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DUMMIES®

4TH EDITION

by Paul Mladjenovic



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About the Author

Paul Mladjenovic is a certified financial planner practitioner, writer, and public speaker. His businesses, PM Financial Services and ProsperityNetwork.net, have helped people with financial and business concerns since 1981. In 1985 he achieved his Certified Financial Planner (CFP) designation. Since 1983, Paul has taught thousands of investors through popular national seminars such as “The \$50 Wealth-BUILDER” and other financial seminars. Paul has been quoted or referenced by many media outlets, including Bloomberg, MarketWatch, Comcast, CNBC, and a variety of financial and business publications and websites. As an author, he has written the books *The Unofficial Guide to Picking Stocks* (Wiley) and *Zero-Cost Marketing* (ProsperityNetwork.net). In 2002, the first edition of *Stock Investing For Dummies* was ranked in the top 10 out of 300 books reviewed by Barron’s. In recent years, Paul accurately forecasted many economic events, including the rise of gold, the decline of the U.S. dollar, and the housing crisis. He edits the financial e-zine Prosperity Alert, available free at www.ProspersityNetwork.net. Paul’s personal website can be found at www.RavingCapitalist.com, and you can view his video commentaries at www.youtube.com/paulmlad.

Dedication

For my fantastic wife Fran, my wonderful boys Adam and Joshua, and a loving, supportive family; I thank God for you.

I also dedicate this book to the millions of investors who deserve more knowledge and information to achieve lasting prosperity.

Author's Acknowledgments

First and foremost, I offer my appreciation and gratitude to the wonderful people at Wiley. It has been a pleasure to work with such a top-notch organization that works so hard to create products that offer readers tremendous value and information. I wish all of you continued success! Wiley has some notables whom I want to single out.

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Lastly, I want to acknowledge you, the reader. Over the years, you've made the *For Dummies* books what they are today. Your devotion to these wonderful books helped build a foundation that played a big part in the creation of this book and many more yet to come. Thank you!

Publisher's Acknowledgments

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Introduction

S*tock Investing For Dummies*, 4th Edition, has been an honor for me to write. I'm grateful that I can share my thoughts, information, and experience with such a large and devoted group of readers.

I appreciate the timing of this edition because the world of investing and the U.S. economy seem as hazardous as ever. Volatility and risk do indeed play a greater role in today's stock market, and that means that patience and discipline are more important than ever. Fortunately, the investing tools, strategies, and vehicles at your beck and call give you the power to keep your portfolio growing even in today's financial battlefield.

Successful stock investing takes diligent work and knowledge, like any other meaningful pursuit. This book can definitely help you avoid the mistakes others have made and can point you in the right direction. It gives you a heads up about trends and conditions that are found in few other stock investing guides. Explore the pages of this book and find the topics that most interest you within the world of stock investing. Let me assure you that I've squeezed more than a quarter century of experience, education, and expertise between these covers. My track record is as good as (or better than) the track records of the experts who trumpet their successes. More important, I share information to avoid common mistakes (some of which I made myself!). Understanding what not to do can be just as important as figuring out what to do.

In all the years that I've counseled and educated investors, the single difference between success and failure, between gain and loss, has boiled down to two words: applied knowledge. Take this book as your first step in a lifelong learning adventure.

About This Book

The stock market has been a cornerstone of the investor's passive wealth-building program for over a century and continues in this role. The past ten years have been one huge roller-coaster ride for stock investors. Fortunes have been made and lost. With all the media attention and all the talking heads on radio and television, the investing public still didn't avoid losing trillions in a historic stock market debacle. Sadly, even the so-called experts who understand stocks didn't see the economic and geopolitical forces that

acted like a tsunami on the market. With just a little more knowledge and a few wealth-preserving techniques, more investors could have held on to their hard-earned stock market fortunes. Cheer up, though: This book gives you an early warning on those megatrends and events that will affect your stock portfolio. While other books may tell you about stocks, this book tells you about stocks and what affects them.

