Striving for Financial Independence

An Honors Thesis (ID 499)

By

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OUTLINE

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Introduction

The United States has the highest per capita income ever known to mankind, but yet, 95 percent of the citizens who reach the age of 65 are flat broke. Out of every 100 people who reach the "golden years," only two are financially independent, 23 must continue to work, and 75 are dependent on their friends, relatives, or charity.¹

These people have lost the money game. The money game is not like other games because people cannot choose whether to play or not to play. It is the only game that is offered. The intelligent thing to do is to learn the rules and play to win because financial insecurity can cause several years of angry frustration. Perhaps there is an educational void in our society about this subject. Millions of dollars are spent each year to teach youths how to equip themselves for a vocation so that they can earn the money necessary to provide a living; however, they are not taught what to do with the money once it is earned.²

A false idea that has been passed down through the ages is that "money is the root of all evil." It is actually the misuse of money that brings about corruption and human suffering, not money itself. If used in the proper manner, money provides the necessary food, hospitals, churches, shelters, and clothes that are needed.
When attempting to become financially independent, a person seems to have three choices. First, he can try to make it fast with only a slight hope of success. Secondly, he can try to make it slowly with a rather good chance for success. Or third, he cannot try at all and join the 95 percent who end up flat broke.3

With a reasonable amount of time, the ability and willingness to earn an average wage, the discipline to save a small portion of earnings, and the intelligence to apply some basic principles, anyone can become financially independent. It does not take brilliance or luck, but discipline and the ability and willingness to make your dollars work as hard for you as you worked to earn them.

One of the services that most public accounting firms offer is a tax service. Because a client's tax liability is dependent upon accounting records, public accounting firms are particularly qualified to provide a variety of tax preparation and planning services. As an accounting major and as an individual interested in investment options, this writer has chosen to investigate investment alternatives that can lead to financial independence. In this thesis, the importance of goal setting, the possible instruments and investments available to meet these goals, the advice of experts for different individuals in different circumstances, and the reasons for success and for failure will be covered.
Goal Setting

Retiring in financial dignity is actually more than a goal. It is an obligation that is owed to yourself and to others such as your family, your community, and other taxpayers. The financial planning part is personal because each and every person is unique. Each person has different financial obligations, different assets, a different tax bracket, and a different temperament.

Financial Periods

Your lifetime can be divided into three financial periods. The first is the "Learning Period," and it lasts about the first 25 years of your life. Time, money, and effort invested in education during this time can increase your productivity. Studies show that a college graduate earns between $250,000 and $300,000 more during his lifetime than a person with only a high school diploma.

The second period in your life is the "Earning Period." If you earn $1500 per month for 40 years between the ages of 25 and 65, nearly three-quarters of a million dollars will pass through your hands. Venita Van Caspel, president of the brokerage firm Van Caspel and Company, Inc. and a nationally known speaker and radio-TV personality, has developed a very simple secret for the accumulation of wealth. The secret is made up of 10 small words, "A part of all I earn is mine to keep."4 In other words, this means that you must pay yourself first.
The third period of your life is your retirement years. These will either be the "yearning years" or the "golden years" depending on the decisions made during the earning years. Social security was never meant to provide financial independence. It was only meant to provide a base upon which to build.5

Sources of Income

There are three sources of income upon which to draw. The first source is from working, the second source is your money at work, and the third source is charity. Since you are only capable of working so much and charity rarely brings happiness, you must use your intelligence to assure that there is sufficient money at work to retire in financial dignity.6

Amount Needed at Retirement

You may ask yourself, how much money will I need at retirement time? Several factors must be analyzed before a rough figure can be estimated. You must consider the number of years you have before retirement, what inflation will have done to the cost of living, what standard of living you desire, and what rate of return you will be receiving on your funds. To calculate the amount of income you will need at retirement, you must determine the amount you would need if you were retiring today and adjust it for inflation. The following chart shows rates of inflation from 2½ to 12 percent and years until retirement from 10 to 35. To
Table 1-1.
Additional Income Needed (in Dollars) at Retirement, with Various Inflation Rates

<table>
<thead>
<tr>
<th>Years until retirement</th>
<th>2 1/2%</th>
<th>3%</th>
<th>3 1/2%</th>
<th>5%</th>
<th>8%</th>
<th>10%</th>
<th>12%</th>
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<td>1.34</td>
<td>1.43</td>
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<td>1.80</td>
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<td>1.38</td>
<td>1.47</td>
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<td>1.89</td>
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<tr>
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<td>1.51</td>
<td>1.62</td>
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<td>4.89</td>
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<td>1.45</td>
<td>1.56</td>
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<tr>
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<td>1.60</td>
<td>1.73</td>
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<td>1.60</td>
<td>1.75</td>
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<td>4.32</td>
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<td>1.81</td>
<td>1.99</td>
<td>2.65</td>
<td>4.66</td>
<td>6.73</td>
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<td>1.86</td>
<td>2.06</td>
<td>2.79</td>
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<td>1.92</td>
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<td>2.93</td>
<td>5.44</td>
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<tr>
<td>23</td>
<td>1.76</td>
<td>1.97</td>
<td>2.21</td>
<td>3.07</td>
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<td>2.03</td>
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<td>3.23</td>
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<td>9.85</td>
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<td>2.09</td>
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<td>26</td>
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<td>7.40</td>
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<td>2.53</td>
<td>3.73</td>
<td>7.99</td>
<td>13.11</td>
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<tr>
<td>28</td>
<td>2.00</td>
<td>2.29</td>
<td>2.62</td>
<td>3.92</td>
<td>8.63</td>
<td>14.42</td>
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<td>2.05</td>
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<td>2.71</td>
<td>4.12</td>
<td>9.32</td>
<td>15.86</td>
<td>26.75</td>
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<td>2.43</td>
<td>2.81</td>
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<td>17.45</td>
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<td>2.50</td>
<td>2.91</td>
<td>4.54</td>
<td>10.87</td>
<td>19.19</td>
<td>33.56</td>
</tr>
<tr>
<td>32</td>
<td>2.20</td>
<td>2.58</td>
<td>3.01</td>
<td>4.76</td>
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</tr>
<tr>
<td>33</td>
<td>2.26</td>
<td>2.65</td>
<td>3.11</td>
<td>5.00</td>
<td>12.68</td>
<td>23.23</td>
<td>42.09</td>
</tr>
<tr>
<td>34</td>
<td>2.32</td>
<td>2.73</td>
<td>3.22</td>
<td>5.25</td>
<td>13.69</td>
<td>25.55</td>
<td>47.14</td>
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<tr>
<td>35</td>
<td>2.37</td>
<td>2.81</td>
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<td>5.52</td>
<td>14.79</td>
<td>28.10</td>
<td>52.80</td>
</tr>
</tbody>
</table>

calculate, subtract your age from 65 to get the number of years until retirement, and then read across to the rate of inflation you feel is safe to assume. This will give you a figure that shows how many dollars you will need then to equal the value of one dollar now.

For example, assume that you would need $1000 per month if you were retiring today, that you are age 40, that you
plan to retire in 25 years at age 65, and that inflation will average 5 percent. Your adjustment factor would be 3.39. Multiply 3.39 by $1000 and you would need $3390 per month in 25 years to obtain the same housing, food, and clothing as you do with $1000 today. Inflation will probably continue even after you retire, so you should put aside an additional amount to cover for this continued inflation.

