

I released the new version of 5 Simple Rules for Investing in the Stock Market on 26 September 2011. For those that purchased the book previously, but want to access the new content I've included it in this file for you.

The two main changes are a new chapter of Investing for the Dividend Income and I also rewrote the Introduction chapter.

Here they are:

INTRODUCTION

This book contains the stock picking strategy that I use to successfully make a profit in the stock market. It contains just five simple rules (and a few extra guidelines) that can be used by anyone to help them pick strong companies without having to know a lot about stocks to begin with.

I didn't set out to be an expert in the stock market and I'm still definitely not an expert, nor am I a financial planner or economist. In fact I'm just a regular person like you that one day, after being fed up with working a boring nine to five temp job decided to dabble in the stock market in an effort to try and make some money.

Of course becoming profitable and finding a winning strategy didn't happen immediately – it took a while before I was actually any good at the whole stock game. Over the course of five years I continued to work in crappy jobs while I read every book on the stock market I could and studied hundreds of different strategies. When I saved up my first thousand dollars I took the plunge and invested it into the stock market. It took another few years (and a few mistakes along the way) but eventually I had built up enough equity that I could leave full time employment and live on the proceeds of my investments.

My goal at the beginning was simply to build up a nice little portfolio and be able to support myself and while there have been both good and bad times when I have and haven't been able to do that (and we are in a rather bad time right now) overall I've been fairly successful with the methods I use. So by writing this book my hope is that it can help you to become successful as well and perhaps be able to build up your own successful little portfolio of stocks.

I think this book will appeal to those people who want to become more involved in buying stocks, so that they can gain more control over their finances, without having to learn too many complicated formula's and strategies.

It's not for everyone however. If you are already seriously involved in investing in the stock market then you may find my strategies rather simplistic. It's more for those everyday investors who are interested in learning more about what makes a good company and how to determine whether it would make a good investment.

Before I wrote this book, 5 Simple Rules for Investing in the Stock Market, I spent a lot of time reading other books in the market to see what was available. Most of the books I found were great on theory but not a lot of them had practical steps that you could take to choose your investments. So that's what I've done in this book. It doesn't contain much theory since you can already get that

in many other wonderful stock market books but rather it contains practical 'how to' steps on what to look for. That's what I believe differentiates it from other books in the market.

I get quite specific in this book about what I look for. I know that I have strong opinions on what constitutes a good investment and it's likely that at times you may not agree with all of my rules.

If you have a different opinion – for example if you don't think debt to equity is as important as I do – then by all means just take out of this book those rules you do agree with and adapt them to your own experiences. These rules work for me, and while I know they can also work for others, you need to make investment decisions that are right for you and your situation. That goes for any financial decisions that you make. You need to be in control and do what is right for you.

The stock market can be very subjective. That's probably why there are so many different strategies and theories on which methods work. Even the experts can't agree sometimes. Some methods work, some of them don't. To be honest I think there are lots of different stock market investment strategies that can work, it just comes down to choosing a method that suits your style the best and sticking with it. But if you want to give my method a try, and I'm guessing that you do because you've purchased this book, then I'll tell you exactly what works for me. Of course in this day and age, you know that I can't guarantee that it will work for you. I sincerely hope it does of course, but alas I cannot guarantee it for fear of being sued. So use your own judgement.

If you're cool with that and you are keen to jump right in and see what these five simple rules are all about then by all means welcome aboard and thanks for buying the book.

The book is set out rather simply and flows in a logical style of how I choose the companies that I do.

- The first chapter talks about whether you should even consider investing in the stock market at all, especially in the rocky economic climate that we are in right now.

- Chapter two outlines the five basic stock picking rules that I use and why I narrowed it down to just five.

The following chapters each cover one of the rules.

- Chapter three is about choosing the market leaders in the field. The blue-chip stocks if you will.

