

What is Diversification?

Suggested Grade

Grades 4-5

Suggested Time

45 minutes

Teacher Background

Diversification is an investment strategy to spread investments over a variety of industries, companies, markets, and securities (e.g. stocks, bonds, mutual funds). The goal is to reduce risk by balancing the losses of one investment with the gains of another. Diversification follows the old saying: "Don't put all of your eggs in one basket."

One way to diversify is to spread investments among different companies in different industries. An industry refers to a range of companies that produce similar goods or provide similar services.

For example, PepsiCo, Inc. and the Coca Cola Company are both in the beverage industry, Apple Computer, Inc. and Dell Computer, Inc., are both in the computer hardware industry, Gap, Inc. and Abercrombie & Fitch Co. are both in the retail clothing industry.

A diversified portfolio might include shares in one company from each of those industries. The Yahoo! Finance Web site provides a complete list of possible industries.

In addition to investments in different industries and markets, diversification can be accomplished by investing in different securities. The Stock Market Game™ provides elementary school students with the opportunity to invest in all three. Students can further diversify by leaving a portion of their Cash Balance intact. The Cash Balance earns 0.75% interest throughout the course of the trading session.

Vocabulary

Diversification: An investment strategy in which you spread your investment dollars among industry sectors.

Industry: A group of companies that make the same products, i.e. pharmaceutical companies

Portfolio: A collection of investments owned by one individual or organization.

Risk: The chance of losing all or part of the value of an investment.



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Risk Tolerance: An individual investor's ability to accept loss of some or all of the money they have invested. A person's risk tolerance is based on a number of factors including age, financial stability, amount of time before the invested funds are needed for other purposes, etc.

Sector: A group of stocks, often in one industry. The performance of any single stock in a sector can be measured against the performance of the group. Pharmaceutical companies are considered in the health care sector for example.

Performance Objectives

Students will be able to:

- Create a diversified portfolio selecting stocks and mutual funds.
- Conduct Internet research on different investment options.
- Interpret company and industry charts to determine which investments to make with their SMG teams.

Materials

<https://finance.yahoo.com/screener>

Activity Sheet 1: How Diversified Are These Portfolios?

Activity Sheet 2: How Diverse is Your SMG Portfolio?

Springboard Activity

Ask your students:

1. How many of you have gone food shopping in a supermarket?
2. Which aisle do you find Kellogg Corn Flakes?
3. What about Purina cat food?
4. Would you find pickles in the meat section?
5. Where would you find bleach and dishwashing soap?

Establish that supermarkets put similar foods in the same aisle so shoppers can efficiently make purchases.

Explain to your students that just like supermarkets are organized to allow customers to purchase a wide variety of brands, industries are organized to allow investors to purchase stock from a wide range of companies.

Procedure

Write and/or state: "Having a diversified financial portfolio lessens the risk of losing money."

Begin a discussion with your students. Do they agree or disagree with this statement? Ask them to explain their answers.

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Discuss whether requiring SMG teams to purchase three different stocks as a rule is a good rule? Many SMG programs require this as a part of their local rules. Have students explain their answers. Many local SMG programs also require their teams to invest in companies from three different industries.

The desired response is it is a good rule because it is one way to diversify their portfolios so if a company's stock goes down in price, it is hoped that the price of others will remain stable or go up. Investing in different industries shields their portfolios more from great losses.

Tell your students that today they will learn how to evaluate the risk of losing money in a portfolio by analyzing the portfolio's diversity and how to create a diverse portfolio.

Novice & Apprentice Levels:

Distribute *Activity Sheet 1* to SMG teams. Guide students through the first example. Begin a guided discussion of the portfolios from the "How Diversified are these Portfolios?"

Questions to guide the discussion:

- How many different industries are represented in each portfolio?
- Can a portfolio be diversified based on the quantity of shares?
- What do you notice about the portfolios? Are any "heavy" with one particular industry?

SMG Teams should then review their current online Account Holdings pages or their planned investments.

Distribute *Activity Sheet 2*. Have each team complete side one. Have them rate on a scale from 5 to 1 the diversification of their own portfolio.

Master & Grand Master Levels:

Distribute *Activity Sheet 1* to SMG teams and begin a discussion around the theme of investment diversification.