What goal should you set for yourself to have a monthly income of approximately $3390 per month at age 65? If you assume that you will not receive a pension from your company, how much capital will it take to produce $3390 per month without denting the principal? If an 8 percent yield is used, you would need $508,000 of capital

\[(3390 \times 12 = 40,680 \times 0.08 = \$508,500)\].

That is a lot of capital. But remember, you have 25 years before you need this amount, and if you decide to use a portion of the principal each month, this capital amount can be reduced considerably. The goal, however, is to make it last at least as long as you do.

A formula that Venita Van Caspel uses regularly is:

"Time and money and American free enterprise = opportunity to become financially independent."

One of the most important ingredients for financial independence is time. It does not take much money to compound to a tidy sum if you have time for it to grow. It is important to start as early as you can to reach your predetermined goal. A savings of $50 a month for 10 years at 12 percent is less than $25 a month
for 15 years at 12 percent. Money is the ingredient that comes each payday or from generous forefathers. You must save and let your money grow. The rate of return that you receive will be determined by how skillfully you put your money to work in our free enterprise system. Here is a chart to show how much of a difference each additional percent can make.

Table 1-2.
$1200 Per Year at Varying Rates Compounded Annually—End of Year Values

<table>
<thead>
<tr>
<th></th>
<th>5th</th>
<th>10th</th>
<th>15th</th>
<th>20th</th>
<th>25th</th>
<th>30th</th>
<th>35th</th>
<th>40th</th>
</tr>
</thead>
<tbody>
<tr>
<td>1%</td>
<td>6,182</td>
<td>12,680</td>
<td>19,509</td>
<td>36,686</td>
<td>43,231</td>
<td>43,359</td>
<td>50,492</td>
<td>59,250</td>
</tr>
<tr>
<td>2%</td>
<td>6,369</td>
<td>13,402</td>
<td>21,168</td>
<td>39,739</td>
<td>49,205</td>
<td>49,654</td>
<td>61,192</td>
<td>73,932</td>
</tr>
<tr>
<td>2%</td>
<td>6,561</td>
<td>14,169</td>
<td>22,988</td>
<td>43,211</td>
<td>58,063</td>
<td>58,803</td>
<td>74,731</td>
<td>93,195</td>
</tr>
<tr>
<td>4%</td>
<td>6,760</td>
<td>14,983</td>
<td>24,990</td>
<td>37,162</td>
<td>51,974</td>
<td>69,993</td>
<td>91,917</td>
<td>118,592</td>
</tr>
<tr>
<td>5%</td>
<td>6,962</td>
<td>15,848</td>
<td>27,188</td>
<td>41,662</td>
<td>60,135</td>
<td>83,713</td>
<td>113,803</td>
<td>152,208</td>
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<tr>
<td>6%</td>
<td>7,170</td>
<td>16,766</td>
<td>29,607</td>
<td>46,791</td>
<td>69,787</td>
<td>100,562</td>
<td>141,745</td>
<td>196,857</td>
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<tr>
<td>7%</td>
<td>7,383</td>
<td>17,740</td>
<td>32,265</td>
<td>52,638</td>
<td>81,211</td>
<td>121,287</td>
<td>177,495</td>
<td>256,332</td>
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<tr>
<td>8%</td>
<td>7,603</td>
<td>18,774</td>
<td>35,188</td>
<td>59,307</td>
<td>94,744</td>
<td>146,815</td>
<td>223,322</td>
<td>335,737</td>
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<tr>
<td>9%</td>
<td>7,827</td>
<td>19,872</td>
<td>38,403</td>
<td>66,918</td>
<td>110,788</td>
<td>178,290</td>
<td>282,150</td>
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<td>8,059</td>
<td>21,037</td>
<td>41,940</td>
<td>75,602</td>
<td>129,818</td>
<td>217,131</td>
<td>357,752</td>
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<td>11%</td>
<td>8,295</td>
<td>22,273</td>
<td>45,828</td>
<td>85,518</td>
<td>152,396</td>
<td>265,095</td>
<td>454,996</td>
<td>774,992</td>
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<tr>
<td>12%</td>
<td>8,538</td>
<td>23,586</td>
<td>50,103</td>
<td>96,838</td>
<td>179,200</td>
<td>324,351</td>
<td>581,355</td>
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<tr>
<td>13%</td>
<td>8,786</td>
<td>24,976</td>
<td>54,806</td>
<td>112,164</td>
<td>211,020</td>
<td>397,578</td>
<td>741,298</td>
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<tr>
<td>14%</td>
<td>9,043</td>
<td>26,454</td>
<td>59,976</td>
<td>124,521</td>
<td>248,799</td>
<td>488,084</td>
<td>948,807</td>
<td>1,835,890</td>
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<tr>
<td>15%</td>
<td>9,304</td>
<td>28,018</td>
<td>65,660</td>
<td>141,372</td>
<td>293,654</td>
<td>599,948</td>
<td>1,216,015</td>
<td>2,455,144</td>
</tr>
<tr>
<td>16%</td>
<td>9,572</td>
<td>29,679</td>
<td>71,910</td>
<td>160,609</td>
<td>346,905</td>
<td>726,194</td>
<td>1,560,032</td>
<td>3,286,173</td>
</tr>
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</table>

For example, an increase of 1 percent from 8 percent to 9 percent for 25 years means a difference of $16,044.
$100,000 as a Minimum Goal

According to one financial expert, a minimum goal for an estate should be $100,000. The following table gives the approximate annual investment required to equal $100,000 at the end of a specified period based on varying rates.

Table 1-3
Approximate Annual Investment Required to Equal $100,000 at the End of a Specified Period--Varying Rates

<table>
<thead>
<tr>
<th>Rate</th>
<th>5 Yrs</th>
<th>10 Yr</th>
<th>15 Yr</th>
<th>20 Yrs</th>
<th>25 Yrs</th>
<th>30 Yrs</th>
<th>35 Yrs</th>
<th>40 Yrs</th>
</tr>
</thead>
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<tr>
<td>1%</td>
<td>19,380</td>
<td>9,464</td>
<td>6,151</td>
<td>4,497</td>
<td>3,506</td>
<td>2,768</td>
<td>2,378</td>
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<tr>
<td>2%</td>
<td>18,841</td>
<td>8,954</td>
<td>5,669</td>
<td>4,036</td>
<td>3,061</td>
<td>2,417</td>
<td>1,961</td>
<td>1,624</td>
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<td>3%</td>
<td>18,290</td>
<td>8,470</td>
<td>5,220</td>
<td>3,613</td>
<td>2,663</td>
<td>2,041</td>
<td>1,606</td>
<td>1,288</td>
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<td>4%</td>
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<td>8,009</td>
<td>4,802</td>
<td>3,229</td>
<td>2,309</td>
<td>1,714</td>
<td>1,306</td>
<td>1,011</td>
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<td>5%</td>
<td>17,236</td>
<td>7,572</td>
<td>4,414</td>
<td>2,880</td>
<td>1,966</td>
<td>1,433</td>
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<td>6%</td>
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<td>7,157</td>
<td>4,053</td>
<td>2,656</td>
<td>1,720</td>
<td>1,193</td>
<td>846.59</td>
<td>609.58</td>
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<td>16,254</td>
<td>6,764</td>
<td>3,719</td>
<td>2,280</td>
<td>1,478</td>
<td>989.39</td>
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<tr>
<td>8%</td>
<td>15,783</td>
<td>6,392</td>
<td>3,410</td>
<td>2,024</td>
<td>1,267</td>
<td>817.36</td>
<td>537.34</td>
<td>357.42</td>
</tr>
<tr>
<td>9%</td>
<td>15,332</td>
<td>6,039</td>
<td>3,125</td>
<td>1,793</td>
<td>1,083</td>
<td>673.06</td>
<td>425.31</td>
<td>271.52</td>
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<tr>
<td>10%</td>
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<td>924.37</td>
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<td>14,467</td>
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<td>2,618</td>
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<td>787.41</td>
<td>452.67</td>
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<td>12%</td>
<td>14,055</td>
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<td>1,239</td>
<td>669.64</td>
<td>369.97</td>
<td>206.41</td>
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</tr>
<tr>
<td>13%</td>
<td>13,658</td>
<td>4,805</td>
<td>2,190</td>
<td>1,070</td>
<td>568.67</td>
<td>301.83</td>
<td>158.00</td>
<td>87.29</td>
</tr>
<tr>
<td>14%</td>
<td>13,270</td>
<td>4,536</td>
<td>2,001</td>
<td>963.69</td>
<td>482.32</td>
<td>245.86</td>
<td>126.47</td>
<td>65.36</td>
</tr>
<tr>
<td>15%</td>
<td>12,898</td>
<td>4,283</td>
<td>1,828</td>
<td>848.82</td>
<td>408.64</td>
<td>200.02</td>
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<tr>
<td>16%</td>
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<td>4,043</td>
<td>1,669</td>
<td>747.16</td>
<td>345.92</td>
<td>165.25</td>
<td>76.92</td>
<td>36.52</td>
</tr>
</tbody>
</table>