- Chapter four is what I consider to be the most important rule of all, and that is only choosing companies that have a Return on Equity figure of fifteen per cent or higher.

- Chapter five talks about the importance of the company having a positive earnings growth.

- Chapter six covers choosing companies that have low debt. You can potentially avoid many disasters by choosing companies that have not borrowed more than they can afford.

- Chapter seven looks back at the history of the stock price to see if it has a proven record of return for investors. While past performance is no guarantee of future performance it does tend to follow that if a company rises steadily each year that it will continue to do so.

- Chapter eight shows you how to determine whether the stock is trading at a fair price and how much you want to purchase it for.

- Chapter nine looks at investing for the dividend income. A sensible strategy for times when the market is rocky and you still want to make a good return from your investment.

- Chapter ten looks at the main reasons when you should sell your stocks and when to continue to hold.

- And finally I wrap things up in the conclusion.

Throughout each chapter I'll show which of the stocks from the Dow Jones Industrial Average make the rules and at the end we'll see which ones, if any, fit all of them and would be great companies to consider investing in.

So if you are ready, let's get started.

Chapter 9 - Investing for the Dividend Income

"Wild swings in share prices have more to do with the "lemming-like" behaviour of institutional investors than with the aggregate returns of the company they own." – Warren Buffett

So now that you've found some great companies to invest in that have an excellent chance of increasing in value over the long term, can it get any better?

Yes it can.

Because many of these companies also pay high dividend yields, making them an excellent source of income as well as capital growth. In fact many investors who don't like the volatility of the stock market will often invest just for the dividend income they produce since many companies pay yields much higher than a regular savings account. Since it's hard push today to find a high interest savings account that pays an interest rate of more than two percent per annum within the United States, companies that offer upwards of three percent dividend yields (and sometimes as high as five or six percent) can look very attractive.

Most of the time the companies that pay the highest yields are those whose businesses receive income payments themselves such as property investment companies, insurance companies and so on. That's why they can afford to pay out such high dividends to investors because they receive high fees from customers themselves. Of course any company can pay high dividends; it isn't limited to only those service businesses.

Not all companies pay dividends however. It's up to the Board of Directors to decide whether to pay out a portion of the profits to investors or use that money to grow the business. This is why many investors believe that you can only invest for the income OR the growth (whereas I believe you can have both).

Investing in companies for the income also lowers your risk, because even if the company or market as a whole experiences volatility usually the dividend yield remains fairly stable. So receiving a

regular check every quarter can mitigate the risks involved in investing your money in stocks. Sure your initial investment isn't secure like it is in a regular bank account, but the higher yield can usually compensate for that. Let's look at an example.

Comparing Savings Account Interest vs. Dividend Yield

Let's imagine that you were an income investor and were only interested in the dividend yield. Let's also say that you have \$10,000 to invest.

If you put it into a standard savings account earning 1.5% (fairly average) over a five year period you'd earn around \$778 in interest. You would still of course keep your initial investment of \$10,000 as well since that money is secure.

Let's instead say that you invested in Verizon (one of the high dividend yield companies within the Dow Jones) who pays an average of 5.4% yield.

Five years ago on September 18, 2006 Verizon was trading at \$37.10. Buying \$10,000 worth of Verizon would have meant you purchased 269 shares. $269 \times \$37.10 = \$9,979.90$.

As of writing, Verizon is now trading at \$36.72 which means that your initial investment is now worth \$9,804.24 ($269 \times \36.72). This represents a loss of \$175.66.

However, each year Verizon paid out dividends remember? So over that period, you would have also received checks totalling well over \$2,000 for the five year period.

Sure your initial investment is slightly down, but the amount of money that you would have made in dividend income has more than covered that and is nearly triple what you could have earned in a regular savings account. That's why investing for the dividend income is so attractive to many people. It doesn't matter as much if the stock market is rocky because each quarter you still receive your dividend check in the mail.

