Stock Investing For Dummies
From Stock Investing For Dummies, 3rd Edition by Paul Mladjenovic

You’re investing in stocks — good for you! To make the most of your money and your choices, educate yourself on how to make stock investments intelligently, the Internet resources available to help you evaluate stocks, and ways to protect the money you earn. And, you need to do your homework before you invest in any company’s stock.

Ten Important Points about Stock Investing

If you’re committed to investing in stocks, keep these points in mind as you make your choices and reap your rewards. After all, stock investing is fun and frightening, sane and crazy-making, complicated and simple — and you may need reminders to stay focused.

1. **You’re not buying a stock; you’re buying a company.**
2. **The primary reason you invest in a stock is because the company is making a profit.**
3. **If you buy a stock when the company isn’t making a profit, you’re not investing — you’re speculating.**
4. **A stock (or stocks in general) should never be 100 percent of your assets.**
5. **In some cases (such as a severe bear market), stocks aren’t a good investment at all.**
6. **A stock’s price is dependent on the company, which in turn is dependent on its environment, which includes its customer base, its industry, the general economy, and the political climate.**
7. **Your common sense and logic can be just as important in choosing a good stock as the advice of any investment expert.**
8. **Always have well-reasoned answers to questions such as “Why are you investing in stocks?” and “Why are you investing in a particular stock?”**
9. **If you have no idea about the prospects of a company (and sometimes even if you think you do), always use stop-loss orders.**
10. **Even if your philosophy is to buy and hold for the long term, continue to monitor your stocks and consider selling them if they’re not appreciating or if general economic conditions have changed.**

Important Numbers to Review before Investing in Stock

As you invest in stocks, you naturally do a little research on the companies you’re thinking of investing in. The following list explains the key components to pay attention to when you look at a company’s main financial statements (the income statement and the balance sheet):

- **Earnings:** This number should be at least 10 percent higher than the year before.
- **Sales:** This number should be higher than the year before.
Debt: This number should be lower than or about the same as the year before. It should also be lower than the company's assets.

Equity: This number should be higher than the year before.

Volume*: This can be good or bad, depending on the stock.

* My comment only.

Financial Measures to Consider before Investing in Stock

You're thinking of buying stock in a company, but before you invest your hard-earned money in hopes of a profitable return, check out some financial ratios that can help indicate whether the company is on sound financial footing. Here are key measures to consider:

- **Price-to-earnings ratio (P/E):** For large cap stocks, the ratio should be under 20. For all stocks (including growth, small cap, and speculative issues), it shouldn't exceed 40.
- **Price to sales ratio (PSR):** The PSR should be as close to 1 as possible.
- **Return on equity (ROE):** ROE should be going up by at least 10 percent per year.
- **Earnings growth:** Earnings should be at least 10 percent higher than the year before. This rate should be maintained over several years.
- **Debt to asset ratio:** Debt should be half of assets or less.

What to Read before Investing in Stock

Before you invest in a company by buying stock in it, you need to do a little light — or not-so-light — reading. Investing in stock without checking out the company beforehand is a recipe for disaster. So, before you plunk down your money, be sure to do the following reading:

- The company's annual report
- The 10K and 10Q reports that the company files with the SEC
- *Standard & Poor's Stock Reports*
- *Value Line Investment Survey*
- *The Wall Street Journal and/or Investor's Business Daily*
- Reputable stock investing Web sites

Internet Resources for Stock Investing

With the tools available on the Internet, you have no excuse for not researching any and every potential stock investment. The following list of resources links you to some of the best financial Web sites around. Look at what they have to say about a company or an investment before you take the plunge.

- *Barron's*
How to Protect Your Stock Investing Profits

Besides being smart about your stock investments, you should protect the money your investments have earned. Protecting stock market profits means being on the defense. These tips will help:

- Always try to have some extra cash on the side, no matter how tempted you are to be 100 percent fully invested; you never know when buying opportunities may show up.
- Spread your money across several stocks.
- Buy more of a down (yet solid) stock.
- Even if you make what you think is the greatest choice in stock market history and still see the price decline, just wait; common sense takes over regarding a stock price over a protracted period. Long term, good choices go up and bad choices go down. ([Investing in Stocks by Term](investing_in_stocks_by_term) explains the differences between long- and short-term stock investing.)
- Use stop-loss orders, trailing stop orders, and limit orders.
- Set up broker triggers.
- Consider put options and covered call options.
- Sell, if you absolutely must.

See also:

- [How to Read a Stock Table](how_to_read_a_stock_table)
- [How to Invest Based on Stock Market Indexes](how_to_invest_based_on_stock_market_indexes)
- [How to Sharpen Your Stock Investment Skills](how_to_sharpen_your_stock_investment_skills)
- [Stock Investing for Your Personal Style](stock_investing_for_your_personal_style)