For example, an annual investment of $1,083 at 9 percent for a 40-year-old person will grow to be $100,000 by the time he retires 25 years later at age 65.

A very simple rule that can be used without tables is The Rule of 72. This rule answers the question: How long does
it take $1 to become $2 at various rates of return? You simply divide 72 by the interest rate to receive the number of years necessary to double your money. For example, it takes 8 years for your money to double at 9 percent (72 / 9% = 8 years).

More than likely your timetable does not fit exactly into 5 year time periods, and the amounts of money that you have to invest do not fit into even blocks of $100 per month. The following tables will allow you to be more exact in your programmed plan. The "Future Value of $1" chart gives you the sum to which $1 of principal will accumulate at the indicated interest rates compounded each period for the given number of periods. The "One Dollar Per Annum Compounded Annually" chart gives you the sum to which one dollar per year, paid at the beginning of each year, will accumulate at the indicated interest rate compounded annually for the given number of years.
<table>
<thead>
<tr>
<th>Period</th>
<th>Future Value of $1 at the End of n Periods: ( FVIF_{k,n} = (1 + k)^n )</th>
</tr>
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<tr>
<td>3</td>
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<td>4</td>
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<tr>
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<td>1.1100</td>
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<tr>
<td>15</td>
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</tr>
<tr>
<td>36</td>
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*FVIF > 59.999.*
Table 1-5
One Dollar Per Annum Compounded Annually

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<tr>
<th>End of Year</th>
<th>5%</th>
<th>6%</th>
<th>8%</th>
<th>10%</th>
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</table>
Determining Amount You Will Have By Retirement

Assuming that you have 9 years before retirement, that you have $15,500 you can put to work in a lump sum, and that you can save $210 per month or $2520 per year, you can figure the amount that you would have by the time you retire.

Using the Future Value Chart, you would go down to 9 years and across:

<table>
<thead>
<tr>
<th>At 8 Percent</th>
<th>At 10 Percent</th>
<th>At 12 Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>$15,500</td>
<td>$15,500</td>
<td>$15,500</td>
</tr>
<tr>
<td>X 1.9990</td>
<td>X 2.3579</td>
<td>X 2.7731</td>
</tr>
<tr>
<td>$30,985</td>
<td>$36,547</td>
<td>$42,983</td>
</tr>
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</table>

From Chart 1-5:

<table>
<thead>
<tr>
<th>At 8 Percent</th>
<th>At 10 Percent</th>
<th>At 12 Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>$2,520</td>
<td>$2,520</td>
<td>$2,520</td>
</tr>
<tr>
<td>X 13.4866</td>
<td>X 14.3974</td>
<td>X 16.5487</td>
</tr>
<tr>
<td>$33,986</td>
<td>$36,281</td>
<td>$41,703</td>
</tr>
</tbody>
</table>

In 9 years at 8 percent you would have $30,985 and $33,986 or $64,971. At 10 percent you would have $36,547, and $36,281 or $72,828. And at 12 percent you would have $42,983 and $41,703 or $84,686.

Conquering Inflation

Inflation is a fact of life that you must learn to accept and to protect against or you will suffer its consequences. During the years between 1940 and 1983, the dollar held its own in only two years. By placing your savings in a "guaranteed" savings account, you are a gambler, and if the past is an indicator of what the future will bring, you are "guaranteed" to lose.
Inflation tends to reward those who owe money, not those who pay cash. You can and should have cash, but you will want to have a large amount of assets invested in hard assets. To win the inflation game in years ahead, you will have to be leveraged in this way. Your assets must be primarily in investments whose prices can rise as fast as the general price levels at each stage of the inflation cycle.

Since the government is the chief creator of inflation, you must watch the government policies closely to determine advance warnings of the amount of inflation that the government will be creating. This will come in cycles, and understanding these cycles will be fundamental in determining investment success. The movement of the inflation rate will affect the price of everything that is owned or purchased—stocks, mutual funds, bonds, real estate, gold, and currencies. 17

Government policy drives the economy and is the creator of all cycles. The policy cycle has its roots in the inflation-unemployment trade-off. Programs are constantly designed to reduce unemployment or to curb inflation and back and forth. But if it is necessary to choose between the two, full employment will be the victor and the result will be more inflation. 18

To take advantage of the transfers that inflation makes in wealth, a total portfolio should be developed that will allow you to be positioned efficiently at the proper time to beat inflation. This portfolio must maximize after-tax
return balanced against a level of risk that provides you with peace of mind. To beat inflation, you must have the right combination of assets. This means that you must be flexible and alert and that you must realize that nothing can be put away in your safe-deposit box and forgotten. Products that are offered are constantly changing, the government is constantly making new regulations, and interest rates are always changing.

To decide whether inflation is going to accelerate or decelerate, the money supply is a reliable indicator. Acceleration in the money supply leads to an acceleration in the inflation rate.¹⁹

Using Financial Planners

One of the first rules for successful investing is diversification, and one of the best ways to diversify is to stand back from your money. But many times you are too close to your hard-earned money to make rational decisions. This is where a good financial planner who has experience with a variety of investments and who is not so emotionally involved can be of great help.

