LEARNING MADE EASY

9th Edition

Investing

for dummies®
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Pick winning stocks, mutual funds, and ETFs

Develop and manage your portfolio through all economies

Invest in real estate and small business

Eric Tyson, MBA

Bestselling author, *Personal Finance For Dummies*

20 Rules for Successful Investing

1. **Saving is a prerequisite to investing.** Unless you have wealthy, benevolent relatives, living within your means and saving money are prerequisites to investing and building wealth.
2. **Know the three best wealth-building investments.** People of all economic means make their money grow in ownership assets — stocks, real estate, and small business — where they share in the success and profitability of the asset.
3. **Be realistic about expected returns.** Over the long term, 9 to 10 percent per year is about right for ownership investments (such as stocks and real estate). If you run a small business, you can earn higher returns and even become a multimillionaire, but years of hard work and insight are required.
4. **Think long term.** Because ownership investments are riskier (more volatile), you must keep a long-term perspective when investing in them. Don't invest money in such investments unless you plan to hold them for a minimum of five years, preferably a decade or longer.
5. **Match the time frame to the investment.** Selecting good investments for yourself involves matching the time frame you have to the riskiness of the investment. For example, for money that you expect to use within the next year, focus on safe investments, such as money market funds. Invest your longer-term money mostly in wealth-building investments.
6. **Diversify.** Diversification is a powerful investment concept that helps you to reduce the risk of holding more aggressive investments. Diversifying simply means that you should hold a variety of investments that don't move in tandem in different market environments. For example, if you invest in stocks, invest worldwide, not just in the U.S. market. You can further diversify by investing in real estate.
7. **Look at the big picture first.** Understand your overall financial situation and how wise investments fit within it. Before you invest, examine your debt obligations, tax situation, ability to fund retirement accounts, and insurance coverage.
8. **Ignore the minutiae.** Don't feel mystified by or feel the need to follow the short-term gyrations of the financial markets. Ultimately, the prices of stocks, bonds, and other financial instruments are determined by supply and demand, which are influenced by thousands of external issues and millions of investors' expectations and fears.
9. **Allocate your assets.** How you divvy up or allocate your money among major investments greatly determines your returns. The younger you are and the more money you earmark for the long term, the greater the percentage you should devote to ownership investments.

10. **Do your homework before you invest.** You work hard for your money, and buying and selling investments costs you money. Investing isn't a field where acting first and asking questions later works well. Never buy an investment based on an advertisement or a salesperson's solicitation of you.

11. **Keep an eye on taxes.** Take advantage of tax-deductible retirement accounts and understand the impact of your tax bracket when investing outside tax-sheltered retirement accounts.

12. **Consider the value of your time and your investing skills and desires.** Investing in stocks and other securities via the best mutual funds and exchange-traded funds is both time-efficient and profitable. Real estate investing and running a small business are the most time-intensive investments.

13. **Where possible, minimize fees.** The more you pay in commissions and management fees on your investments, the greater the drag on your returns. And don't fall prey to the thinking that "you get what you pay for."

14. **Don't expect to beat the market.** If you have the right skills and interest, your ability to do better than the investing averages is greater with real estate and small business than with stock market investing. The large number of experienced, full-time stock market professionals makes it next to impossible for you to choose individual stocks that will consistently beat a relevant market average over an extended time period.

15. **Don't bail when things look bleak.** The hardest time, psychologically, to hold on to your investments is when they're down. Even the best investments go through depressed periods, which is the worst possible time to sell. Don't sell when there's a sale going on; if anything, consider buying more.

16. **Ignore soothsayers and prognosticators.** Predicting the future is nearly impossible. Select and hold good investments for the long term. Don't try to time when to be in or out of a particular investment.

17. **Minimize your trading.** The more you trade, the more likely you are to make mistakes. You also get hit with increased transaction costs and higher taxes (for non-retirement account investments).

18. **Hire advisors carefully.** Before you hire investing help, first educate yourself so you can better evaluate the competence of those you may hire. Beware of conflicts of interest when you consider advisors to hire.

19. **You are what you read and listen to.** Don't pollute your mind with bad investing strategies and philosophies. The quality of what you read and listen to is far more important than the quantity. Find out how to evaluate the quality of what you read and hear.

20. **Your personal life and health are the highest-return, lowest-risk investments.** They're far more important than the size of your financial portfolio.

