

# 7-Simple Investing Rules Your Mother Taught You

When I was growing up my mother had a saying, or an answer, for just about everything?as do most mothers. Every answer to the question? *Why???* was immediately met with the most intellectual of answers:

*??because I said so?.*

Seriously, my mother was a resource of knowledge that has served me well over the years, and it wasn't until late in life that I realized that she had taught me the basic principles for staying safe in the investment process. So, by imparting her secrets to you I may be violating some sacred ritual of motherhood knowledge, but I felt it was worth the risk to share the knowledge which has served me well.

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## 1) *Don't Run With Sharp Objects!*

It wasn't hard to understand why she didn't want me to run with scissors through the house ? I just think I did it early on just to watch her panic. However, later in life when I got my first apartment I ran through the entire place with a pair of scissors, left the front door open with the air conditioning on, and turned every light on in the house. That rebellion immediately stopped when I received my first electric bill. Sometime in the early 90's, the financial markets became a casino as the internet age ignited a whole generation of stock market gamblers who thought they were investors. **There is a huge difference between investing and speculating, and knowing the difference is critical to overall success.** Investing is backed by a solid investment strategy with defined goals, an accumulation schedule, allocation analysis and, most importantly, **a defined sell strategy and risk management plan.** **Speculation is nothing more than gambling.** If you are buying the latest hot stock, chasing stocks that have already moved 100% or more, or just putting money in the market because you think that you? *have to?*, you are gambling. The most important thing to understand about gambling is that success is a function of the probabilities and possibilities of winning or losing on each bet made. In the stock market, investors continue to play the possibilities instead of the probabilities. The trap comes with early success in speculative trading. **Success breeds confidence, and confidence breeds ignorance.** Most speculative traders tend to? *blow themselves up??* because of early success in their speculative investing habits. The speculative trader generally fails to hedge against the random events that occur in the financial markets. This in turn results in the trader losing more money than they ever imagined possible. **When investing, remember that the odds of making a losing trade increase with the frequency of transactions being made.** Just as running with a pair of scissors; do it often enough and eventually you could end up really hurting yourself. *What separates a winning investor from a speculative gambler is the ability to admit and correct mistakes when they occur.*



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## 2) **Look Both Ways Before You Cross The Street.**

I grew up in a small town so crossing the street wasn't as dangerous as it is in the city. Nonetheless, I was yanked by the collar more than once as I started to bolt across the street seemingly anxious to "find out what's on the other side." It is important to understand that traffic does flow in two directions, and if you only look in one direction, sooner or later you are going to get hit. A lot of people want to classify themselves as a *Bull* or a *Bear*. **The smart investor doesn't pick a side; he analyzes both sides to determine what the best course of action in the current market environment is most likely to be.** The problem with the proclamation of being a *bull* or a *bear* means that you are not analyzing the other side of the argument and that you become so confident in your position that you tend to forget that *the light at the end of the tunnel just might be an oncoming train.* It is an important part of your analysis, before you invest in the financial markets, to determine not only *where* but also *when* to invest your assets.

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## 3) **Always Wear Clean Underwear**

This was one of my favorite sayings from my mother because I always wondered about the rationality of it. I always figured that even if you were wearing clean underwear prior to an accident; you're still likely left without clean underwear following it. The first rule of investing is: *You are only wrong if you stay wrong.* However, being a smart investor means always being prepared in case of an accident. That means quite simply **have a mechanism in place to protect you when you are wrong with an investment decision.** You will notice that I said *when you are wrong* in the previous paragraph. You will make wrong decisions, in fact, the majority of the decisions you will make in investing will most likely turn out wrong. **However, it is cutting those wrong decisions short, and letting your right decisions continue to work, that will make you profitable over time.** Any person that tells you about all the winning trades he has made in the market is either lying, or he hasn't blown up yet. One of the two will be true 100% of the time. Understanding the *risk versus reward* trade off of any investment is the beginning step to risk management in your portfolio. Knowing how to mitigate the risk of loss in your holdings is crucial to your long-term survivability in the financial markets.