With new ways to invest, new types of life insurance, and changes in income and estate taxes, many people are looking for financial advice. One group of advisors typical of the profession includes those known as certified financial planners, or CFP's. They are generalists. This means that they are knowledgeable in the fields of stocks, bonds, limited
partnerships, insurance, taxes, retirement, wills, estates, and household budgeting. The initials CFP mean that the person is a graduate of the College for Financial Planning in Denver and adheres to a professional code of ethics.20

You should be sure to choose a planner who is interested in working with people that have your level of income and assets. Some planners, usually in the larger cities, cater only to wealthy clients. The best way to find a planner suited to your needs and philosophy is through word of mouth. You can also get a list of CFP's in your area by writing to the Institute of Certified Financial Planners, 9725 Hampden Avenue, Denver, Colorado 80231.21

This writer interviewed Ron Rentschler, a certified financial planner with Thomson McKinnon Securities Inc. of Fort Wayne, Indiana about setting up a financial plan. He said that the first things that he needs to have are a balance sheet and an income statement. From these he can tell the assets that are available and the disposable income that can be used for investing. He also requests a personal financial planning guide to be completed disclosing family information and financial objectives. From these he maps out a plan that he feels will match the individual's income, objectives, needs, and temperament, and he tries to do away with any preconceived notions about certain investments. He is a general financial planner and does not charge for his plans. He is paid for his services through the commissions on the products that he sells. He is an example of just one
of many types of financial planners who can help set up a financial plan geared toward financial independence.22

Setting Up a Plan Based on Personal Needs

Some analysts say that singles, working couples, and new families might well come out ahead today by renting a place to live and building up their assets first through other investments such as stocks, bonds, and commercial real estate. David Biehl, executive vice president of Bailard, Beihl and Kaiser, a financial-counseling concern in San Mateo, California, believes that the appeal of home ownership as an investment is being minimized by relatively high mortgage rates and only stable to slowly rising home values.

Gary Shilling, a New York economic consultant, believes that is especially true for young people in lower tax brackets, since their deductions for mortgage interest and property levies will have little effect in offsetting income taxes.23

Not everyone agrees with this theory, however. One stock advisor insists "basics come first, and that includes adequate life insurance, savings for an emergency, and owning a home. Then come other investments." He also believes that the psychological satisfaction of owning your own home remains strong.24

Alexandra Armstrong, head of Alexandra Armstrong Advisors in Washington, D.C., says that young people should seek out funds that emphasize long-term growth rather than current income through dividends.25 This idea was also stressed by Ron Rentschler, a financial planner for Thomson McKinnon, who
said that the long-term results should be studied, not just the short-term as people have done in the prosperous periods of late.\textsuperscript{26} This approach may build a bigger nest egg over the long run and cut current taxes. One widely offered hint is to invest in a fund that is part of a group of affiliated funds and allows easy switching of investments from one to another.\textsuperscript{27}

Many financial experts are now also advising young people to consider putting the maximum allowed into an IRA before considering other investments. They say that even if the cash might be needed before age 59\(\frac{1}{2}\), the tax penalty for early withdrawals from an IRA is not all that severe. Arthur Young and Company figures that for people in the 30 percent tax bracket, an IRA deposit earning 10 percent a year will outperform a similar taxable savings plan even if the deposit is withdrawn after only 6 years. In the 50 percent bracket, a 10 percent IRA does better after only 5 years. Although changing tax rates and interest yields may vary the results, the basic point is one and the same: You should not let the tax penalty scare you away.\textsuperscript{28}

For many couples, one of the biggest challenges may be saving for their children's college educations. If you are willing to start giving money to your child ahead of time, you can get Uncle Sam to pay part of the bill. The tactic is to shift funds for investment to the child so that the returns are taxed at his or her low rate, if at all. This allows the funds to grow faster. A simple way to shift the tax is
to make a gift of money or securities and open a custodial account for the child at a bank or brokerage firm.²⁹

Parents saving for a child's education might consider deep-discount bonds that will mature about the time that the money will be needed. These issues sell at well under the maturity value in order to compensate for the fact that the interest rates have risen since the bonds were originally issued. Another possibility may be a tax deferred annuity issued by an insurance company. The money put in will grow tax-free until withdrawn. Payments may begin when the child begins college. The trick in saving for college is to estimate what will be needed and put away enough each year to gradually reach that goal.³⁰

Whatever your goals for the future are, the money that you have to invest, the risks that you are willing to take, the return on investment that you are seeking, and the liquidity that you feel is necessary, your portfolio of investments will differ from everyone else's. Your plan will be unique to your own needs. Following are a description of some of the more popular investment tools available and some of their strengths and weaknesses.

**Instruments and Investments Available to Meet Goals**

**Stocks**

Stocks have been a good hedge against inflation in the long run although not necessarily in the short run. According to a comprehensive study done by the Center for Research and
Security Prices at the University of Chicago, an investment in a random cross section of stocks on the New York Stock Exchange over a 40 year period would have given you an average rate of return (before taxes) of approximately 9.3 percent a year compounded annually.31

Timing in the market will be the key to success. You will want to be invested in stocks when, in your best judgment, the rate of inflation is less than the rate of inflation that the general public expects. Unless inflation is decelerating or about to decelerate, you will want to be out of the stock market and into short-term money instruments, such as the money market funds. One clue is when short-term rates are higher than long-term rates. Also, there will be more bearish predictions (downward predictions) about stocks than bullish recommendations (upward predictions). In more general terms, stocks can help you beat inflation if you remember that they do best when inflation is decelerating and often do poorly when it is accelerating.32

Successful investing is a skill that you must learn yourself or hire the professionals to do it for you. To be successful in the stock market, you must know how to use the mass network of facilities available to your for trading securities. The four largest exchanges are the New York Stock Exchange, the American Stock Exchange, the Pacific Stock Exchange, and the Mid-West Stock Exchange.33

There is a lot of information available to you on stocks and you should investigate before you invest. Standard and
Poors Reports are a good source of some general information. The Wall Street Journal, Business Week, Barrons, and Financial Trends can also supply you with some information.

Temperament of the investor is very important and must be considered before making any investment, because no matter how well an investment fits a financial objective, if the investor is uncomfortable with it, it is not right for him, and he may abandon it before it has time to achieve the desired goal. Investing in the stock market is a risky business and the possible risks and rewards must be weighed against each other. One major advantage that stocks have over some other investments is that long-term capital gains (those over one year and one day) are only taxed at 40 percent. They also provide the greatest potential for gain (or loss).

Mutual Funds

If you do not have the time, training, temperament, and money necessary to diversify your holdings, Venita Van Caspel recommends that you put professional money managers to work for you.34

There are two ways to obtain professional management. If you have a large amount of funds to invest, you may qualify for private professional management through an investment advisory service. There are some that will accept accounts as small as $50,000 for a fee of 1 percent of the net assets per year. Most of the top services will not accept an account less than $300,000. If the amount that you have for
investment is less than $100,000, you should consider using public professional management through the investment medium of the investment company trusts, commonly called mutual funds. "Mutual" means that you may mutually benefit from pooling your resources with others. A mutual fund should do for you what you would do for yourself if you had sufficient time, temperament, training, and money. 35

The Investment Company Act of 1940 provides that a mutual fund may not have more than 5 percent of its assets in any one company, nor more than 10 percent of the outstanding shares of one company. Because of this regulation, you know that any mutual fund portfolio should have at least 20 stocks in it and also that none of the 20 will represent more than 10 percent of the outstanding shares of that company. This in itself insures a fair degree of diversification. 36

Minimum purchase requirements for mutual funds are small, usually $250 to $500, although some require initial purchases of $1,000 or more. Shares are redeemable at any time. 37 You can choose from hundreds of funds designed to satisfy varied investment goals, such as long-term growth in value, additional income, or tax-exempt earnings. As with any investment that you make, however, you will have to make the final choice in terms of your needs, preferences, and expectations about the economy. The chart below depicts the risk/reward potential of various mutual funds.
THE RISK/REWARD POTENTIAL OF VARIOUS MUTUAL FUNDS
This chart gives you a general idea of some basic types of mutual funds. Remember that an individual fund's actual performance depends upon the management and the changing economy.

