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The ABCs of investing

How to teach your kids about the stock market

By ABBY COHN, *Special to the Mercury News*

Your 12-year-old daughter is making a tidy bundle on babysitting jobs, but she blows it each weekend on clothes and CDs. (That's CDs as in compact discs—not certificates of deposit.)

You'd like to teach her the virtues of investing, but you don't feel qualified to pitch the concepts to your budding consumer. Worse, you smell a battle in the works.

Relax. There are plenty of strategies for launching youngsters into the world of saving and investing that won't strip them of all their spending money or spur fights. A few hundred dollars, some research and a little guidance from parents can transform adolescents into gung-ho Wall Street investors.

"It should be fun for kids," says Janet Bodnar, author of the "Ask Dr. Tightwad" syndicated financial column and a senior editor at Kiplinger's Personal Finance Magazine. "You don't want to get too serious. You don't want to create Peter Lynches out of your 6-year-old."

Still, the lessons learned will be invaluable and lifelong. B. Douglas Bernheim, an economics professor at Stanford University, says youngsters who are taught basic financial concepts are "more comfortable" and "make better decisions" with their money as adults. He's found that people who got financial education in high school saved more and by their 40s were ultimately wealthier, by the equivalent of a

year's earnings, than those who didn't.

Depending upon the child, ages 10 through 12 can be an ideal time to introduce kids to investing. Many financial planners and child finance experts recommend the stock market as one good place to teach children with just a couple of hundred dollars to invest. A stock is more tangible to youngsters than a mutual fund because it represents a single company to research and follow. For more serious investment as your child gets older and has more money, the pros generally suggest seeking the diversification of mutual funds.

Teach your children well

Before jumping in, talk with your children about the stock market, how companies work and what's involved in becoming an owner. "If they don't understand there's a fundamental business underlying the stock, then it's just gambling," says venture capitalist Tim Draper of Redwood City, who has created a weeklong class he's taught in some Peninsula elementary schools in which students team up to design, make and sell friendship bracelets. Classmates have the opportunity to "invest" in the enterprise.

Lessons can be as simple or sophisticated as you want. A stop at the bank can lead to a review of savings plans like passbook accounts and CDs and what their

interest rates would pay on a \$1,000 deposit, suggests Jane Lopus, director of the Center for Economic Education at California State University, Hayward. Talk about favorite breakfast cereals and who makes them the next time you and your child go to the supermarket. Or stop by a brokerage to watch the tape—and meet with your broker.

Teach your child how to read the stock page in the newspaper. "Dr. Tightwad's Money-Smart Kids" by Bodnar (Kiplinger Books, \$15) can give you a hand explaining the symbols. Then—without putting up any real money—start tracking some of the companies that have sparked your child's curiosity.

"Start with something the child identifies with," recommends Stanford Young, president of Financial Clarity Inc. in Palo Alto. "Maybe they're into in-line skates." You and your child can research who manufactures the skates your child likes best and follow the company's stock.

Financial conversations should stay upbeat, urges Elizabeth Schiever, director of high school financial planning for the National Endowment for Financial Education. Frequently, money talk at home is either taboo or tense. "So often, what we pick up about money is the negative, where we can't pay the bills and so on," she says. "Sometimes when we're teaching, we're not teaching the positives at home."

Play with investments

You might want to play your own version of the popular Stock Market Game, a 10-week program where students in grades 4-12 compete to see who can make the most money when they invest an imaginary \$100,000. While the game is designed for use in schools—about 15,000 students in Northern California participate—families can play over the Internet as a non-competing adult team. The Web site is at <http://www.smg2000.org>; last year's registration fee was \$40. Teachers interested in learning about the game can contact the Center for Economic Education at Cal State Hayward.

"This gets the kids interested," says Mike Zochetti, an economics teacher who has played the game for 12 years with students at Independence High School in San Jose. He's watched students who knew nothing about stocks rush into class every morning to check the stock pages to see if their investments have gone up or taken a dive. "There's no way you could get as much mileage by reading a book," he says.

On the Internet, Santa Cruz County teacher Jory Post has developed a program called "Taking Stock" that teaches students, among other things, about the stock page, profit and loss and corporate research. It's at www.santacruz.k12.ca.us/vft.

To avoid broker fees that would take a big bite out of young investment dollars, Draper set up a "cyber market" for three of his kids, ages 13, 11 and 8. They pick stocks, pay their dad the going share cost and track prices with an online computer program—all without ever actually purchasing the stock. When they're ready to sell, Draper shells out the new share price.

After taking a hit on some penny stocks that lost money, 11-year-old Adam Draper figures he's made about \$15 or \$20 on his \$200 investment over the last three or four years. "This is really fun," says Adam, whose current investments include CKS, Cell Net, GT Bicycles Inc. and Marvel. "I like watching the stocks just go up and down."

Become a real shareholder

Taking the actual plunge into the stock market probably requires a few hundred dollars—and a little help from parents.

Consider giving your child some stock as a birthday or holiday present. For her nephew's bar mitzvah, Barbara Steinmetz, a financial planner in Burlingame, gave stock in Eli Lilly & Co., where her husband works. Her nephew now is considering putting a chunk of his gift money into Coca-Cola.

Children may be more vested in the process if they're using their own money. But teens also can be leery about taking the first step, says Duane Moyer, division director of the National Foundation for Teaching Entrepreneurship. He recently talked about the stock market with students at Woodside High School who have started their own businesses as part of an NFTE program. The students were offered a chance to invest in one or more shares of Wendy's fast-food restaurant chain. Afterward, 18-year-old Richard Martinez expressed interest but added, "I don't want to jump into something I don't know." He's made about \$300 this year in the program by selling rings and "I don't want to lose money."