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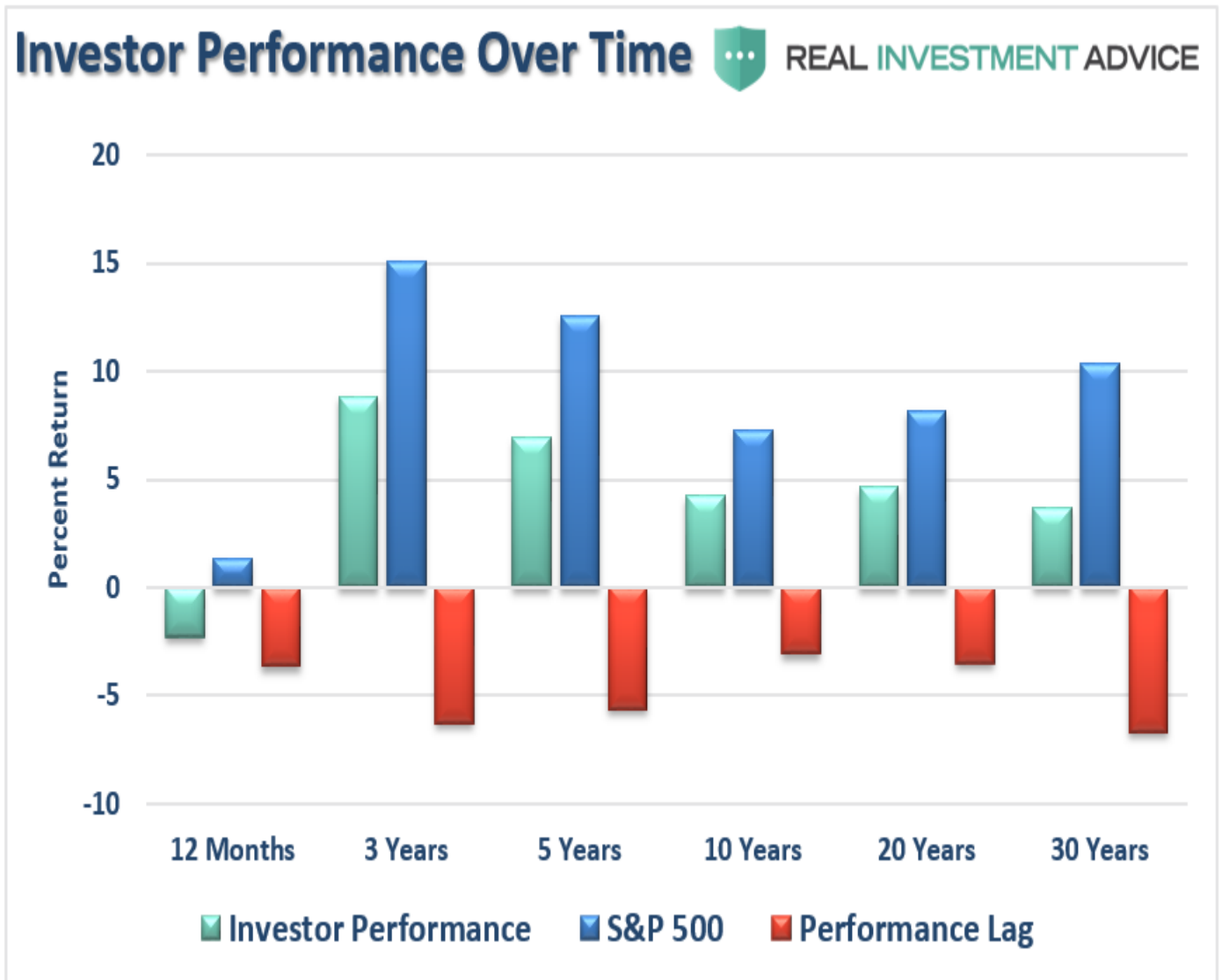
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## 4) **If Everyone Jumped Off The Cliff ? Would You Do It Too?**

Every kid, at one point or another, has tried to convince their Mother to allow them to do something through the use of *peer pressure.* I figured if she wouldn't let me do what I wanted, then surely she would bend to the will of the imaginary masses. She never did. *Peer pressure* is one of the biggest mistakes investors repeatedly make when investing. Chasing the latest *hot stocks* or *investment fads* that are already overvalued, and are running up on speculative fervor, always ends in disappointment. In the financial markets, investors get sucked into buying stocks that have already moved significantly off their lows because they are afraid of *missing out.* **This is speculating, gambling, guessing, hoping, praying ? anything but investing.** Generally, by the time the media begins featuring a particular investment, individuals have already missed the major part of the move. By that point, the probabilities of a decline began to outweigh the possibility of further rewards. It is a well-known fact that the market works in what is called a *herd mentality.*

Historically, investors all tend to run in one direction at one time until that direction falters, the *herd* then turns and runs in the opposite direction. This continues to the detriment of investor's returns over long periods as shown by [Dalbar investor studies](#).



This is also generally why investors wind up **buying high, and selling low**. In order to be a long-term successful investor, you have to understand the *herd mentality* and use it to your benefit **which means getting out from in front of the herd before you are trampled**. So, before you chase a stock that has already moved 100%, or more, try and figure out where the herd may move to next, and *place your bets there*. This takes discipline, patience, and a lot of homework but you will be well rewarded for your efforts in the end.