<table>
<thead>
<tr>
<th>Fund Type/Purpose</th>
<th>Risk Factor</th>
<th>Buy/Sell Advice</th>
<th>Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>AGGRESSIVE GROWTH (high capital gains)</td>
<td>Volatile</td>
<td>Buy on rising stock market; consider selling in falling market, or buying more at lower rates and staying in for the long haul.</td>
<td>Very limited, if any.</td>
</tr>
<tr>
<td>GROWTH (long-term capital gains)</td>
<td>Less volatile than aggressive growth funds.</td>
<td>Buy through dollar cost averaging over long term; seek widely diversified portfolio.</td>
<td>Limited.</td>
</tr>
<tr>
<td>GROWTH AND INCOME (long-term capital gains plus income)</td>
<td>Medium</td>
<td>Don't buy when interest rates are rising if portfolio contains many bonds; seek wide diversification.</td>
<td>Limited if fund stresses growth; more dividends paid if fund stresses income.</td>
</tr>
<tr>
<td>INCOME (steady income)</td>
<td>Medium, but can be higher if interest rates rise sharply.</td>
<td>Compare to yields from money funds before buying.</td>
<td>Can be high.</td>
</tr>
<tr>
<td>AGGRESSIVE INCOME (high income)</td>
<td>More volatile than regular income funds.</td>
<td>Buy when interest rates are falling.</td>
<td>Varies.</td>
</tr>
<tr>
<td>MUNICIPAL BOND (tax-favored income)</td>
<td>Medium, but can be higher if rates rise sharply.</td>
<td>Look for high-rated bonds with long maturity.</td>
<td>Federal taxes exempt; sometimes local, too.</td>
</tr>
<tr>
<td>MONEY MARKET (liquidity and income)</td>
<td>Minimal</td>
<td>Buy when interest rates high and/or volatile; consider selling when rates dropping.</td>
<td>Current market rate.</td>
</tr>
</tbody>
</table>

A good place to look to find out how well the funds you like have performed in good and bad years is in Forbes magazine's yearly late-August issue. Money magazine also ranks the performance of mutual funds in their November issue.
These are excellent sources of information that can be found in just about any library. After reviewing the issues, you may want to write to each of the best-performing funds that met your investment objectives and ask for a prospectus. Then study the prospectuses to find out what each fund can do for you.

A recent New York Stock Exchange study compared 22 million investors who owned only common stocks with 9 million investors who owned mutual funds. It contrasted the "stock only" investors with the fund investors and found:

1. Fund investors are better educated: 65 percent are college graduates while only 50 percent of the "stock only" investors are college graduates.

2. Fund investors are the wealthiest clients: 23 percent have portfolios of more than $25,000 vs. 15 percent of the other clients.

3. Fund investors are the highest income clients: Nearly one-half have incomes of $15,000 (1978 figures) vs. only one-third of the other clients.

4. Fund investors are the most active clients: One-fourth make more than six transactions per year vs. only one-tenth of other clients.39

Mutual funds offer some valuable characteristics that may contribute to accomplishing financial independence. Some of these are (1) diversification, (2) constant supervision, (3) convenience, (4) dollar-cost averaging, (5) easy record keeping, (6) exchange privileges, (7) professional management,
(8) ease of estate settlement, (9) check-a-month plans, (10) performance, (11) management during probate, and (12) financial objectives to meet yours.

Dollar-Cost-Averaging

There may not be an infallible way to invest in the stock market, but there is one way that comes closer than any others. It is called dollar-cost-averaging. Instead of trying to time the "highs" and "lows" for purchases, a fixed amount of money is invested on a regular schedule which allows the principal of dollar-cost-averaging to work for itself. This plan does not require brilliance or luck, but the discipline to save and invest over a long period of time.

When you use dollar-cost-averaging, you invest the same amount of money in the same security at the same interval over a long period of time, with the assumption that the stock market will fluctuate and eventually go up. These two things have always occurred in the past. Venita Van Caspel says that "if your real reason for investing is to make money, dollar-cost-averaging is the most infallible way that I have found to approach the market."

Money Market Funds

The standard money market fund looks like a checking account that pays high interest, but unlike a bank account, money fund shares are not insured. It is conceivable then that you could lose cash as a result of fraud, mismanagement, or economic calamity, but it is not likely. Burton Berry, a
San Francisco investment advisor and publisher of the No Load Fund-X newsletter, says, "The money funds are not the same, but from the very safest to the least is really a very small difference." While millions of Americans have invested billions of dollars in money funds since the first one was started in 1972, only 2 funds have run into trouble. With no loss to shareholders, one was bailed out by its parent company, and the other was salvaged by a merger with a healthy fund.

It is usually not wise to pick the money fund currently paying the highest yield. You should rather look for funds with yields that are consistently above average. You should check a fund's performance over at least the past year. Many funds will provide this information if you just ask for it. One way to compare various funds is to consult Donoghue's Money Fund Directory ($15 from P.O. Box 540, Holliston, Massachusetts 01746), which gives the performance record of 166 of them for the past 2 years. The directory also gives the funds' minimum investment requirements, fees, and investment policies.

Individual Retirement Accounts

Most workers look forward to the day when they can retire and enjoy their senior years in comfort. It is for this reason that Congress authorized the Individual Retirement Account (IRA) in 1974.
Anyone who is receiving a salary, wages, or commissions is entitled to open an IRA. Once an IRA is established, you can contribute up to the lesser of 100 percent or $2000 of your earnings to your IRA each year. All taxes on those contributions plus any interest, dividends, or capital gains which accumulate in the account are tax deferred until withdrawals begin during your retirement years. If your spouse is employed, he or she can set up a separate IRA for up to $2,000. If your spouse is not working, you can make an additional contribution of $250 raising the maximum to $2250. The contributions may be divided between the two accounts in any ratio provided no more than $2,000 is contributed into either account.

IRA plans can also be helpful to workers who retire early as well as those who leave an employer and receive a lump sum distribution from a qualified plan. If you do receive a lump sum distribution, you can avoid current taxes on all or any portion of that distribution by placing the desired amounts of cash or securities in an IRA Rollover program within 60 days from the day you receive the assets.

You have until April 15 (or your extended federal tax filing date) of the year following your intended plan year to establish an IRA and make your contribution. There is no limit as to how large your IRA assets may eventually grow.

Investments eligible for IRAs include CDs, stocks, bonds, mutual funds, annuities, limited partnerships, and Treasury securities to name the principal ones. Only life insurance,
precious metals, collectibles, and investments bought on margin are off limits. The choice of offerers of IRAs is also varied: commercial banks, savings and loans, credit unions, mutual fund companies, and insurance and brokerage firms.49

Distributions of your earlier contributions, plus all accumulated interest, dividends, and capital gains can begin when you reach age 59½ but must begin no later than age 70½. If you withdraw money prior to age 59½, you are subject to an IRS penalty tax of 10 percent plus payment of your ordinary income tax on the amount withdrawn. The only exceptions to the age 59½ rule occur in the event of disability (benefits can begin immediately, without penalty, regardless of age) or death (in which case benefits are payable to your named beneficiary).50

Distributions are taxed only as you actually receive them, which is generally after retirement when you are in a lower tax bracket. When you reach age 65 you are entitled to an additional personal exemption. If your spouse is age 65 and you are filing a joint return, the four exemptions will lower your tax bracket even further. If you take distributions over a period of years, your tax liability may be reduced considerably. If you choose to receive a lump sum distribution at retirement, you may be eligible for five-year income averaging.51
Tax Deferred Annuities

About a million individuals own annuity contracts, a sort of reverse insurance where you pay the insuring company a large chunk of money up front—the average is $20,000—and the company agrees to dole out regular amounts over a period of years, usually until you die.\textsuperscript{52} Annuities can create a nest egg that is free from market risk and also protected against taxation and inflation. Annuities have proven beneficial for individuals whom the price spiral has pushed into higher tax brackets and for those who demand maximum safety as well as generous yields from their investment commitments.

