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***Share
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FOR
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by James Dunn



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Share Investing For Dummies®

Third Australian edition published by

Wiley Publishing Australia Pty Ltd

42 McDougall Street

Milton, Qld 4064

www.dummies.com

First edition published 2002

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National Library of Australia

Cataloguing-in-Publication data:

Author: Dunn, James, 1962–
Title: Share Investing For Dummies / James Dunn.
Edition: 3rd Australian ed.
ISBN: 978 1 74246 889 1 (pbk.)
Notes: Includes index.
Subjects: Stock exchanges — Australia.
Investments — Australia.
Stocks — Australia.
Dewey Number: 332.63220994

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Typeset by diacriTech, Chennai, India

Printed in China by

Printplus Limited

10 9 8 7 6 5 4 3 2 1

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About the Author

Over a 23-year career, James Dunn has built a reputation as one of Australia's leading investment journalists. James was founding editor of *Shares* magazine, and oversaw one of the most successful magazine launches in Australian publishing history. He has also written for *BRW*, *Personal Investor*, *The Age* and *Management Today*, and was subsequently personal investment editor at *The Australian* and editor of financial website investorweb.com.au. He writes for *The Australian*, *Insto*, *Asia Asset Management* and *The Investing Times* magazines, and the websites thebull.com.au and *SmartCompany*, and is also a sought-after speaker on investment, economic and leadership issues. On radio, James is heard daily on 3AW in Melbourne, and the nationally syndicated Newstalk ZB in New Zealand, and has a weekly commentary spot on Sky Business.

Born and raised in Ararat, western Victoria, James graduated from the University of Melbourne as Bachelor of Letters and Bachelor of Arts. He is a fellow of the Williamson Community Leadership Program, operated by Leadership Victoria.

In 1984, James won two BMWs on *Sale of the Century*. The sale of the cars financed a year of overseas travel and a substantial share portfolio, which did not survive the crash of 1987, because it was virtually all in speculative stocks. After that event, James decided on a career in financial journalism.

He has never lost his fascination with the sharemarket, and has developed a strong interest in educating people about their investments.

Dedication

Some things have not changed from the first and second editions of this book, when I wrote: This book simply would not exist without the support of and inspiration from my family. Writing a book is a selfish thing to do, and I can't thank my wife, Jane, enough for her love and support. I dedicate this book to her and to my wonderful children, Eliza and Harry, to whom I apologise for locking myself in the study and worse, hogging the computer. This is for you.

Share Investing For Dummies is also dedicated to my mother and father, who made books a part of my life from my earliest memory. At long last, I was able to put my own on the other side of the ledger, a feat they never doubted.

All of the preceding still stands in this third edition of *Share Investing For Dummies* — triply so with regard to Jane, Eliza and Harry. They've got their own computers now, but I still hog the one with all the bells and whistles.

Author's Acknowledgments

Thanks firstly to commissioning editor Rebecca Crisp and developmental editor Hannah Bennett, who drove this third edition. Also thanks enormously to the project editor who oversaw the process, Jenny Scepanovic. All three handled the delicate task of badgering and cajoling me with huge reserves of patience and understanding and I want them to know how much I appreciated that. Thanks also to Zoë Wykes at John Wiley in the US, and my technical reviewer, Clare Gichard, for her attention to detail, and to the designers and everyone else at John Wiley who have helped to make this book possible.

I also want to express my appreciation to Leeanne Bland and Jeff Olsson at ASX, Anton Tagliaferro at Investors Mutual, David Reid at Andex Charts, Kirsty Gross and Odette Monaghan at IRESS Market Technology, Rebecca Fesq at Citigroup, Daryl Guppy at Guppytraders.com, Andrew Boal at Towers Watson, Sharon Beach and Claudia Sanchez at Standard & Poor's, Alex Dunnin at Rainmaker Information, Elio D'Amato at Lincoln Indicators, Brian Phelps, Craig James and Savanth Sebastian at CommSec, Shane Oliver at AMP Capital Investors, Michael Knox at RBS Morgans, Andrew Stanley at Ralton Asset Management, Aaron Stambulich at RBS, Moghseen Jadwat at Commonwealth Bank of Australia, Phillip Gray at Morningstar Australasia, Martha Wood and Roger McIntosh at Vanguard Investments, George Boubouras at UBS Wealth Management, Gary Stone at Share Wealth Systems, Jim Taig at Seismo Australia, Peter Strachan at StockAnalysis, Kyla Morgan at the Australian Securities and Investments Commission, Jeff Bresnahan at Super Ratings, Max Newnham at Taxbiz Australia, Joe Kaleb at australianbiz.com.au, Tony McLean at Delisted.com.au, Robert Grigg at the Australian Technical Analysts Association, David Wood at Mallesons Stephen Jaques, Ron Bewley at Woodhall Investment Research, Vince Smith at Ernst & Young, Sean Dostal at Moneybags, Mark Johnston at Investment Trends, David Blake at Bioshares, Jamie Nemtsas at the Centre for Investor Education and Wayne Lee at Nasdaq OMX.