Praise for Eric Tyson's Best-Selling *For Dummies* Titles

"Eric Tyson For President!!! Thanks for such a wonderful guide. With a clear, no-nonsense approach to . . . investing for the long haul, Tyson's book says it all without being the least bit long-winded. Pick up a copy today. It'll be your wisest investment ever!!!" —Jim Beggs, VA

"Eric Tyson is doing something important — namely, helping people at all income levels to take control of their financial futures. This book is a natural outgrowth of Tyson's vision that he has nurtured for years. Like Henry Ford, he wants to make something that was previously accessible only to the wealthy accessible to middle-income Americans." —James C. Collins, co-author of the national bestsellers *Built to Last* and *Good to Great*

"The organization of this book is superb! I could go right to the topics of immediate interest and find clearly written and informative material." —Lorraine Verboort, Beaverton, OR

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"*Personal Finance For Dummies* is the perfect book for people who feel guilty about inadequately managing their money but are intimidated by all of the publications out there. It's a painless way to learn how to take control." —Karen Tofte, producer, National Public Radio's *Sound Money*

Investing

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by Eric Tyson, MBA

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Introduction

With each new edition of this investing guide, I find that the core investment philosophy I discuss within it has stood the tests of time and changing market forces.

During the financial crisis of 2008, things got scary. Large Wall Street firms were going under, stock prices were plummeting, and layoffs and unemployment rates were soaring. And all this was happening in the midst of the 2008 presidential election. Talk of another Great Depression was in the air. In fact, polls showed a majority of Americans feared that another depression was actually happening. Housing prices were dropping sharply in most communities, and more and more properties were ending up in foreclosure.

Investing didn't seem so fun anymore. However, even though the downturn was the worst in decades, it had similarities to prior downturns, and people who kept their sense of perspective and followed my advice have enjoyed tremendous returns since the market bottom.

Now, fast forward to 2020. The United States was enjoying one of the longest continuous periods of economic expansion and the unemployment rate had sunk to a 50-year low. Stock prices continued to rise to new highs despite periodic setbacks. And then the coronavirus upset the good times and quickly reminded us that investing involves risks and sharp price declines, often when least expected.

I know from working with people of modest and immodest economic means that they increase their wealth by doing the following:

- Living within their means and systematically saving and investing money, ideally in a tax-favored manner
- Buying and holding a globally diversified portfolio of stocks
- Building their own small business
- Investing in real estate

This book explains each of these wealth boosters in detail. Equally, if not more important, however, is the information I provide to help you understand and choose investments compatible with your personal and financial goals.

About This Book

The best investment vehicles for building wealth — stocks, real estate, and small business — haven't changed. But you still need money to play in the investment world. Like the first edition of *Investing For Dummies*, the ninth edition of this national bestseller includes complete coverage of these wealth-building investments as well as other common investments, such as bonds. Here are the biggest changes in this edition:

- **I've updated the data and examples in this book to provide you the latest insights and analyses.** Having trouble comprehending whether the Federal Reserve's interest rate policy will impact the stock market? Curious about how tax law changes may impact your investment strategies? Worried what impact the election will have on the economy and financial markets? Confused with the increasing array of retirement account savings options such as individual 401(k)s and Roth 401(k)s? Seeking a way to invest in stocks without exposing yourself to the tremendous risks experienced during the 2008 financial crisis or the 2020 coronavirus downturn? Curious about what an exchange-traded fund (ETF) or hedge fund is and whether you should invest in one? Wondering why people are talking about cryptocurrencies like Bitcoin and whether you should consider them? Contemplating using an online broker that is advertising "free" trading? Weighing whether and where to invest in real estate given current market conditions? Wondering what the best ways are to invest globally? Having trouble making sense of various economic indicators and what they mean to your investment strategy? You can find the answers to these questions and many more in this edition.
- **I offer more information on investing resources.** With the tremendous growth in websites, software, apps, publications, media outlets, and other sources of investing advice and information, you're probably overwhelmed in choosing among the numerous investing research tools and resources. Equally problematic is figuring out who you can trust — and who you need to ignore. So many pundits and prognosticators claim excellent track records for their past predictions, but who, really, can you believe? I explain how to evaluate the quality of current investment tools and resources, and I provide tips on deciding who to listen to and who to tune out.

To build wealth, you don't need a fancy college or graduate-school degree, and you don't need a rich dad (or mom), biological or adopted! What you do need is a desire to read and practice the many simple yet powerful lessons and strategies in this book.

Seriously, investing intelligently isn't rocket science. By all means, if you're dealing with a complicated, atypical issue, get quality professional help. But educate yourself first. Hiring someone can be risky if you're financially challenged. If you do decide to hire someone, you'll be much better prepared if you educate yourself. Doing so can also help you focus your questions and assess that person's competence.