Fixed annuities guarantee that premium values can only increase. Returns compound and accumulate faster tax free without price risk, and they are guaranteed available at any time to the contract owner. The variable annuity features returns tied in part to the performance of common stocks or other assets rather than fixed guarantees.

Annuity guarantees are extremely significant, coming as they do from legal-reserve life insurance companies. By state law such companies are required to maintain reserves sufficient to satisfy all possible claims against them. A brochure from Kidder, Peabody and Co., "Annuities--Better than CDs or Money Funds?" states,

Just as FDIC insures T-Bills and some CDs, insurance companies are subject to stringent state regulation and must maintain reserves at least equal to the full cash surrender value of their contracts, including interest.\textsuperscript{53}
A conventional (fixed) tax deferred annuity's guarantee of principal and interest is superior to that of uninsured corporate or municipal bonds and money market funds; it is also more sweeping than the protection given to those who deposit their money in commercial banks and thrift institutions where agencies of the U.S. Government insure passbook or other savings accounts only up to a specified amount. 54

Annuities also offer a high degree of security. To illustrate, an investor in the 50 percent bracket would have to run an inordinate market risk to achieve a 22 percent return simply to match the 11 percent tax-deferred earnings guaranteed free of all market risk. The following table gives a comparison of equivalent taxable returns for various tax brackets.

<table>
<thead>
<tr>
<th>Taxable Income Joint Return</th>
<th>Maximum Tax Bracket</th>
<th>To Match a Tax-Deferred Accumulation of 9% Before Paying Uncle Sam You Must Earn 10%</th>
<th>To Match a Tax-Deferred Accumulation of 11% Before Paying Uncle Sam You Must Earn 11%</th>
</tr>
</thead>
<tbody>
<tr>
<td>$29,000</td>
<td>30%</td>
<td>12.86%</td>
<td>14.29%</td>
</tr>
<tr>
<td>35,200</td>
<td>35%</td>
<td>13.85%</td>
<td>15.38%</td>
</tr>
<tr>
<td>$45,800</td>
<td>40%</td>
<td>15.00%</td>
<td>16.67%</td>
</tr>
<tr>
<td>60,000</td>
<td>44%</td>
<td>16.07%</td>
<td>17.86%</td>
</tr>
<tr>
<td>$85,600</td>
<td>48%</td>
<td>17.31%</td>
<td>19.23%</td>
</tr>
<tr>
<td>109,400</td>
<td>50%</td>
<td>18.00%</td>
<td>20.00%</td>
</tr>
</tbody>
</table>

Variable annuities afford many of the advantages offered by the conventional annuities, with one significant difference. The value of variable annuities can fluctuate, down
as well as up—since premium payments are invested at the owner's direction in assets that can vary in value. Variable contracts guarantee payments at regular intervals in the future, but the amounts, however, can vary up or down, depending on the performance of the separate portfolios. In brief, the investor is trading a wholly guaranteed result for the chance to obtain an inflation hedge. 56

Annuities are desirable on several accounts. They have (1) earnings on the principal (your premium payment), (2) earnings compounded on earnings, and (3) earnings on the money that otherwise would have been paid in taxes. Unlike an investment in stocks, bonds, etc., a fixed tax-deferred annuity guarantees that you can recoup at least your original investment anytime you want it. 57

Typically, commission-free annuities impose a modest early withdrawal fee (e.g., 6 percent during the first year of the contract) that scales down annually (i.e., 6 percent, 5 percent, 4 percent, etc.) should one need to cash in the annuity before the agreed-upon date. 58

While annuities are tax-favored, they are not tax-exempt. You will naturally have to pay taxes on accumulated earnings once you start to withdraw them—presumably in retirement when you have dropped into a lower tax bracket. All cash withdrawals attributed to investments made after August 13, 1982 are taxable first as ordinary income until the withdrawal amount is actually a return of the original investment which is non-taxable. 59
The new Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982 has also added a 5 percent tax surcharge on withdrawals that are earnings, not investments. This applies to individually owned annuities if the contract has not been in force for at least 10 years and was not purchased prior to August 13, 1982. This penalty is waived for annuity owners age 59½ or older as well as for those who become disabled or die. Also exempt are equal payments extending at least 60 months after the contract starts to pay regular payments that you have selected and those distributions allocated to purchases made before August 13, 1982.60

**Municipal Bonds**

When establishing a diversified investment portfolio, tax-exempt bonds can serve as the defensive portion. A municipal bond is an interest-bearing debt obligation of an American state, local government, or agency. "Interest-bearing debt" means that municipal bonds pay interest, usually every 6 months; they are "debt" rather than "equity" in that owners of municipal bonds—as with other bonds—do not own a share of the issues. Almost all municipal bonds pay interest which is a fixed percentage of par value.61

The fact that municipal bonds are issued by the states or their subdivisions is the reason why interest on municipal bonds is exempt from Federal income tax. There has been talk from time to time about Congress eliminating the tax-free privilege inherent in municipal bonds. Federal taxation
of state and municipal bonds does, however, require an amend-
ment to the constitution ratified by 2/3 of the states.
Heavily indebted states are not likely to look favorably
on such an amendment.62

There are two general types of municipals, general obli-
gation bonds and revenue bonds. These are distinguished
by their source of payment. General obligation bonds, usu-
ally called G.O.'s, are payable from all tax sources avail-
able to the issuer, and the issuer pledges its full faith
and credit to payment of principal and interest. Revenue
bonds are payable from the net revenues of public enterprises
derived from user charges. Examples include airport revenue
bonds from rents and landing fees, bridge and turnpike bonds
from tolls, housing bonds from mortgage repayments, electric
and water bonds from service charges, stadium bonds from
leases and university bonds from tuition or dormitory rent-
als.63 Unless he has expert advice in separating sound ones
from shaky ones, an investor should avoid revenue bonds backed
only by revenues from a special project, such as a generating
plant or a hospital. These bonds carry higher interest rates
than general obligation bonds and revenue bonds backed by
financially secure corporations, but they are riskier.64

In general, investors in brackets above 35 percent can
usually earn equal or better after-tax yields on municipals
than on corporate bonds of similar maturity and rating.
This is because tax-exempt municipals afford yields about
two-thirds those available on taxable issues of comparable
quality and maturity. Given this relationship, the tax tables turn in your favor when you reach the 35 percent bracket.