Publisher's Acknowledgments

We're proud of this book; please register your comments through our online registration form located at <http://dummies.custhelp.com>.

Some of the people who helped bring this book to market include the following:

Acquisitions Development and Editorial

Project Editor: Carolyn Beaumont,
Jenny Scepanovic

Review Editor: Zoë Wykes

Acquisitions Editors: Lesley Beaumont,
Charlotte Duff, Rebecca Crisp

Technical Reviewer: Clare Gichard

Editorial Manager: Hannah Bennett

Production

Layout and Graphics: Wiley Art Studio

Proofreader: Pam Dunne

Cartoons: Glenn Lumsden

Indexer: Karen Gillen

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Foreword

Welcome to the third edition of James Dunn's book *Share Investing For Dummies* — a book I highly recommend to any investor who wishes to be better equipped to navigate and understand the vagaries of the sharemarket.

Investing is all about employing surplus funds from income earned today to earn a rate of return and be available for use later on down the track. Investors have a choice of three main asset classes — cash/term deposits, property and shares. The concept of investing is fairly simple to understand, but what never ceases to amaze me is how many people lose sight of their objective and, through bad advice, ignorance or greed, end up losing significant amounts of their capital.

I have been investing monies in the sharemarket for over 25 years. What I've learnt is that caution is always warranted when investing in any asset class. Investing in the sharemarket can be very rewarding for the patient investor, but it can be a very easy way to lose money if you're hasty or greedy.

In the last few years we've lived through a global financial crisis (the GFC), which was caused by excessive borrowing in the previous decade. The crisis has resulted in many parts of the developed world suffering fairly major recessions. In fact, at the time of printing many governments around the world are still grappling with the after effects of the crisis.

During the GFC we saw many companies, such as Babcock & Brown, ABC Learning Centres and Centro with too much debt, run by people who over-promised and over-expanded, suffer major downturns with huge losses for the many people who backed them. On the other hand many quality, well-established and conservatively run companies such as Woolworths, Amcor and CSL have continued to post record profits and dividends to shareholders. Patient investors who wisely placed their money in the hands of well-run companies were rewarded while many who backed the headline-grabbing, overzealous companies suffered huge losses.

Once you have read this book you'll have a much better understanding of the many important aspects governing sharemarket investing and will be in a better position to make the right decisions when investing your hard-earned savings in the sharemarket.

I hope you find James' book extremely useful and that you enjoy reading it. And, of course, I wish you the best of luck in putting together a quality portfolio of shares that will reward you in the future.

Anton Tagliaferro
Founder and Investment Director
Investors Mutual Limited

Introduction

I said these important words in the first and second editions. Now I'm saying them again: Thanks for choosing *Share Investing For Dummies*. In this third edition I bring you up to date on how the Australian stock market is recovering from the massive financial storm that hit it (and all of its global peers!) between 2007 and 2009; and describe some of the wondrous investment stories that have played out on the corporate paddock since the first edition of the book was published nine years ago.

The global financial crisis (GFC) and the market slump that ensued has dented many investors' faith in shares as an investment, but despite the scary headlines and the ever-present possibility of a market fall, profitable companies continue to generate capital growth for their shareholders over the long term. The great paradox of the sharemarket is that while it is the most volatile of the asset classes, it is also the one most capable of reliably building wealth over the long term for the individual investor; I show you how in this book.

This third edition also updates advice on where to start if you're a first-time investor, the pitfalls to avoid and how to have fun (and not take too many risks) while your money goes to work for you.