## 5) Don't Talk To Strangers

This is just good solid advice all the way around. Turn on the television, any time of the day or night, and it is the *Stranger's Parade of Malicious Intent*. I don't know if it is just me, or the fact the media only broadcast news that reveals the very depths of human depravity, but sometimes I have to wonder if we are not due for a planetary cleansing through divine intervention. Back to investing **getting your stock tips from strangers is a sure way to lose money in the stock market**. Your investing homework should **NOT** consist of a daily regimen of CNBC, followed by a dose of Grocer tips, capped off with a financial advisor's sales pitch. **In order to be successful in the long-run, you must understand the principals of investing, and the catalysts which will make that investment profitable in the future**. Remember, when you invest into a company you are buying a piece of that company, and its business plan. You are placing your hard earned

dollars into the belief the individuals managing the company have your best interests at heart. **The hope is they will operate in such a manner as to make your investment more valuable, so that it may eventually be sold to someone else for a profit.** This is also the very embodiment of the *Greater Fool Theory*, which states that there will always be someone willing to buy an investment at an ever higher price. **However, in the end, there is always someone left holding the bag, the trick is making sure that it isn't you.** Also, you need to be aware that when getting advice from the *One Minute Money Manager* crew on television. When an expert tells you about a company you should be buying, remember he already owns it, and most likely will be the one selling his shares to you.

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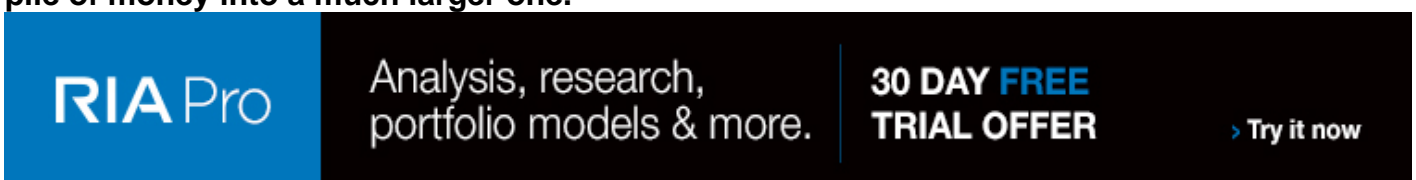
## 6) You Either Need To Do It (polite version) Or Get Off The Pot!

When I was growing up I hated to do my homework, which is ironic, since I now do more homework now than I ever dreamed of in my younger days. Since I did not like doing homework, school projects were almost never started until the night before they were due. I was the king of procrastination. My Mom was always there to help, giving me a hand, and an ear full of motherly advice, usually consisting of a lot of *because I told you so!* **I find it interesting that many investors tend to watch stocks for a very long period of time, never acting on their analysis, buy rather idly watching as their instinct proves correct, and the stock rises in price.** The investor then feels that he missed his entry point, and decides to wait, hoping the stock will go back down one more time so that he can get in. The stock continues to rise, the investor continues to watch becoming more frustrated until he finally capitulates on his emotion and buys the investment near the top. Procrastination, on the way up, and on the way down, are harbingers of emotional duress derived from the loss of opportunity or the destruction of capital. **However, if you do your homework and can build a case for the purchase, don't procrastinate.** If you miss your opportunity for the right entry into the position don't chase it. Leave it alone, and come back another day when ole' Bob Barker is telling you *The Price Is Right.*

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## 7) Don't Play With It ? You'll Go Blind

Well, do I really need to go into this one? All I know for sure is that I am not blind today. What I will never know for sure is whether she believed it, or if it was just meant to scare the hell out of me. When you invest in the financial markets it is very easy to lose sight of what your intentions were in the first place. Getting caught up in the hype, getting sucked in by the emotions of fear and greed, and generally being confused by the multitude of options available, can **cause you to lose your focus. Always go back to the basic principle you started with which was to grow your small pile of money into a much larger one.**

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## Putting It All Together

My Dad once taught me a very basic principle: **KISS: Keep It Simple Stupid** This is one of the best investment lessons you will ever receive. Too many people try to outsmart the market to gain a very small, fractional, increase in return. Unfortunately, they wind up taking on a disproportionate amount of risk which, more often than not, leads to negative results. **The simpler the strategy is, the better the returns tend to be. Why? There is better control over the portfolio. Designing a KISS portfolio strategy will help ensure that you don't get blinded by continually playing with your portfolio and losing sight of what your original goals were in the first place.**

1. **Decide what your objective is:** Retirement, College, House, etc.
2. **Define a time frame** to achieve your goal.
3. **Determine how much money you can** realistically put toward your goal each month.
4. **Calculate the amount of return needed** to reach your goal based on your starting principal, the number of years to your goal and your monthly contributions.
5. **Break down your goal into milestones that are achievable.** These milestones could be quarterly, semi-annual or annual and will help make sure that you are on track to meet your objective.
6. **Select the appropriate asset mix** that achieves your required results without taking on excess risk that could lead to greater losses than planned for.
7. **Develop and implement a specific strategy to sell positions** in the event of random market events or unexpected market downturns.
8. **If this is more than you know how to do** ? hire a professional who understands basic portfolio and risk management.

There is obviously a lot more to managing your own portfolio than just the principles that we learned from our Mothers. However, this is a start in the right direction, **and if you don't believe me?? just ask your Mother.**