This book is designed to give you a realistic approach to making money in stocks. It provides the essence of sound, practical stock investing strategies and insights that have been market-tested and proven from more than 100 years of stock market history. I don't expect you to read it cover to cover, although I'd be delighted if you read every word! Instead, this book is designed as a reference tool. Feel free to read the chapters in whatever order you choose. You can flip to the sections and chapters that interest you or those that include topics that you need to know more about.

Stock Investing For Dummies, 4th Edition, is also quite different from the “get rich with stocks” titles that have crammed the bookshelves in recent years. It doesn't take a standard approach to the topic; it doesn't assume that stocks are a sure thing and the be-all, end-all of wealth-building. In fact, at times in this book, I tell you *not* to invest in stocks (or even to bet against them!).

This book can help you succeed not only in up markets but also in down markets. Bull markets and bear markets come and go, but the informed investor can keep making money no matter what. To give you an extra edge, I've tried to include information about the investing environment for stocks. Whether it's politics or hurricanes (or both), you need to know how the big picture affects your stock investment decisions.

Conventions Used in This Book

To make navigating through this book easier, I've established the following conventions:

- ✓ **Boldface** text points out key words or the main parts of bulleted items.
- ✓ *Italics* highlight new terms that are defined.
- ✓ `Monofont` is used for web addresses.

When this book was printed, some web addresses may have needed to break across two lines of text. If that happened, rest assured that I haven't put in any extra characters (such as hyphens) to indicate the break. So when using one of these web addresses, just type in exactly what you see in this book, pretending as though the line break doesn't exist.

What You're Not to Read

Sidebars (gray boxes of text) in this book give you a more in-depth look at a certain topic. Although they further illuminate a particular point, these sidebars aren't crucial to your understanding of the rest of the book. Feel free to read them or skip them. Of course, I'd love for you to read them all, but my feelings won't be hurt if you decide to skip over them.

The text that accompanies the Technical Stuff icon (see the forthcoming section "Icons Used in This Book") can be passed over as well. The text associated with this icon gives some technical details about stock investing that are certainly interesting and informative, but you can still come away with the information you need without reading this text.

Foolish Assumptions

I figure you've picked up this book for one or more of the following reasons:

- ✓ You're a beginner and want a crash course on stock investing that's an easy read.
- ✓ You're already a stock investor, and you need a book that allows you to read only those chapters that cover specific stock investing topics of interest to you.
- ✓ You need to review your own situation with the information in this book to see if you missed anything when you invested in that hot stock that your brother-in-law recommended.
- ✓ You need a great gift! When Uncle Mo is upset over his poor stock picks, you can give him this book so he can get back on his financial feet. Be sure to get a copy for his broker, too. (Odds are that the broker was the one who made those picks to begin with.)

How This Book Is Organized

The information is laid out in a straightforward format. The parts progress in a logical approach that any investor interested in stocks can follow very easily.

Part I: The Essentials of Stock Investing

This part is for everyone. Understanding the essentials of stock investing and investing in general will only help you, especially in uncertain economic times. Stocks may even touch your finances in ways not readily apparent. For example, stocks aren't only in individual accounts; they're also in mutual funds and pension plans.

An important point is that stocks are really financial tools that are a means to an end. Investors should be able to answer the question, "Why am I considering stocks at all?" Stocks are a great vehicle for wealth-building, but only if investors realize what they can accomplish and how to use them. Chapter 2 explains how to take stock of your current financial situation and goals, and Chapter 3 defines common approaches to stock investing.

One of the essentials of stock investing is understanding risk. Most people are clueless about risk. You can't avoid every type of risk out there (life itself embodies risk). However, Chapter 4 can help you recognize it and find ways to minimize it in your stock investing program. It's one of the most important chapters that serious stock investors should read. While I'm at it, I also discuss volatility because that concept is frequently tied at the hip with risk.