Tell your students that many professional money managers study just one industrial sector. They become experts on the companies in their sector. Each student will study one sector to become their team's expert in the sector they choose. (If there are five students per team, each team can cover an industrial sector.)

Each student will research two stocks in their sector and present their findings to their team. They must address the problems and benefits of purchasing stock in this industry sector.

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Assessment

Student will write an analysis of the following *Sample SMG Portfolio* and advise the team on how to further protect their portfolio through diversification.

Sample SMG Portfolio

Account Holdings for Team ID : SIA_99_A261 Date : 08/07/2019

Cash Balance : \$44,982.12

TICKER	Position	Shares or \$Value	Last Trade Date	Net Cost per Share or \$100	Net Cost	Current Price per Share or \$100	Current Value	Unrealized Gains Losses	% Unrealized Gains Losses	Option
CCL	Long	200	2019-02-15	\$57.66	\$11,532.18	\$45.06	\$9,012.00	(\$2,520.18)	-21.85 %	Trade
CCL	Long	200	2019-02-15	\$57.95	\$11,590.76	\$45.06	\$9,012.00	(\$2,578.76)	-22.25 %	Trade
FLWS	Long	100	2019-02-15	\$16.93	\$1,692.76	\$19.12	\$1,912.00	\$219.24	12.95 %	Trade
FLWS	Long	100	2019-02-07	\$16.96	\$1,695.79	\$19.12	\$1,912.00	\$216.21	12.75 %	Trade
LUV	Long	100	2019-02-15	\$58.87	\$5,887.29	\$49.71	\$4,971.00	(\$916.29)	-15.56 %	Trade
LUV	Long	100	2019-02-13	\$59.04	\$5,904.46	\$49.71	\$4,971.00	(\$933.46)	-15.81 %	Trade
LYFT	Long	10	2019-04-02	\$67.67	\$676.70	\$58.70	\$587.00	(\$89.70)	-13.26 %	Trade
RMCF	Long	100	2019-02-15	\$8.84	\$883.75	\$8.96	\$896.00	\$12.25	1.39 %	Trade
RMCF	Long	100	2019-02-13	\$8.78	\$877.69	\$8.96	\$896.00	\$18.31	2.09 %	Trade
TIF	Long	100	2019-02-15	\$91.46	\$9,146.03	\$88.60	\$8,860.00	(\$286.03)	-3.13 %	Trade
TIF	Long	100	2019-02-07	\$89.63	\$8,962.74	\$88.60	\$8,860.00	(\$102.74)	-1.15 %	Trade

Total Net Cost

\$58,850.15

Total Current Value

\$51,889.00

Total Unrealized Gains Losses

(\$6,961.15)

Total % Unrealized Gains Losses

-11.83 %

Ticker	Company	Industry
CCL	Carnival Corporation	Leisure
FLWS	1-800-Flowers.com, Inc.	Specialty Retail
LUV	Software Airlines Co.	Airline
LYFT	Lyft, Inc.	Software – Application
RMCF	Rocky Mountain Chocolate Factory, Inc.	Confectioners
TIF	Tiffany & Co.	Luxury Goods

Application

Novice & Apprentice Levels:

Students review their current SMG portfolio to analyze the diversification of their holdings. They will then write a plan to diversify their portfolio, based on their findings.

Master & Grand Master Levels:

Arrange students in industry sector expert groups. Each team of experts will make a presentation to the class on why the SMG teams in the class should invest in their particular sectors.



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Enrichment Activities

Each SMG team should develop a strategy for investing and creates a tip sheet for other teams. For example, they may want to invest in companies they consider to be socially responsible corporate citizens. Or they may wish to invest in companies that are less than five years old.

Ask

If you have narrowed your investment options by deciding to follow a particular strategy, does this mean that you cannot have a diversified portfolio? Explain your answer.

Answer Keys

Activity Sheet 1: How Diversified are These Portfolios?

