

BRAIN WORKS ACADEMY

BFN 203 Summary

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Here is a more detailed, step-by-step summary of Module 1 from BFN 203 Basic Financial Literacy.

Everything is broken down into simple language with bolded headings and subtopics so even a complete beginner can follow along.

MODULE 1: THE BASICS OF INVESTING AND CREATING WEALTH

This module explains what investment means, how to start a business, why you should spread your money around, and smart strategies to protect and grow your money in the stock market.

UNIT 1: MEANING, NATURE, AND TYPES OF INVESTMENT

What Is Investment?

- Simple definition: Using your money to buy something that will give you more money in the future.
- Economist's view: Saving money now (delayed consumption) so you can use it later to earn more.
- Finance view: Buying things like stocks, bonds, property, or gold so they can grow in value or give you regular income.

Main Characteristics (Features) of Investment

1. Earnings (Returns)

- The main reason people invest – to make money.
- Earnings can come as interest, dividends, or capital gains (selling at a higher price than you bought).
- Formula: $\text{Earnings} = \text{Current Price} - \text{Original Price}$

2. Risk of Loss

- There is always a chance you could lose some or all of your money.
- Low-risk examples: Government bonds, Treasury bills (called "gilt-edged" securities).
- High-risk examples: Stocks of small companies, new businesses.

3. Safety of Investment

- How protected your money is.
- Factors that can hurt safety: bad management, fraud, economic downturn, inflation, unstable government policies.

4. Liquidity

- How fast and easily you can turn an investment into cash.
- Very liquid: Treasury bills, government securities.

- Less liquid: Real estate (takes time to sell a house).

Types of Investment

A. Ownership Investment (You own the asset)

- Stocks (Shares): You buy a small piece of a company.
- Derivatives: Value depends on another asset (e.g., options, futures).
- Business Ventures: Starting or buying a business.
- Real Estate: Buying land or buildings to rent or sell later.
 - Note: Your own home is not an investment unless it generates income.
- Precious Metals & Objects: Gold, diamonds, rare paintings – you hope their value goes up.

B. Lending Investment (You lend money to someone)

- You give money to a company or government, and they pay you interest.
- Examples: Bonds, debentures.
- Lower risk than ownership investment.
- If the company goes bankrupt, lenders are paid back before owners.

C. Marketable Security Investment (Easily sold investments)

- Treasury Bills (T-bills):
 - Short-term government debt (less than 1 year).
 - You buy at a discount, get full value at maturity – the difference is your profit.
- Treasury Securities:
 - Notes (1–10 years), Bonds (10+ years).
- Government Agency Securities: Issued by government agencies, very safe.

UNIT 2: VENTURE CREATION (STARTING A BUSINESS)

What Is Venture Creation?

- Turning a new idea or technology into a real business that can succeed and attract investors.
- It's like a manufacturing process: take an idea, add effort and money, and create a product people want.

The Process of Venture Creation (Different Models)

Deakins Model (5 Stages)

1. Idea Formulation – Come up with a business idea (get input from family, friends, experts).

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2. Opportunity Recognition – See a real chance to make money.
3. Pre-start Planning – Research the market, find money, build a team, write a business plan.
4. Establishment & Launch – Start the business, deal with legal issues, begin selling.
5. Post-Entry Development – Build credibility, find customers, learn from mistakes.

Hult Model (5 Phases)

1. Idea Phase – The beginning, even if the idea is not fully developed.
2. Test & Persuasion – Share the idea with friends and family to get feedback.
3. Preparation – Do calculations, budgets, market analysis.
4. Start-up – The “trigger event” that makes you finally launch.
5. Ongoing Business – Keep running, growing, and seeking advice.

Bhave Model (7 Stages)

1. Opportunity Recognition – Spot the business chance.
2. Technology Set-Up – Buy and install the tools needed to produce.
3. Organization Stage – Set up management structure.
4. Product Creation – Actually make the product.
5. Exchange Stage – Connect with customers.
6. Customer Feedback – Learn what customers think.
7. Continuous Improvement – Adjust based on feedback.