There's more than one way to invest in stocks. The bulk of this book is about direct stock investing. But for some, indirect stock investing is the way to go. Exchange-traded funds (ETFs) provide some opportunities for conservative investors that I can't ignore! Therefore, check out Chapter 5 on this great approach to stock investing.

Part II: Before You Start Buying

When you're ready to embark on your career as a stock investor, you need to use some resources to gather information about the stocks you're interested in. Fortunately, you live in the information age. I pity the investors from the 1920s who didn't have access to so many resources, but today's investors are in an enviable position. This part tells you where to find information and how to use it to be a more knowledgeable investor (a rarity in recent years!). For example, I explain that stocks can be used for both growth and income purposes, and I discuss the characteristics of each; see Chapters 8 and 9 for more information.

Chapter 6 is a great starting place for your information gathering; I show you how to stay on top of financial news and read stock tables, among other topics.

When you're ready to invest, you'll invariably have to turn to a broker. Several types of brokers are out there, so you should know which is which. The wrong broker can make you . . . uh . . . broker. Chapter 7 helps you choose.

New to this edition is Chapter 10, which gives you the lowdown on the basics of technical analysis, which is critical to know, especially if you have a short-term investing focus.

Part III: Picking Winners

I compare buying stock to picking goldfish. If you look at a bunch of goldfish to choose which ones to buy, you want to make sure that you pick the healthiest ones. With stocks, you also need to pick companies that are healthy. Part III can help you do that. It's about picking good stocks by using micro-economics, meaning that you look at the stocks of individual companies. I explain how to evaluate a company's products, services, and other factors so that you can determine whether a company is strong and healthy.

If I can steer you toward those segments of the stock market that show solid promise for the coming years, that alone would make your stock portfolio thrive. Putting your money into solid companies in thriving industries has been the hallmark of superior stock investing throughout history. It's no different now. Check out Chapter 13 if you want to know more about emerging sector opportunities.

Where do you turn to find out about a company's financial health? In Chapters 11 and 12, I show you the documents you should review to make a more informed decision. When you find the information, you'll discover how to make sense of that data as well. While you're at it, check out Chapter 14 (on investing with megatrends) and Chapter 15 (on understanding the big picture with the economy and politics, which affects the art of stock-picking).

Part IV: Investment Strategies and Tactics

Investing in stocks isn't just about what you invest in; it's also about how you go about doing it. Part IV reveals tips, strategies, and resources that you shouldn't ignore to enhance your approach to prudent stock investing.

Investing is a long-term activity, but stocks can also be short-term buying and selling opportunities, so I discuss stock trading in Chapter 16. This chapter covers the fine art of speculating, too.

In Chapter 17, I provide guidance on understanding brokerage orders. Even using the basic types will definitely enhance your chance of success. After you master the basics, you can move on to Chapter 18, which gets a little more advanced. Triggers and advanced conditional orders are the newest tools for investors, so be sure to take a look.

You may be an investor, but that doesn't mean that you have deep pockets. Chapter 19 tells you how to buy stocks with low (or no) transaction costs. If you're going to buy the stock anyway, why not save on commissions and other costs?

As an investor, you must keep an eye on what company insiders are doing. In Chapter 20, I explain what it may mean if a company's management is buying or selling the same stock that you're considering. I even touch on insider buying by politicians (nothing is sacred!).

After you spend all your time, money, and effort to grow your money in the world of stocks, you have yet another concern: holding on to your hard-earned gains. This challenge is summarized in one word: taxes. Sound tax planning is crucial for everyone who works hard. After all, taxes are the biggest expense in your lifetime (right after children!). See Chapter 21 for more information.

Part V: The Part of Tens

I wrap up the book with a hallmark of *For Dummies* books — the Part of Tens. These chapters give you a mini crash course in stock investing.

In this part, I discuss what to do when your portfolio is down (Chapter 22) and what to consider when your portfolio is up (Chapter 23). Chapter 24 covers ten opportunities and challenges that face stock investors. I also offer some tips on nonstock strategies that go well with stocks (Chapter 25).