Most bonds are quoted in terms of their "yield," which is the overall annual return to the investor expressed as a percentage of the dollar price paid. Except for floating rate bonds, once a bond has been offered, the interest rate (or "coupon") does not change. Yield and price vary inversely on all fixed income securities: the higher the yield, the lower the price. A bond that yields more than its coupon rate is selling at a discount from par. A bond that yields less than its coupon is selling at a premium over par. 65

Quotations of the bid and ask price of certain dollar bonds are published with other market quotes in many daily papers, including the Wall Street Journal. There is no equivalent of the New York Stock Exchange for municipal bonds because there are too many different bonds available to list each efficiently. 66

The difference between the bid and ask price is called the spread which varies with the amount of bonds traded, the quality, the amount of time until maturity, and the relative volatility of the market. You do not pay a sales charge or commission separate from the price of a bond; that comes out in the spread. 67

Municipal bonds can serve as the defensive portion of a diversified portfolio, defensive because municipal bonds
offer a low level of risk. Other investments offer the possibility of greater rewards but with an increase in risk. Virtually any investor with $5,000 to invest in bonds is at or near a tax bracket where municipals offer an after-tax yield advantage over taxable debt. Also, next to U.S. government bonds, municipal bonds have been the safest of all securities. Moody’s Investor Service and Standard and Poor each rate municipal bond obligations according to relative investment qualities.  

**Tax Shelters**

The term tax shelter, or more appropriately, tax-advantaged investments, refers to an income and/or appreciation-oriented investment that offers the opportunity to convert part of your tax bill into assets which generate even more current or future assets. Conceptually, tax shelters represent a policy decision by Congress to attract private capital to socially desirable ventures involving above-average risk.

Tax shelters are investments that offer the opportunity for profit as well as a means of reducing current tax liabilities. A quality tax shelter gives you a chance to create and accumulate assets with dollars that would otherwise go for taxes. In most cases, anyone whose income is subject to taxation of 50 percent by the federal government should consider tax shelter investments.

The laws and Internal Revenue Service regulations covering tax shelters are complex. Also, judicial and/or
administrative decisions may change the ground rules on short notice. Careful professional planning is necessary to realize the maximum benefits of programs, so you should consult competent tax and legal counsel before committing funds to any tax-sheltered investment.

As a tax shelter participant you are not investing in conventional securities like common stocks or bonds, but as a rule, you become a member of a limited partnership. A limited partnership is an association between a general partner with managerial expertise in a particular industry (real estate, oil and gas drilling, equipment leasing, or agriculture, for example) and a group of limited partners with capital to invest. 71

Under most circumstances, financial exposure is limited to the amount of investment, plus a share in any undistributed profits. Furthermore, in a limited partnership, all profits, losses, and tax benefits flow through to individual participants on a pro-rata basis. The partners themselves, not the partnership, pay any taxes due on earnings. They also utilize the expenses and losses typical of an enterprise's formative years to offset ordinary income on their tax returns. Interests in limited partnerships are often difficult to sell in a hurry and thus virtually all tax shelters require some sacrifice of liquidity. 72

Oil and gas programs, along with real estate projects, rank among the most favored and popular tax shelters. Equipment leasing and agricultural programs also rate well. 73
Real estate investments can encompass apartments, office buildings, hotels, shopping centers, retail stores, industrial plants, warehouses, mobile home parks, and other properties that generate rental income. Apartments are a very popular commitment principally because Congress has accorded residential income-producing real estate incentives beyond tax benefits available on all other real property.\(^7\)

The total return on oil and gas investment is derived from the write-off of 80 to 90 percent of the initial investment, subsequent cash flows over a 10 to 15 year period, and tax sheltering of that cash flow from depletion deductions. Oil and gas is actually one of the few remaining true tax shelters because investors can deduct 15 percent of the gross revenues as a "percentage depletion" even though no costs are actually incurred.\(^5\)

There are three basic approaches to drilling in oil and gas shelters. They are exploratory programs (higher risk drilling), development programs (which drill only near producing wells in proven fields), and balanced programs, which are now the most prevalent (that offer both exploratory and developmental participations).\(^6\)

The typical program for the small investor is the public partnership—with a minimum investment of $5,000 or $10,000. Total funds raised range from $3 million to sometimes as high as $100 million. Studies have shown that smaller funds are better because larger funds become unmanageable. The
quality of the sponsor, however, is the most important factor in selecting a fund.\textsuperscript{77}

Making tax-sheltered investments does not necessarily complicate filing income tax returns. The management of a tax-sheltered partnership normally provides each investor, by March of each year, with the information he needs to file his personal income tax return by April 15. This information is normally easy to integrate into one's own return.\textsuperscript{78}

Many stock brokerage firms maintain special departments to service the needs of clients who require tax shelters. They provide investors with a prospectus fully describing each opportunity, its objectives, risks, tax aspects, etc. Management is a very critical factor.\textsuperscript{79}

**Advice of Experts for Different Individuals in Different Circumstances**

**Developing a Systematic Program**

For the beginner the stock market can be confusing and the consequences of a bad buy are dreaded. But financial advisors reassure that anyone can be a successful investor. With a regular, systematic program and endurance, anyone can accumulate a surprisingly large portfolio during his working days.

When you are just starting out, your program should not be too complicated or ambitious. You should start out slow and build. One of the most common mistakes that people make is not following sequential steps when they invest.
A systematic investing program should proceed through four stages: accumulating a rainy day fund in a money market account; dipping a toe in the stock market through mutual funds; picking a portfolio of common shares; and finally balancing your holdings by adding bonds, income-oriented limited partnerships, or options. As with any system developed, some time will have to be spent keeping records.80

The top priority should be to put money away for emergencies. You should figure on putting away 3 months after-tax pay, and expect that it could take two to three years to save it up. It takes a lot of self-control, especially at first, but sometimes simply changing the exemptions on your withholding form can help you find the money faster.81

Initially, the best place to put your cash is in a money market fund. Many funds require a minimum investment of $1000 to $2500, but then you can add whatever you can afford each month. It must be a minimum of $25, however. Money market funds pay a much higher percentage than savings accounts do, and they allow you to write checks, usually for $500 or more.82

Once you have an emergency reserve, you are ready to start investing any other money that you accumulate. Novices should begin with some type of mutual fund because it provides exactly what beginners need—professional management and a large portfolio for diversification. To get information about funds, you may want to talk to a stockbroker. He will more than likely recommend a load fund which carries
a commission of 8½ percent. You can also subscribe to a monthly newsletter to find out about funds sold directly to investors without the commission or load.83

After you have been buying shares in mutual funds for awhile, there will probably come a time when you will want to have your own stock portfolio. It is best to leave your emergency fund intact and to continue with your mutual fund program, thus only buying stock with additional investment funds. If you are afraid of losing money, you may want to consider joining an investment club. In addition to assistance from others in the group, you get advice from the National Association of Investment Clubs. Its manuals and regular monthly magazine can help you become a smart buyer.84

As a novice you would probably only be able to afford one or two stocks at first. Ultimately you should own about ten, which is small enough to be manageable and large enough for diversity. "You should have a rainbow of stocks," says William Sandvig, president of the Minneapolis-St. Paul Council of Investment Clubs.85

Most of your assets should be tucked away in a regular long-term investment program. Eventually, however, you may want to consider adding bonds, income-oriented limited partnerships, or options. Financial planners are numerous and most investors can afford them. They typically charge $75 an hour and need 4 hours to analyze your situation and offer recommendations.86 An investment that is especially popular with planners is the limited partnership, or tax shelter,
particularly in real estate, producing oil wells, and, lately, cable television. Sound shelters (and many are not) are favored by investors in high brackets.

For the beginner, the best bet is to confine investments to mutual funds and stocks until you have become very knowledgeable. If your approach is steady and sensible, you do not have to make spectacular decisions, and a systematic program does not need to be terribly time consuming.

How you divide your money is a personal decision that you must make depending on your circumstances, your goals, and your outlook for the coming year. Following are examples of some people in typical situations and the ways that financial advisors recommend that they allocate their portfolios in 1984. All of them are assumed to have enough life and other insurance. Although two couples are in high enough tax brackets to warrant buying traditional tax shelters, their immediate needs prevent them. Their investments have still been structured to provide some tax advantages.