Role of the Entrepreneur (What the Business Founder Does)

1. Idea Generation – Come up with and evaluate business ideas.
2. Develop a Business Plan – Write a detailed roadmap.
3. Generate Resources – Find money, people, and materials.
4. Establish Management – Hire the right people and set up structure.
5. Strategic Planning – Plan for future growth (e.g., expansion, selling shares to the public).

UNIT 3: DIVERSIFICATION AS A BASIS FOR INVESTMENT PORTFOLIO

What Is Diversification?

- Simple saying: “Don’t put all your eggs in one basket.”
- Spread your money across different types of investments so if one fails, others may succeed.

Two Types of Risk

Risk Type What It Is Can Diversification Help?

Systematic Risk Market-wide risk (inflation, war, interest rates) **✗** No – affects everyone

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Unsystematic Risk Risk specific to one company or industry  Yes – diversification helps

How to Use Diversification

- Mix stocks, bonds, and cash.
- Mix different industries (banks, oil, tech, agriculture).
- Mix different asset classes (stocks and bonds often move in opposite directions).
- Experts say 15–20 stocks across different industries is enough for good diversification.

Advantages of Diversification

1. Risk Management – Losses in one area can be balanced by gains in another.
2. Portfolio Optimization – You can take more aggressive investments safely.

Disadvantages of Diversification

1. Diversification Double Dip – Too many investments can reduce your profits.
2. Downside Danger – In a major recession, almost everything falls together.

How to Avoid Bad Diversification

- Don't buy too many investments (keep it manageable – 20 to 30 stocks max).
- Don't buy the same type of investment (e.g., 20 bank stocks is not diversification).
- Be careful with foreign funds (they often perform poorly).
- Avoid illiquid or high-fee investments (e.g., some hedge funds and mutual funds).

UNIT 4: INVESTING WISELY USING HEDGING

What Is Hedging?

- Simple definition: Like buying insurance for your investments.
- You take an opposite position so if one investment loses money, the other gains.

How Hedging Works (Example)

- You buy ₦10,000 worth of Company A shares (expecting price to rise).
- But the industry is risky, so you short sell ₦10,000 worth of Company B shares (a weaker competitor).
- If bad news hits the industry:
 - Company A drops 50% → you lose ₦5,000.
 - Company B drops more → you gain on your short position.
 - Result: Your loss is much smaller.

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Advantages of Hedging

1. Lower risk of losing money.
2. Flexibility – Can use many types of financial instruments.
3. Less volatile than individual stocks.
4. Good for companies exposed to commodity or interest rate changes.

Disadvantages of Hedging

1. High minimum investment – Not for small investors.
2. Higher risk if done wrong – one bad move can cause huge losses.
3. Low liquidity – Can't buy or sell instantly.
4. High fees – Management fees can be very expensive.
5. Low regulation – More chance of unfair practices.
6. Mispricing – Fund managers may set unfair prices.

UNIT 5: INVESTING WISELY USING ARBITRAGE

What Is Arbitrage?

- Simple definition: Buying something cheap in one market and selling it at a higher price in another market at the same time to make a risk-free profit.

Conditions for Arbitrage

1. The same asset has different prices in different markets.
2. Two assets with the same future cash flows have different prices.
3. An asset's future price is not equal to its current price plus interest.

How Arbitrage Works (Example)

- A stock costs ₦100 on the Lagos Stock Exchange.
- The same stock costs ₦105 on the Abuja Stock Exchange.
- You buy in Lagos (₦100) and sell in Abuja (₦105) at the same time.
- Your profit: ₦5 per share (risk-free).

Important Rules

- Transactions must be simultaneous (at the same time) to avoid market risk.
- Usually done electronically with securities.
- Missing one side of the trade is called execution risk or leg risk.

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Who Can Do Arbitrage?

- Mostly banks and brokerage firms (called arbitrageurs).
- As an individual, you can hire a brokerage firm to do it for you – they take a commission.

Quick Recap of Module 1

Topic One-Sentence Summary

Investment Using money to make more money.

Risk Chance of losing money – higher risk often means higher possible reward.

Liquidity How fast you can turn an investment into cash.

Venture Creation Starting a business from an idea.

Diversification Spreading money across different investments to reduce risk.

Hedging Insurance for your investments – protects against big losses.

Arbitrage Buying low and selling high at the same time in different markets for risk-free profit.

FULL SUMMARY AVAILABLE

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