Part VI: Appendixes

Don't overlook the appendixes. I pride myself on the resources I can provide my students and readers so that they can make informed investment decisions. Whether the topic is stock investing terminology, economics, or avoiding capital gains taxes, I include a treasure trove of resources to help you. Whether you go to a bookstore, the library, or the Internet, Appendix A gives you some great places to turn to for help. In Appendix B, I explain financial ratios. These important numbers help you better determine whether to invest in a particular company's stock.

Icons Used in This Book

Useful icons appear in the margins of this book; here's what they mean.



When you see this icon, I'm reminding you about some information that you should always keep stashed in your memory, whether you're new to investing or an old pro.



The text attached to this icon may not be crucial to your success as an investor, but it may enable you to talk shop with investing gurus and better understand the financial pages of your favorite business publication or website.



This icon flags a particular bit of advice that just may give you an edge over other investors.



Pay special attention to this icon because the advice can prevent headaches, heartaches, and financial aches.

Where to Go from Here

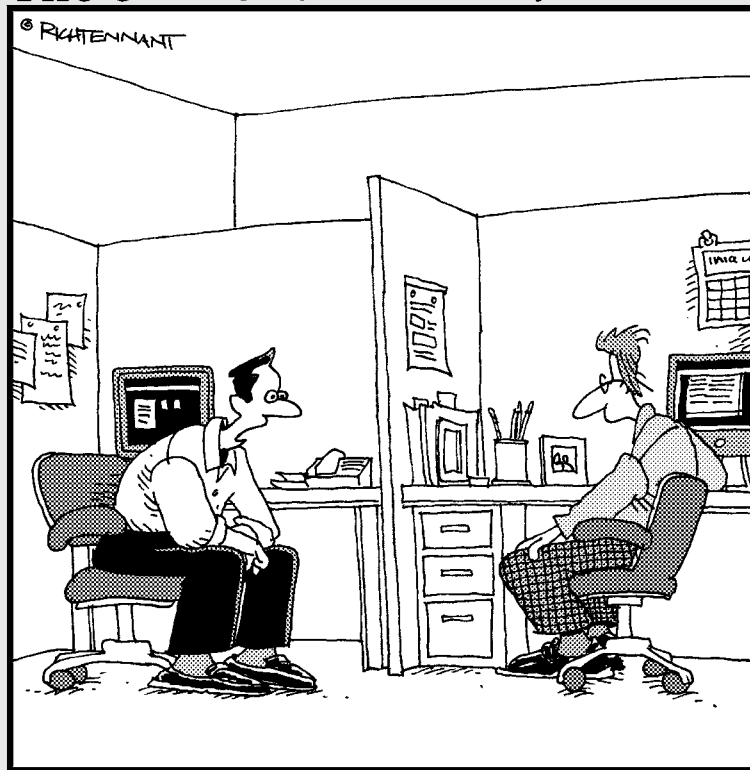
You may not need to read every chapter to make you more confident as a stock investor, so feel free to jump around to suit your personal needs. Because every chapter is designed to be as self-contained as possible, it won't do you any harm to cherry-pick what you really want to read. But if you're like me, you may still want to check out every chapter because you never know when you may come across a new tip or resource that will make a profitable difference in your stock portfolio. I want you to be successful so that I can brag about you in the next edition!

Part I

The Essentials of Stock Investing

The 5th Wave

By Rich Tennant



"I told my broker I wanted him to be more aggressive, so he called me an idiot and hung up the phone."

In this part . . .

The latest market turmoil and uncertainty tell investors to get back to square one. Your success is dependent on doing your homework before you invest your first dollar in stocks. Most investors don't realize that they should be scrutinizing their own situations and financial goals at least as much as they scrutinize stocks. How else can you know which stocks are right for you? Too many people risk too much simply because they don't take stock of their current needs, goals, and risk tolerance before they invest. The chapters in this part tell you what you need to know to choose the stocks that best suit you. I even include a chapter on exchange-traded funds (ETFs) because they give you an easier venue into the world of stocks.