INVEST SMART

Why Volatility Is Like Chocolate Milk

by Kaptain Kelmoore

(NAPSA)—Greetings, citizen investors. A while back, I found myself comparing notes with Socrates, the Father of Western Philosophy. The topic? How does one learn about investing?

I thought it wise to start with the question that plagues all investors: Is my glass of chocolate milk half empty or half full? The answer, dear investor, depends on what my ultimate milk-drinking goals are.

This turned my thoughts to volatility in the stock market. Depending on an investor's goals, some might view the volatility of the market as a good thing, while it can drive others to distraction.

So, in my desire to map the ABCs of Investing, I thought it best to begin with the letter "V"—for volatility.

Volatility measures the degree to which an asset's market value fluctuates and at what speed that change will occur.

Higher volatility may make conservative stock investors uncomfortable, because it implies rapid movement of stock prices. More aggressive investors may see lower levels of volatility as a drag on their portfolio's growth potential.

An investor's time horizon—how long he or she intends to hold a position in an investment—contributes to how comfortable he or she is with volatility.

For example, if investors are hoping for growth over a five-year period, they might see a volatile market as less worrisome than they would if they were hoping to buy and sell a stock in a 30-day period.

If you are an options investor, the higher the volatility of the underlying stock typically means higher premiums.

The premium is the price an investor pays for the opportunity to purchase the option and the price volatility of the underlying stock is one factor that helps to set the price of the premium.

Depending on an investor's goals, volatility can cause one person to smile and give another one sleepless nights.

This is because higher volatility means a greater chance the stock price will move in the direction that the option investor desires, in the allotted time. This movement can cause the price of the option to rise. If you are selling a call option, then you could happily receive a higher price for that sale.

All of which means that volatility can cause one investor to smile and give another one the shakes. Only a clear understanding of your investment goals will allow you to know what amount of volatility is right for you.

In good markets and in bad, knowledge and education are power. With these tools, you can take control of your financial future.

Until next time, invest wisely—and feel free to visit me online at www.kaptainkelmoore.com.

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