New Investors: Do This Before Investing in Your 1st Stock!

Description

Did you just get some birthday money or your first paycheque? It's exciting to finally have some money in your hands. And good for you for thinking of investing your money instead of spending it.

First thing's first, though. Make sure you have your financial house in order before you start investing. This way, you won't be stressed about the money you have invested, which is meant for long-term financial goals.

Build an emergency fund

If you're a student and still living at home, you might be tempted to skip this step. However, it's good practice to have an emergency fund. You don't want to be caught off guard when an emergency arises!

For example, having an emergency fund helped relieve financial stress for those who lost their jobs temporarily during the pandemic.

Financial experts recommend having at least three to six months of living expenses as one's emergency fund. Living expenses include food, rent/mortgage payments, utilities (internet, phone, hydro, gas, electricity, etc.), transportation, etc.

After building an emergency fund, highly consider paying off high-interest debt.

Pay off high-interest debt

High-interest debt costs more. At the top of the debt pyramid is likely your credit cards. You're paying higher interest rates on this debt. So, it makes good sense to pay them off first.

Credit cards charge interest rates of about 20% on purchases and an even higher rate on cash advances. I'll have you know that the long-term average stock market returns don't exceed 10%. So, it's like doubling your returns by paying off your credit cards instead of using that money to invest in the stock market.

Always have enough money in your chequing account to pay off your credit cards every month. Sticking to this habit will save you thousands of dollars in interest down the road!

Once you've paid off your high-interest debt, you might want to grow your funds.

Grow your investment capital

As a student or someone who just started working, you will have tonnes of things to spend money on. These things compete for your money. You might not have as much to save and invest as you think.

If you start with individual stocks, your portfolio will be highly concentrated in a few stocks. You might not be comfortable with being exposed to the risk of most of your money concentrated in a few stocks.

Additionally, learning and managing a stock portfolio takes time and effort, too. You might rather spend your free time doing something else. If so, you might be better off starting out investing in low-maintenance, low-cost funds instead of individual stocks.

Stocks cost anywhere from $5-10 per trade. Once your investment portfolio grows "large enough," if you're still interested, you can consider transitioning to a stock portfolio.

You need at least 10 stocks to build a diversified stock portfolio. Let's say you put a minimum of $1,000 in each stock, you'd need at least $10,000 for your stock portfolio.

The Foolish takeaway

Before you start investing your money, make sure you have built an emergency fund, paid off high-interest debt, and grown your investment capital.

The financial markets are not meant for making quick bucks (though they're sometimes portrayed as such). Instead, they're meant for long-term investment with an investment horizon of ideally *at least* five years.

Long-term stock performance is driven by underlying businesses. Rome wasn't built in one day. Neither are businesses that continue to change. By holding shares of a stock, you have confidence that the underlying business has bright prospects that will take time to realize.

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