Australia has grown and developed in many directions since the first edition of *Share Investing For Dummies* welcomed investors taking their first steps into the sharemarket. If you followed the first two editions, you're hopefully now managing a portfolio, researching stocks that interest you, keeping abreast of the daily market play and boosting your initial investment to something that'll at least pay for your dream holiday and at best see you comfortably through the years.

In many of the speeches that I've made around the country in 23 years as a finance journalist, I've tried to present the sharemarket as a hugely interesting institution. Because it is! And, moreover, this market, which touches every one of our lives in one way or another, doesn't have to be daunting. The sharemarket is not a hard concept to understand. When people say to me that I make the idea of buying and selling shares understandable for them, I curse whatever it was they'd been reading or hearing that made it appear the opposite.

About This Book

Share Investing For Dummies explains the sharemarket's intricacies in terms that anyone can understand. Although the sharemarket looks like a high-tech computer game with its flashing lights and scrolling letters and numbers on the trading screens, the sharemarket is actually based on a very simple concept. Companies divide their capital into tiny units called *shares*, and anyone can buy or sell these units in a free market at any time. Companies use the sharemarket to raise funds from the public and the public — meaning you — invests in the companies' shares. You invest your money in shares because you expect to get a better return in earnings than with other investments.

Most of the time the sharemarket is profitable for investors. Despite the occasional spectacular market fall, such as the great 'bear market' of 2007 to 2009 — or even the odd collapse of one of its constituent companies — the sharemarket generally plods along making money for its investors. The sharemarket revolves around money, but is also very much a human institution. The sharemarket is sometimes described as a living entity (for which we finance journalists are often mocked). Oddly, the sharemarket does have human moods because it reflects the greed or fear of its users, who are sometimes *very* human.

Greed is a powerful influence on the sharemarket, and so is fear. A saying on Wall Street suggests that these two emotions are the only influences at work on the sharemarket, and they fight a daily battle for supremacy. On a day-to-day basis, the sharemarket wavers between the two. The 2000s began with the fear of the 'tech bust', then switched firmly to greed for the middle part of the decade, only for fear to come roaring back into the spotlight in late 2007. The two will always have their days on top.

The sheer range of activities of the companies listed on the Australian Securities Exchange (formerly the Australian Stock Exchange) makes it a very interesting place — if a trading system that you can see only on computer screens all over the nation can be called a place. The number of different types of shares you can invest in is mind-boggling — perhaps there is too much choice. As an individual investor, you can't own every type of share so the solution is for you to come up with a share investment strategy.

As you will discover, of the 2,200 or so stocks listed on the Australian Securities Exchange (ASX), most investment professionals confine their activity to about one-sixth of them. Even in the 500 stocks that comprise

the All Ordinaries Index (one of the Australian sharemarket's main indicators), the last 1,900 or so don't hold much interest to Australian fund managers. This is where a self-reliant investor like you can find some undiscovered gems caught in that bind of being too small to attract the fund managers' and brokers' attention, and then remaining small because they can't get this attention. Some of the sharemarket's acorns really do become great oaks. As a self-reliant investor, with the knowledge and the time to thoroughly research potential stock purchases, you can really steal a march on the pros.

It gets harder and potentially more rewarding the deeper you delve into the sharemarket. In the bottom 1,900 or so stocks, you may find some real dogs that should not be listed (and probably won't be for very much longer), but you can also discover wonderful companies that are just about to flourish. This kind of investing is called bottom-fishing. You need to be wary and know how to back up your discoveries with solid research. At these depths of the market, you can make some very wrong moves.

You have to own some of the 2,200 stocks in order to experience the ups and downs of the sharemarket. The tools that enable you to get into the market intelligently are right here in this book. The sharemarket should be an essential part of everybody's investment strategy. Sharemarket participation in Australia is among the highest in the world, but too many people still don't understand its benefits. As the nation's population ages and superannuation grows in importance, the amount of Australians' investment assets (and retirement nest eggs) going into Australian shares is set to rise dramatically. My aim in this book is to help you understand the sharemarket so that you can control your future financial security.

How This Book Is Organised

You don't need to read this book cover to cover, but if you're a beginner in terms of the sharemarket, starting at Chapter 1 is a good way to go. In fact, I hope you do. If you're not a beginner, then each chapter is written as a self-contained read, with plenty of cross-references to other chapters scattered throughout the book. If you want to know more about a particular topic, don't hesitate to follow the cross-references and gain a broader, fuller understanding of that particular topic.