Picking a stock starts with a basic interest in the product, but shouldn't end there. The pros recommend that children choose companies they understand and like. Young investors also should research the product.

When Steinmetz's nephew said he liked Coca-Cola and wanted to buy it, she told him, "That's just the starting point for the research. You have to make sure there are other people who think it's a good thing." She encouraged him to check out the company on the Internet and in guides like Value Line, and follow news reports about the business. Kids also should be encouraged to think about factors—such as health or environmental concerns—that could bolster or hurt a product.

Solid, blue-chip companies with kid appeal make the best investments for youngsters, the pros say. While tempting because of their low

cost, experts interviewed strongly urged against buying penny stocks. "That's not investing, that's gambling," Bodnar says.

Bodnar suggests either picking a discount broker or buying a no-load fund so limited investment dollars won't be eaten up by commission fees. Parents also may want to pick up commission charges on their children's investments. Since children can't own the stocks directly, parents need to set up a custodial account for them. Kids pay no taxes on the first \$650 of earnings from their assets.

Kid-friendly brokers

In the May issue of Kiplinger's, Bodnar listed Kennedy, Cabot & Co. in an "honor roll" of kid-friendly brokers. The firm (1-800-252-0090) charges \$20 commission plus a \$3 service fee for any trade of 1 to 99 shares. There's no minimum investment. Also mentioned was Charles Schwab (1-800-435-4000), which has a minimum \$39 transaction fee. It's discounted 20 percent if the trade is placed through the Internet or 10 percent by an automated phone call. Schwab's custodial accounts have a \$500 minimum.

Your regular broker may cut fees if you explain that you're starting a portfolio for your kids, says Carey Cook, a broker with Sutro & Co. in San Francisco.

A growing number of companies offer their stocks directly, with varying minimums to invest. Many charge enrollment or service fees. The lowest minimum that Bodnar discovered was \$50 from Bob Evans Farms. McDonald's has a \$1,000 minimum or a \$100 automatic monthly investment; Mattel's minimum is \$500. Disney plans to start a no-load program later this year.

Though not a prime consideration in picking a stock, some kid-friendly companies offer perks that are attractive to children. Jan Brock, a broker at Dean Witter Reynolds Inc. in San Jose, had one small client who got excited because Wrigley's sent free gum to its stockholders.

For children interested in mutual funds, look for those with a

relatively low minimum to start combined with a solid history of returns. Some funds, such as the Stein Roe Young Investor (1-800-338-2550), are targeted for children. The Young Investor supplies educational material and a newsletter; its holdings include companies like McDonald's, Disney and Mattel. It has a \$1,000 minimum that is dropped to \$100 if a \$50 monthly automatic investment plan is established.

Keep expectations low

Neither you nor your child should go into the market with visions of sizzling returns.

San Francisco financial planner

Norman Boone and others say that mistakes often are a better learning tool than blazing success stories. "Whether you're 13 or 30, you're going to make some mistakes," Boone says. "If you go in expecting 20 percent per year, you'll be disappointed 9 out of 10 years." Though the stock market probably will do better over time than putting money in a savings account, "it's equally important to understand the joys and frustrations of investing," he says.

Young urges parents to regularly review the ups and downs of the investment. "An investment is never a one-time thing," he says. "It's nothing without ongoing

monitoring and decision making."

He suggests that parents and kids sit down for the first few months to review each statement line by line. "If you do that, you can actually figure it out," he says. Later, family reviews can be stretched out to a quarterly basis.

Several years into his cyber-market investing, Adam Draper checks his stocks monthly, picks companies that make products he likes or are owned by people he's met. Says his dad: "He's been ahead of a lot of the curves."

Adam thinks he's also figured out the right time to sell a stock—"once it's gone up a lot and it's fading away, little by little." □

Where to read more about it

"Dr. Tightwad's Money-Smart Kids" by Janet Bodnar
(Kiplinger Books, \$15)

"Money Doesn't Grow on Trees" by Neale S. Godfrey
and Carolina Edwards (Simon & Schuster, \$11)

How to get your kids to save or invest their money

Here are some suggested guidelines for encouraging youngsters to channel spending dollars into savings or investments:

■ Elizabeth Schiever of the National Endowment for Financial Education recommends a 70-20-10 rule. Let your children spend 70 percent of their money. Have them save 20 percent for bigger ticket items that they can't afford immediately, such as a bike or stereo. The remaining 10 percent is earmarked for long-term investments.

"It's important that there's some self-gratification," she says. At the same time, her program encourages students to view saving as a way to "pay yourself first." Children also should be taught the power of

investing over time. (She says students are amazed by a formula showing what happens when someone puts aside \$2,000 annually at 9 percent interest for nine years starting at age 22. The original \$18,000 investment grows to more than a half million dollars at age 65.)

■ Family finance author Neale S. Godfrey proposes a jar system where 10 percent of earnings goes to charity. The remaining money is evenly divided into three jars designated for instant cash for spending, medium savings for larger purchases and long-term savings.

■ San Francisco financial planner Norman Boone says some of his friends require their kids to

save half their allowance with the belief that "a little deferred gratification pays off."

■ Stanford Young of Financial Clarity Inc. recommends using gift money for investments. "I think that makes a logical model for the future," he says. "Most people view salary as spending money (and) bonuses, gifts as savings money."

■ Financial planner Barbara Steinmetz says parents could match each of their children's investment dollars with one of their own. She likens it to a 401(k) plan for kids, saying "if the same thing works for adults, why doesn't it work if the kid saves \$5 a week, the parent matches the money?"

—Abby Cohn