Foolish Assumptions

Every book is written with a certain reader in mind, and this book is no different. Here are some assumptions I made about you:

- You may have some investments, but you're looking to develop a full-scale investment plan.
- You'd like to strengthen your portfolio.
- You want to evaluate your investment advisor's or broker's advice.
- You have a company-sponsored investment plan, like a 401(k), and you're looking to make some decisions or roll it over into a new plan.

If one or more of these descriptions sound familiar, you've come to the right place.

Icons Used in This Book

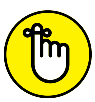
Throughout this book, icons help guide you through the maze of suggestions, solutions, and cautions. I hope the following images make your journey through investment strategies smoother.

ERIC'S PICKS

If you see this icon, I'm pointing out companies, products, services, and resources that have proved to be exceptional over the years. These are resources that I would or do use personally or would recommend to my friends and family.

INVESTIGATE

I use this icon to highlight an issue that requires more detective work on your part. Don't worry, though; I prepare you for your work so you don't have to start out as a novice gumshoe.



REMEMBER

I think the name says it all, but this icon indicates something really, really important — don't you forget it!

TECHNICAL STUFF

Skip it or read it; the choice is yours. You'll fill your head with more stuff that may prove valuable as you expand your investing know-how, but you risk overdosing on stuff that you may not need right away.

TIP

This icon denotes strategies that can enable you to build wealth faster and leap over tall obstacles in a single bound.

WARNING

This icon indicates treacherous territory that has made mincemeat out of lesser mortals who have come before you. Skip this point at your own peril.

Beyond the Book

In addition to the material in the print or e-book you're reading right now, this product comes with a free access-anywhere Cheat Sheet that can set you on the path to successful investing. To get this Cheat Sheet, simply go to `www.dummies.com` and search for "Investing For Dummies Cheat Sheet" in the Search box.

Where to Go from Here

If you have the time and desire, I encourage you to read this book in its entirety. It provides you with a detailed picture of how to maximize your returns while minimizing your risks through wealth-building investments. But you don't have to read this book cover to cover. If you have a specific question or two that you want to focus on today, or if you want to find some additional information tomorrow, that's not a problem. *Investing For Dummies*, 9th Edition, makes it easy to find answers to specific questions. Just turn to the table of contents or the index to locate the information you need. You can get in and get out, just like that.

1

Getting Started with Investing

IN THIS PART . . .

Get familiar with the different types of investments you have to choose from, including stocks, bonds, real estate, small business, and funds.

Deepen your understanding of risks and returns so you can make informed investing decisions and react to changes in the market.

Make wise investing decisions that fit with your overall financial situation and goals.

IN THIS CHAPTER

» Defining investing

» Seeing how stocks, real estate, and small business ownership build long-term wealth

» Understanding the role of lending and other investments

» Knowing where not to invest your money

Chapter 1

Exploring Your Investment Choices

In many parts of the world, life's basic necessities — food, clothing, shelter, healthcare, and taxes — consume the entirety of people's meager earnings. Although some Americans do truly struggle for basic necessities, the bigger problem for other Americans is that they consider just about *everything* — eating out, driving new cars, hopping on airplanes for vacation — to be a necessity.

I've taken it upon myself (using this book as my tool) to help you recognize that investing — that is, putting your money to work for you — is a necessity. If you want to accomplish important personal and financial goals, such as owning a home, starting your own business, helping your kids through college (and spending more time with them when they're young), retiring comfortably, and so on, you must know how to invest well.

It's been said, and too often quoted, that the only certainties in life are death and taxes. To these two certainties I add one more: being confused by and ignorant about investing. Because investing is a confounding activity, you may be tempted to look with envious eyes at those people in the world who appear to be savvy with money and investing. Remember that everyone starts with the same level of financial knowledge: none! *No one* was born knowing this stuff! The only difference between those who know and those who don't is that those who know have either devoted their time and energy to acquiring useful knowledge about the investment world or have had their parents instill a good base of investing knowledge.

Getting Started with Investing

Before I discuss the major investing alternatives in the rest of this chapter, I want to start with something that's quite basic yet important. What exactly do I mean when I say "investing"? Simply stated, *investing* means you have money put away for future use.

You can choose from tens of thousands of stocks, bonds, mutual funds, exchange-traded funds, and other investments. Unfortunately for the novice, and even for the experts who are honest with you, knowing the name of the investment is just the tip of the iceberg. Underneath each of these investments lurks a veritable mountain of details.