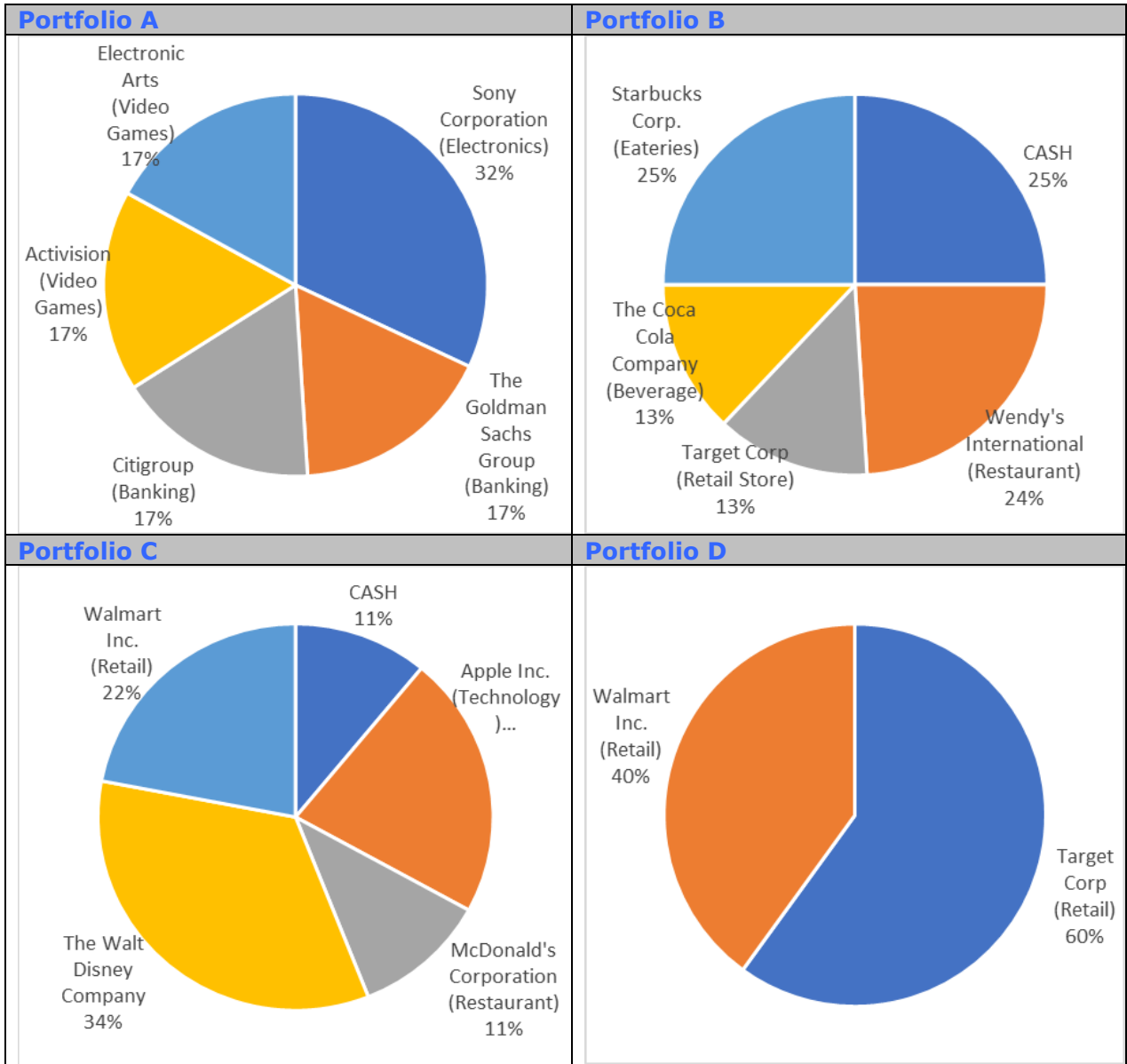
Answers may vary. The goal of the activity is for the students to debate and formulate arguments and defend their stance by interpreting visual information provided by the pie charts.



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Activity Sheet 1: How Diversified are These Portfolios?



1. Complete the statement below to make it true:

Portfolio _____ is the most diverse because _____



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2. Select one of the portfolios listed in Question 1 and diversify it. Complete the following statements to make them true:

a) Portfolio _____ is the least diversified because _____

b) To diversify Portfolio _____ I would sell _____.

Because

b) To diversify Portfolio _____ I would buy _____.

Because



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