to ensure that over the long term, you're able to minimize or mitigate the long-term risks associated with those investments. So, as an example, a classic risk tolerance would have many investors at 60% stocks and 40% bonds. That is primarily achieved via the returns that we've seen over history. So, going back over 100 years and looking at, what should stocks generate, what should bonds generate, and how much risk do they each have in a portfolio.

Sarah Fister Gale:

So, this feels like a lot of information, especially for someone who is managing their own investing. Can you explain, how does self-directed investing differ from, say, working with an investment advisor?

Alan McKnight:

Certainly. With self-directed investing, you're deciding what to invest in. You've made the determination of how much risk you wanna take on, the type of security you would like to purchase, and you're directing that decision. You're tasked with knowing how to position yourself. Conversely, an investment advisor will work with you to set risk tolerance, objectives, and build a portfolio with you and make decisions around where the portfolio should be positioned. The best example, or how to think about the differences, would be one of, if you're going on a trip and you've decided that you're going to pick out the flight, pick out the hotel, pick out the route in which you're going to go, the restaurants you're gonna go to, you do that all on your own. It's self-directed in making that determination. So, if you're in South Africa, you will determine exactly what you're gonna do in those places, and then hope for the best. Counter that to having a travel guide, where you would like someone to help you build out an itinerary, understand where you should be staying, understand the risks associated with that, and the path that you would like to take to experience that destination.

Sarah Fister Gale:

That is a great way of explaining the difference. So Alan, as you know, we like to ask for some key takeaways at the end of each episode. What are some key takeaways for parents hoping to teach their children the fundamentals of investing?

Alan McKnight:

The three key takeaways for us would be, one, start early and invest often. There is really no downside to starting the process early, to having the conversation with your children, to applying a certain level of rigor to that. And in terms of having regular discussions, showcasing what it may mean, that doesn't mean that every application is the same. So, certain children may have a real interest in it early on, others, it may take a little bit longer. But just keep applying the same process, adopting the same methodology, of talking about it, initiating them, and you'll have some success over time.

The second is have a goal in mind and understand what you're trying to achieve. So, if you go into it and think, I'm going to have each of my children have the same level of interest and the same level of success right out of the gate, you're probably gonna be disappointed. Similarly, if you explain to your children that they have the ability to make an unbelievable amount of money and this is going to change their lives before they even go to college, you're probably going to disappoint them. So, focus on a goal, similar what you would if you want them to be able to make the soccer team or get an A in school, and then work each week to achieve on that, to discuss it. And again, practice makes progress, not perfection.

And then, finally, make it interesting for your kids. So, adopt technologies, use anecdotes and examples, be a part of it with them. Show small goals, even, in the short-term, whether that be on savings or you paying interest on certain jobs or chores, to keep them involved in the process. The surest sign that it's not going well is that you just don't ever talk about it, they're not interested in it, and therefore, it just dies on the vine. So, with those three takeaways, both,

you will have success in the conversations with your children, and hopefully, your children will have success as an early investor.

Sarah Fister Gale:

Thank you so much. That was Alan McKnight, Chief Investment Officer for Regions Bank. Alan, you've given us plenty of great information today.

Alan McKnight:

Well, thank you so much for having me. It's always a pleasure.

Sarah Fister Gale:

And thank *you* for joining us today. If you're a parent looking for more financial education resources, be sure to check out past episodes of this podcast series. In episodes 37 and 38, we covered tips for creating and maintaining generational wealth and in both episodes, our guests shared some great tips for parents. You can check those out at regions.com/wealthpodcast, or on your favorite podcast platform.

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