REMEMBER

If you wanted to and had the ability to quit your day job, you could make a full-time endeavor out of analyzing economic trends and financial statements and talking to business employees, customers, suppliers, and so on. However, I don't want to scare you away from investing just because some people do it on a full-time basis. Making wise investments need not take a lot of your time. If you know where to get high-quality information and you purchase well-managed investments, you can leave the investment management to the best experts. Then you can do the work that you're best at and have more free time for the things you really enjoy doing.

An important part of making wise investments is knowing when you have enough information to do things well on your own versus when you should hire others. For example, foreign stock markets are generally more difficult to research and understand than domestic markets. Thus, when investing overseas, hiring a good money manager, such as through a mutual or exchange-traded fund, makes more sense than going to all the time, trouble, and expense of picking individual international stocks.

I'm here to give you the information you need to make your way through the complex investment world. In the rest of this chapter, I clear a path so you can identify the major investments and understand the strengths and weaknesses of each.

Building Wealth with Ownership Investments

ERIC'S PICKS

If you want your money to grow faster than the rate of inflation over the long term and you don't mind a bit of a roller-coaster ride from time to time in your investments' values, ownership investments are for you. *Ownership investments* are those investments where you own an interest in some company or other asset (such as stock, real estate, or a small business) that has the ability to generate revenue and profits.

Observing how the world's richest have built their wealth is enlightening. Not surprisingly, many of the champions of wealth around the globe gained their fortunes largely through owning a piece (or all) of a successful company that they (or others) built.

In addition to owning their own businesses, many well-to-do people have built their nest eggs by investing in real estate and the stock market. With softening housing prices in many regions in the late 2000s, some folks newer to the real estate world incorrectly believe that real estate is a loser, not a long-term winner. Likewise, the stock market goes through down periods but does well over the long term. (See Chapter 2 for the scoop on investment risks and returns.)

And, of course, some people come into wealth through an inheritance. Even if your parents are among the rare wealthy ones and you expect them to pass on big bucks to you, you need to know how to invest that money intelligently.

REMEMBER

If you understand and are comfortable with the risks and take sensible steps to *diversify* (you don't put all your investment eggs in the same basket), ownership investments are the key to building wealth. For most folks to accomplish typical longer-term financial goals, such as retiring, the money that they save and invest needs to grow at a healthy clip. If you dump all your money in bank accounts that pay little if any interest, you're more likely to fall short of your goals.

Not everyone needs to make his money grow, of course. Suppose that you inherit a significant sum and/or maintain a restrained standard of living and work well into your old age simply because you enjoy doing so. In this situation, you may not need to take the risks involved with a potentially faster-growth investment. You may be more comfortable with *safer* investments, such as paying off your mortgage faster than necessary. Chapter 3 helps you think through such issues.

Entering the stock market

Stocks, which are shares of ownership in a company, are an example of an ownership investment. If you want to share in the growth and profits of companies like Skechers (footwear), you can! You simply buy shares of their stock through a brokerage firm. However, even if Skechers makes money in the future, you can't guarantee that the value of its stock will increase.

Some companies today sell their stock directly to investors, allowing you to bypass brokers. You can also invest in stocks via a stock mutual fund (or an exchange-traded fund), where a fund manager decides which individual stocks to include in the fund. I discuss the various methods for buying stock in Chapter 6.

REMEMBER

You don't need an MBA or a PhD to make money in the stock market. If you can practice some simple lessons, such as making regular and systematic investments and investing in proven companies and funds while minimizing your investment expenses and taxes, you should make decent returns in the long term.

However, I don't think you should expect that you can "beat the markets," and you certainly are not likely to beat the best professional money managers at their own full-time game. This book shows you time-proven, non-gimmicky methods to make your money grow in the stock market as well as in other financial markets. I explain more about stocks and mutual funds in Part 2.

Owning real estate

People of varying economic means build wealth by investing in real estate. Owning and managing real estate is like running a small business. You need to satisfy customers (tenants), manage your costs, keep an eye on the competition, and so on. Some methods of real estate investing require more time than others, but many are proven ways to build wealth.

John, who works for a city government, and his wife, Linda, a computer analyst, have built several million dollars in investment real estate *equity* (the difference between the property's market value and debts owed) over the decades. "Our parents owned rental property, and we could see what it could do for you by providing income and building wealth," says John. Investing in real estate also appealed to John and Linda because they didn't know anything about the stock market, so they wanted to stay away from it. The idea of *leverage* — making money with borrowed money — on real estate also appealed to them.

John and Linda bought their first property, a duplex, when their combined income was just $35,000 per year. Every time they moved to a new home, they kept the prior one and converted it to a rental. Now in their 50s, John and Linda own seven