



FUNDAMENTALS OF INVESTING

Lawrence J. Gitman • Michael D. Joehnk

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PREFACE

During the past decade, major changes have taken place in both the process of investing and the range of investment vehicles available to individual investors. New exchanges such as the Chicago Board Options Exchange have opened. New mechanisms for making transactions such as discount brokerages and electronic telequote machines have come into widespread use. New vehicles such as listed options and gold certificates, and new concepts such as beta and portfolio theory, have been introduced. It is our belief that most existing investments books do not deal adequately with these and many other exciting advances in the field. Instead, they continue to concentrate on the institutional aspects of the investments world of yesterday. In contrast, *Fundamentals of Investing* reflects the state of the art for individual investors, providing up-to-date coverage of modern investment practice in easy-to-read language.

Our principal aim in writing this book was to satisfy the needs of the individual investor who is actively developing and monitoring an investments portfolio. *Fundamentals of Investing* presents techniques, vehicles, and strategies for implementing investment goals in light of risk-return tradeoffs. Key factors in determining the makeup of the individual portfolio are emphasized throughout.

Before writing this book we examined all available investments texts. With the help of our publisher, we posed a group of questions concerning these texts to a number of instructors who currently teach the course. Their responses, along with feedback obtained from our own students, guided us in developing the structure of the text. Drafts of the manuscript were reviewed by practicing investment counselors and teachers, whose opinions and suggestions helped us greatly in shaping the final form of the text.

ORGANIZATION

Fundamentals of Investing is divided into six parts, each of which begins with a schematic diagram of the world of investments. The diagram highlights the subject of the part to show where it fits into the overall picture.

Part One examines the investments environment in general and introduces several important concepts that will be discussed throughout. Individual chapters are devoted to the investments environment sources of investment information and advice, the concepts of return and risk, and the process of establishing an investments program.

Part Two is devoted to common stock. It includes a discussion of various procedures for analyzing investment potential, such as valuation, technical analysis, and efficient markets.

Part Three considers various fixed income securities, emphasizing the role each might play in an individual investment portfolio.

Part Four discusses speculative vehicles—rights, warrants, puts and calls, and the commodities and financial futures markets. It also examines two speculative investment strategies—margin trading and short selling.

Part Five looks at a variety of investment vehicles, including mutual funds, real estate, gold, antiques, art, annuities, and limited partnerships.

Part Six deals with the investment administration process. It explores quantitative and applied aspects of portfolio management in a nontechnical fashion.

CONTENT FEATURES

Several key features of this text help to distinguish it from other texts currently on the market:

1. The text is organized around a structural model that interrelates investment principles and practices.
2. The concepts of risk and return and portfolio diversification lie at the heart of the book and are integrated throughout the discussion of all investment vehicles.
3. Emphasis is placed on assessing one's financial position, establishing personal financial goals, considering insurance and retirement needs, and recognizing important tax factors, as they relate to investment plans.
4. A wide variety of new investment vehicles is covered in detail without slighting the traditional forms of common stocks and bonds.
5. The treatment of portfolio management has been made as practical and realistic as possible.
6. All references to structural and legal changes in the investments environment and procedures are as up-to-date as possible.
7. Each chapter contains two or more boxed essays that describe real world situations, problems, or controversies, with an emphasis on practical aspects of investing. These brief text inserts place concepts within specific, real world contexts and make learning easier and more enjoyable.

PEDAGOGICAL FEATURES

Each part of the book opens with a brief content overview, and each chapter begins with a list of objectives that sets forth key points to be covered. Up-to-date tables and figures, accompanied by full descriptive captions, further facilitate the learning process, as do the boxed inserts. Each chapter ends with a list of key terms, 15 or more review questions and problems, and succinct case problems that illustrate the investment decision-making process in action. A list of selected readings for each chapter directs the investor to recent articles from such publications as *Barron's*, *Changing Times*, *Financial World*, *Forbes*, *Fortune*, *Money*, and *The Wall Street Journal*.

End-of-the-book material includes two appendixes—an annotated listing of readily available sources of investment information and a set of interest tables—and a glossary of key terms, with a reference to the chapter in which each is first used.

For those who are teaching the course, a comprehensive *Instructor's Manual* has been prepared. The manual contains the following materials for each chapter:

1. Some general comments on chapter coverage and suggestions for its effective use, along with suggestions for lectures and discussions.
2. Detailed answers to all end-of-chapter review questions and case problems.
3. A battery of 40 multiple-choice and true-false questions for that chapter, which may be used for quizzes and exams.

READABILITY

We feel that instructional prose for investment courses need not be stiff and colorless. In *Fundamentals of Investing*, we have used an informal style and personal, conversational tone wherever possible. Since the subject of investments is inherently interesting and dynamic, it surely does not deserve to be cloaked in “banker’s gray” rhetoric. A variety of headings and visual devices also enhance the presentation. Finally, careful attention was given to ensure that the reading level is consistent throughout the book.

ACKNOWLEDGMENTS

Many people gave us their generous assistance during the development of *Fundamentals of Investing*. The expertise, classroom experience, general advice, and reassurance of many colleagues and practitioners were invaluable. Reactions and suggestions from students in California, Texas, and Oklahoma sustained our belief that a fresh, informative, and teachable investments text could be created.

In particular, we wish to thank four people who made significant contributions to the formation of this text. They are Samuel C. Hadaway of the Texas Public Utility Commission, who contributed to the chapter on analysis and valuation of common stock; Terry S. Maness of Baylor University, who contributed to the commodities and financial futures chapter; Arthur L. Schwartz, Jr., of California Polytechnic State University, who contributed to the chapters of real estate, gold, and other tangible investments, annuities, limited partnerships, and investment administration; and Robert J. Doyle, Jr., of The American College, who prepared the appendix on sources of investment information and advice.

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