Choosing the Trade-Off

Compare how investments offer returns and carry risks.

GE.6.6 "Compare and contrast different types of financial investments."

NAME _____ DATE _____

1 READ AND MARK

Read it twice

YOUR JOB Underline details about possible returns, circle details about risks, and number the four main investment types as they first appear so you can compare their trade-offs.

Four Booths at the Career Fair

1 At a school career fair, students imagine investing money they will not need for several years. One booth explains shares of stock, which represent ownership in a company. A shareholder may gain if the share price rises, and some companies pay dividends from profits. But the price can fall sharply, and dividends are not promised. Another booth describes bonds. Buying a bond means lending money to a government or company. The issuer promises interest and repayment on a stated date, but it might fail to pay. If a bond is sold early, its market price can change.

2 A third booth offers mutual funds. Investors pool their money in a fund that holds a collection of assets, such as stocks or bonds. A stock fund can spread money among many companies, so one company's decline may have less effect than it would on a single-company investment. Still, a broad market drop can lower the fund's value. Fund investors pay fees, which reduce their returns. The fund's holdings matter: a bond fund and a stock fund can face different risks. Unlike owning one bond until its repayment date, a bond fund does not promise to return your original investment on a set date.

3 At the last booth, a bank offers certificates of deposit, or CDs. A CD generally pays a stated interest rate if the money stays deposited for an agreed term. At an insured bank, deposits are protected up to legal insurance limits, unlike stocks, bonds, and mutual funds. Taking money out before the term ends can trigger a penalty. Students notice a trade-off: a CD offers more predictable payments than a stock fund, but the fund offers a chance of higher returns along with a greater chance of loss. The best fit depends on when the money is needed and how much uncertainty the investor can bear.

2 ANSWER WITH EVIDENCE

Use the passage

1. How might a stockholder and a bondholder earn money in different ways, and what risk do both face?

2. How does a stock fund change the risk of owning shares in just one company, and what risk remains?

3. How does the stated repayment date of one bond differ from what a bond fund provides?

4. Compared with a stock fund, what makes an insured bank CD more predictable, and what trade-off might an investor face?

3 YOUR TURN

Your own words

Invent two investors with different timelines and tolerance for loss. For each, choose one investment type from the passage and explain why it fits better than a different type in four to six sentences total.

Choosing the Trade-Off

PART 1 · READ AND MARK

Underline details about possible returns, circle details about risks, and number the four main investment types as they first appear so you can compare their trade-offs. Accept any marking that follows this job and points at the right text.

PART 2 · ANSWERS

#	QUESTION	ANSWER
1	How might a stockholder and a bondholder earn money in different ways, and what risk do both face?	**A stockholder may gain from a rising share price or dividends; a bondholder is promised interest. Both can lose money: a stock price can fall, while a bond issuer might fail to pay or the bond's resale price might fall.**
2	How does a stock fund change the risk of owning shares in just one company, and what risk remains?	**A stock fund spreads money among companies, reducing the effect of one company's decline. A broad market drop can still lower the fund's value.**
3	How does the stated repayment date of one bond differ from what a bond fund provides?	**A bond issuer promises repayment on a stated date, though it might fail to pay. A bond fund does not promise to return the investor's original money on a set date.**
4	Compared with a stock fund, what makes an insured bank CD more predictable, and what trade-off might an investor face?	**A CD generally pays a stated rate, and eligible deposits at an insured bank are protected up to legal limits. A stock fund offers a chance of higher returns but a greater chance of loss; early CD withdrawal can also bring a penalty.**

PART 3 · YOUR TURN (SAMPLE ANSWER)

Maya needs her savings in two years and cannot afford a loss. She chooses a two-year CD at an insured bank because its stated rate and deposit protection make it more predictable than a stock fund. Leo will not need his money for fifteen years and can accept price swings. He chooses a stock mutual fund rather than one company's stock because the fund spreads his money among companies. Leo knows a market decline could still reduce the fund's value.

Accept different investment choices when each comparison accurately connects the investor's timeline and tolerance for loss to returns or risks described in the passage. CD insurance applies only to eligible deposits within legal limits.