The sections that follow describe the parts in this book and what they cover.

Part I: Putting the Share in Sharemarket

This part explains how the sharemarket works, and where it fits in the economy. Here's where you find out the meaning of sharemarket terms, such as 'dividend yield' or a 'liquid stock'. I guide you through the primary and secondary markets and show you how shares are traded on the Australian Securities Exchange. You get the essentials needed for starting out in the sharemarket.

Part II: Investing Strategies for Success

Developing a strategy is the key to building an investment portfolio. This part explains how the magic of compounding and capital growth can build wealth. An investment strategy is meaningless if it doesn't take risk fully into account. You can manage risk by looking for warning signs and researching your shares. Your best weapons for protecting your portfolio are time and diversification, and I show you how to use these tools to shock-proof your portfolio as far as possible.

Part III: Buying, Buying, Sold

In this part, I get down to the basic questions about buying and selling shares — How, What, When and Why. I talk about how you choose stocks, and how you know when to buy and sell. I also take a good long look at the stockbroking industry, and the changes brought about by the internet. Part III ends with a discussion of why and how companies float — go public — on the sharemarket, and how to spot a good float from a dud.

Part IV: Doing Your Homework

Don't be put off by calculations and statistics. In time, you can get to know a lot of jargon used in analysing shares in order to make investment decisions. The professionals use price/earnings ratio, dividend yield, interest cover and many more calculations. You need to understand these terms. This part also reviews technical and fundamental analysis, two different concepts that analysts use to find out how shares perform. I take you through share trading and analysis software, and helpful resources available on the

internet. Tax questions are important whether you're investing millions or hundreds. You need to know your possible tax obligations, so find out that information here.

Part V: Shares Are for Everyone

This part shows how share investing covers many different aspects of our lives. The sharemarket plays a key role in superannuation and also allows investors to own shares in foreign companies. The more specialised areas of share derivatives — contracts for difference (CFDs), options and warrants — are increasingly opening up for the use of retail investors; I take you through the basics of using the leverage that share derivatives give you, to enhance the returns from your share portfolio. The kinds of derivatives designed for quick and easy speculation (easy in the sense of execution, not in getting it constantly right!) are covered, as are ways that you can borrow to buy shares.

Part VI: The Part of Tens

Here you find out what I think are the ten best books to read next — after you finish this one, that is! I describe the ten worst crashes in sharemarket history — so far — and take you on a tour of ten well-known investment strategies. I look at ten great Australian stocks, and end with a warning about the ten things never to do as an investor.

Glossary

This book is full of everything you could possibly want to know about investing in shares, but I kept room at the end for a jargon-buster. The world of share investing is filled with technical terms, which many professional investors and financial advisers use habitually, without even knowing they're speaking gobbledegook. Like all jargon, financial terms are actually simple once you distil them to the basics. You need a comprehensive list of financial terms and their definitions to do battle out there in the market. I've tried to include all the relevant language, and I hope I've demystified some of the most common terms that can appear so bamboozling at first.

Icons Used in This Book

Throughout this book you see friendly and useful icons to enhance your reading pleasure and highlight special kinds of information. The icons give added emphasis to the details that I think are extra important. Although the icons are self-explanatory, here are their basic messages.



Take extra special notice of this piece of information. I mean this detail is really something to store away for future use.



It's not vital that you read this stuff as you'll get a good understanding of the subject matter anyway. But it's often interesting and sometimes an entertaining diversion.



This is information I think you can profit from, so I've pre-highlighted it for you (I'm trying to save you from getting highlighter ink on the opposite page when you close the book).



Uh-oh! Wealth hazard ahead! Manoeuvre carefully around this obstacle, and mark it down in the memory bank.

Where to Go from Here

I hope that after you go through this book — if you haven't already dipped your toe in the sharemarket waters — you'll want to take the steps to starting your first portfolio of shares. If you're already an investor — great! Now you'll want to become a better-informed and more effective investor. Work out for yourself what financial security means to you, sit down with a financial adviser (or not, if you prefer; but it is advisable) and decide how shares can help you achieve your goals. Then, get started. Today!