Investment Plan for Mid-Life Couple

These people are in their forties with two children, ages 17 and 12. Together they earn $55,000. They want to invest the $100,000 that they have accumulated to build an education fund for their children.

Fifty percent in common stocks with 3/4 of them being blue chips (companies known nationally for the quality and wide acceptances of its products and services, and for its
ability to make money and pay dividends) or growth mutual funds, and the remainder in more aggressive issues or mutual funds aiming for maximum capital gains.

Forty percent in interest-free loans to the children to be invested in discount Treasury notes whose maturities correspond with the bills for college tuition.

Ten percent in money market funds or other short-term money market securities.

Investment Plan for Divorced Mother

The divorced mother is 35 and has custody of her children, ages 8 and 5. Between her salary and child-support payments, she has income of $25,000. She wants to be able to save enough for the down payment on a house, but she only has $15,000 from her divorce settlement to invest. Her biggest need is to be able to tap her funds immediately in case of an emergency.

Fifty percent in money market funds or other short-term money market securities.

Fifty percent in growth-and-income mutual funds.

Investment Plan for Newlywed Couple

The newlyweds are in their late twenties and earn $45,000. They have only $2500 to invest and need to develop a savings habit. One painless way to save is through corporate stock purchase plans or mutual funds that automatically deduct money every month from their paychecks or checking accounts. Once they have $2,000 or $3,000 in their money
market fund, this two-income couple may want to assume more risk and invest everything else in common stocks. They can afford to take chances now because they are young and can earn back any losses.

Seventy percent in common stocks, with 3/4 in mutual funds aiming for maximum capital gains, and the rest in growth funds.

Thirty percent in a money market fund or other short-term money market securities. 89

Investment Plan for Older Couple

The older couple are in their mid-fifties and are planning for his retirement in 10 years from a $65,000-a-year job. They are at the point where they should invest every available dollar--presently that is $150,000--for the most growth that they can achieve in the shortest time with the least risk.

Sixty percent in blue-chip common stocks or growth mutual funds.

Thirty percent in floating-rate municipal bonds or short- and intermediate-term discount bonds that will mature as they start to need the money to live on.

Ten percent in an oil and gas income program. 90

The common denominator of success seems to be that the successful person has formed the habit of doing things that failures do not like to do. Successful people do the things that they do not like to do in order to accomplish the things
that they want to accomplish. Successful people are motivated by the desire for pleasing results. Failures search for pleasing experiences and are satisfied with results that can be obtained by doing things that they like to do.

Reasons for Failure

What are the main reasons for failing to win the money game? (1) The greatest cause for failure is the lack of a well-defined goal and a step-by-step plan to accomplish that goal. (2) A second cause of failure is a lack of self-discipline. The secret of financial independence is not brilliance or luck but the discipline to save a part of all that you earn and put it to work. (3) Procrastination is a deadly enemy to success. If you have a sufficient amount of time, you do not need as large an amount of money to combine with American industry or other major areas of investing. (4) Lack of persistence is another major cause of failure. If you experience a temporary setback, you must not give up. (5) A fifth reason for failing is that decisions are reached, if at all, very slowly and then changed frequently and quickly. Men who succeed reach decisions promptly and change them, if at all, very slowly. (6) Overcaution is as bad, if not worse, than lack of caution. Not to win is a sin, but not to try is a tragedy. (7) Lack of concentration of efforts is another reason for failing. You must apply your intelligence, use your ability to acquire knowledge, and give attention to details and timing. If you cannot, will not, or do not have
the ability to do these things, then you should put professionals to work for you. (8) In investing, you cannot desire something for nothing. The important factor is not what it costs but what it pays. (9) Do not let indifference or plain laziness keep you from acquiring the facts essential to making good judgments. Information is available about almost any subject you need. (10) Lack of capital does not need to be a problem. Build up a nest egg of capital and do it while you are young. Money gives you options. (11) Finally, do not let others overinfluence you when you are reaching decisions about your money. Opinions are cheap.

Reasons for Success

What are the reasons for success? Why do some people succeed? (1) The most important reasons is that they have a plan. Success in money management can be predicted, but you must have a plan and follow that plan. (2) A good attitude brings about good results. A fair attitude, fair results. You will shape your own financial life by the attitudes that you hold each day. Everything in life operates on the law of cause and effect. You must produce the causes, and the rewards will take care of themselves. (3) Luck may or may not be involved. More times than not, luck is when preparedness and opportunity get together. If you are prepared, you will become lucky. (4) Successful people come in all shapes and in all sizes. They have different backgrounds, intelligence, and education. The one thing that they all have in common is that they expect more good out of life than
bad, and they expect to succeed more often than fail. (5)  
Money is important. But money is the harvest of your production. The amount of money that you receive will be in direct relation to the need for what you do, your ability to do it, and the difficulty of replacing you.  

Summary  
How much you can earn, however, is not as important as how much you are allowed to keep. As Judge Learned Hand, the famous New York State jurist said,  
Anyone may so arrange his affairs that his taxes shall be as low as possible: He is not bound to choose that pattern which best pays the treasury. Everyone does it, rich and poor alike, and all do right; for nobody owes any public duty to pay more than the law demands.  
Tax avoidance is using your intelligence. Tax evasion is illegal.  
All that you need is a plan and the courage to arrive at your destination, knowing in advance that there will be problems and setbacks, but also knowing that nothing can stand in the way of completing your plan if it is backed by persistance and determination. Money must be kept in its proper place though. It is a tool with which you can live better and see more of the world around you. Money is necessary in your life, but too much emphasis on money can reverse the whole picture and make you the servant and it the master. You do want to have money and the things that it can buy, but continually check to make sure that you have not lost the things that money cannot buy.
ENDNOTES


2 Ibid.

3 Ibid., p. xiv.

4 Ibid., p. 4.

5 Ibid., pp. 2-7.

6 Ibid., pp. 7-8.

7 Ibid., pp. 8-9.


9 Ibid., p. 15.

10 Ibid., pp. 18-19.

11 Ibid., pp. 19-20.

12 Ibid., p. 21.


14 Van Caspel, pp. 26-27.

15 Ibid., p. 33.

16 Ibid.

17 Ibid., p. 42.

18 Ibid.

19 Ibid., p. 43.


21 Ibid.


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"Investment Advice for Young People," p. 71.


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Ibid., pp. 174-175.

Ibid., p. 181.


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Ibid., p. 60.


48 Ibid., p. 3.


50 IRA Retirement Planning Questions & Answers, p. 4.

51 Ibid., pp. 4-5.


53 Ibid.


55 Ibid.

56 Ibid., p. 3.

57 Ibid., p. 4.

58 Ibid., pp. 4-5.

59 Ibid., p. 5.

60 Ibid., p. 7.


62 Van Caspel, p. 348.


66 Ibid., p. 11.

67 Ibid.
68 Ibid., pp. 11-12.
70 Ibid.
71 Ibid., p. 2.
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79 Ibid.
81 Ibid., p. 83.
82 Ibid.
83 Ibid., p. 84.
84 Ibid.
85 Ibid.
86 Ibid., p. 86.
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89 Ibid.
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91 Van Caspel, pp. 424-428.
92 Ibid., p. 428-431.
93 Ibid., p. 345.
94 Ibid., p. 431.
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