You can check out the dividend yields on the Key Statistics page, the same page where we are getting all of our other financial figures. It's listed under Dividends and Splits and you can also see here when the next payout is. Generally though, payments are usually January, April, July and October.

Investing for income sounds great, and it is, but you also know that I like to choose companies with strong fundamentals that have the potential for high growth. Most investors think that you can't invest for both growth and income, however I disagree. I think that you can find great companies and then see if they pay a good dividend yield as well, so that you can have the best of both worlds.

The Companies from the Dow Jones That Fit All the Rules AND Have High Dividends

So far in this book, we narrowed down the selections to the following three companies who fit all of the five simple rules and were trading at below sixteen times earnings. Let's now look at what their dividend yields are.

Chevron – 3.1%

Intel – 3.8%

Exxon Mobil – 2.5%

I consider anything above three percent a good dividend yield (and anything above five percent outstanding), so of these companies both Chevron and Intel look like the best bets.

Why it's Not Just Retiree's that Invest for the Dividend Income

It makes sense that those people that want a regular investment income such as retiree's, will choose to invest for income rather than growth since they don't usually have time on their side to wait until the market increases, they need the money now to live on. But the same can be said for anyone that wants to receive a regular income; college students, single parents, anyone really. Of course you do need a fairly substantial capital to earn a full time living simply from the investment checks.

To receive a yearly income of \$50,000 you'll need to have invested a cool one million dollars first. (You DO have one million just sitting around waiting to invest in stocks don't you? No?) This is the reason why generally it is only retiree's that can afford this strategy, but even if you have a few thousand you still should be taking advantage of the dividend yields since it lowers the volatility of your investment. It's been proven that those that invest in companies that pay good dividend yields make higher returns overall than those that don't.

But that doesn't mean you should simply find the stock paying the highest dividend yield and be done with it.

Currently Frontier Communications (FTR) has a dividend yield of 10.7% (extremely high). Five years ago, it was trading at \$13.66 and today it is trading at \$7.11. That represents a loss of around 48%. Now over time you would have received dividends of course, but even the high yield that this company pays out wouldn't have protected you. On an investment of \$10,000 your initial investment would now be worth \$5,200 and over that time you would have received around \$4,000 in dividend income. While it sounds nice, the high dividend payout wouldn't have been enough to protect your initial investment from eroding. That's why it's still important to choose strong companies first and THEN look at the dividend yield so that you have an increased chance of making a profit.

If you can find great companies that are paying good dividend yields then you'll be able to ride out the volatility and still make money.

Should You Take The Cash Or Re-Invest Your Dividends?

Some companies that pay out dividends may give you the option to re-invest the dividend amount back into the company in the form of more stocks. This is usually done at a slight discount to the

current market price to make it more attractive to stockholders. But is it a good idea to do this, or should you take the cash instead?

Both are fine options, and it really comes down to preference over whether you need the money or not in the short term. If you rely on the dividend income, or even just think it's a nice bonus then by all means take the cash, but if you already have an income and the odd dividend check isn't going to make a whole lot of difference to your bottom line then reinvesting your dividends back into the company is a very good idea.

Now you still will be taxed on those dividends whether you receive them as cash or reinvest, since they are still classed as income, so don't think that just because you don't get the check you are off the hook in this regard. Speak to your accountant for the best tax advice.

The main benefit of re-investing your dividends back into the company is that you can take advantage of the magic of compound interest. The more stock that you hold, the more dividend income that you make, so by re-investing that dividend amount and buying more stock, the next time you get a bigger piece of the pie. Over a long period of time you can essentially be holding more than double the amount of stock that you started with, each time getting 'paid' the dividend back in the form of more stock.

Dividend reinvestment plans work best on growth stocks or those companies that pay a high yield since both can accelerate the value of your portfolio.

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This file contains the updated chapters in the [5 Simple Rules for Investing in the Stock Market](#) book by Tracey Edwards.

