Chapter 1

Getting Started with Stocks

Every year, investors pour billions of dollars into mutual funds, especially stock funds. And, every year, investors are shocked by the tax bills those funds generate.

When taxes are considered, the old-fashioned way is better: Buy individual stocks instead. As long as you buy and hold with minimal trading, your tax bill from your investments will be negligible.

THE MUTUAL FUND MINEFIELD

To understand the advantages of buying stocks directly, consider the tax rules governing mutual funds. Federal tax law requires that mutual funds distribute at least 98% of their *ordinary income* and net realized gains for a calendar year within that same calendar year.

ordinary income taxable income that receives no favorable tax treatment.

Suppose, for example, ABC Growth Fund invested $1 million in Microsoft back in the 1980s. Since then it has held on to Microsoft, watching the stock appreciate—and generating no tax obligation.

In the year 2000, concerned about the company's battles with the government, ABC Growth Fund sells its Microsoft stake, which has grown to $20 million.

The company has a long-term gain of $19 million, practically all of which must be distributed to shareholders.

FUNDS CHURN, INVESTORS ARE BURNED

turnover rate
a measure of how actively a mutual fund trades its holdings. A fund with a 100% turnover rate holds each investment for an average of one year before selling it.

Of course, ABC Growth Fund won't have only one sale of its Microsoft stock during the year. More likely, it will have dozens of sales, each of which generates a gain or a loss. (The average stock fund has a *turnover rate* greater than 80%, so a typical mutual fund is a fairly active trader.)

The net trading gains must be distributed annually. If ABC Growth Fund winds up the year with $50 million in net gains and there are 50 million shares outstanding, it will distribute $1 per share.

MANY UNHAPPY RETURNS

Such distributions are taxable to you, whether you reinvest your capital gains distributions and thus collect no cash. That's true even if the fund loses value in a year.

This happens frequently. Indeed, in times of market trouble investors bail out of losing funds, and those investors who stay behind (or buy in shortly before the distribution date) get larger per-share distributions, so they owe more tax.

If you invest after the fund enjoyed big gains but before the distribution, you'll still owe tax on the distribution you receive.

In this example, ABC Growth Fund sells Microsoft and other long-term holdings as well, winding up distributing $1 per share. Suppose you bought ABC Growth Fund at $20 per share just before the $1 per share distribution (which drops the price to $19 per share). You would get $1 per share in distributions, on which you'll owe tax. In effect, you're paying a tax on a return of your own capital.

SHORT GAINS, LARGE PAIN

The Taxpayer Relief Act of 1997 provided a cut in the capital gains tax, and subsequent legislation in 1998 enhanced this tax break. Now, if you hold a stock, mutual fund share, or other investment for more than one year, any gain will be taxed no more than 20% (down from 28%), even if you are in a higher tax bracket.

On the other hand, when you buy mutual funds, net realized gains must be distributed to investors each year. Some distributions will be short-term capital gains, taxable at rates up to 39.6%; only if the fund has held the shares for more than 12 months will shareholders get the benefit of the 20% rate.

It makes no difference whether you reinvest the short-term capital gains distribution; it makes no difference how long you've held the shares of that mutual fund. If you own the fund in a taxable account, you'll owe short-term capital gains tax at rates up to 39.6%. (Any *dividends* passed through to investors also will be taxed at ordinary rates up to 39.6%.)

dividends payments of profit by a corporation to its shareholders.

COSTLY COMBINATION

Most mutual funds are managed to maximize pretax rather than after-tax results, so mutual fund distributions tend to be a mix of short- and long-term gains. Although the end result will vary according to your tax bracket, your state tax situation, and your fund's trading practices, you can expect to pay around 25% of each annual distribution in tax.

Suppose, for example, Jane Jones has $10,000 invested in XYZ Value Fund. In 1999, XYZ posted a total return of 25%. Of her $2,500 return, though, about $1,000 (40%, the industry norm) came to her in the form of distributions. At an effective 25% tax rate, Jane had to pay $250, knocking her actual return from $2,500 (25%) down to $2,250 (22.5%).

Long-term, losing that much in taxes each year can make a huge difference in the wealth you accumulate.

ROLL YOUR OWN

For more control and lower tax, you can buy individual stocks. Trading through a discount broker, costs will be minor: Online trades may be under $10 apiece.

Then, you can just hold on to your stocks indefinitely. You'll owe tax on the dividends you receive, but the average dividend yield on the S&P 500 is around 1.5%. At a 30% tax rate, your tax bill would be a token 0.45%.

CASHING IN

Buy-and-hold is a fine investment strategy, but what if you need to get your hands on some cash? Do you have to sell shares and trigger a taxable gain?

- ✔ If your stocks appreciate and you want to cash in some of your profits, you can borrow up to 50% against the full value of your stocks. The interest you pay likely will be deductible, as an offset to taxable investment interest.
- ✔ Another possibility is to sell off your winners. You can specify which shares you want to sell, choosing those that will generate the smallest tax bill. And you can sell off some losers as an offset, reducing or eliminating your tax bill.

Impact: With some savvy planning you can wind up each year with a net realized loss of $3,000, fully deductible, while you let most of your winners ride.

MISSION: CONTROL

You can do some of the same things with mutual funds that you can do with individual stocks. You can match winners with losers; you can borrow against your funds if they're held in a brokerage account.

However, with individual stocks you're likely to have

more variability from one issue to another, which will provide you with increased flexibility for tax planning. And you'll certainly have more control—you'll realize taxable gains when you choose to do so, not at the whim of some fund manager.

BOLD NEW WORLD

As mentioned earlier, recent changes in tax law lowered the maximum tax on capital gains from 28% to 20% on assets held more than 12 months. These changes created many new opportunities for investors.

Stocks beat bonds—by a wider margin than ever. As an investment, equity is preferable to debt, provided you diversify your holdings and stay in for the long term. Now that the tax on any gains is reduced, stocks look even better.

Impact: Don't rush to switch from stocks to bonds as you near retirement. You're better off keeping your money invested in *equities* and then meeting any cash needs by selling stocks. Changes in the tax law decrease the tax you'll pay when liquidating appreciated securities.

equities ownership interests. Publicly traded stocks are often called equities.

Borrowing to buy stocks or real estate makes more sense. The after-tax cost of borrowing remains the same, while your after-tax gains may be greater.

Suppose, for example, you take a $10,000 margin loan to buy stocks, paying 8% ($800) per year in interest. In a 39.6% tax bracket, deducting the interest on your income tax return will save you $317 in tax, so your net cost will be only $483 per year.

Suppose the stocks you buy go up 10% ($1,000) per year. Under prior law, your net annual gain would have been $720, after paying capital gains tax at 28%; now your after-tax gain is $800 a year.

Retirement plans are good—but not as great. Under current tax law you'll need a commitment to higher returns (perhaps by investing more in stocks) and longer holding periods for investments inside deductible individual retirement accounts (IRAs), 401(k)s, simplified employee pensions (SEPs), and other plans.

marginal tax rate
the rate at which your last dollar (or your next dollar) of income will be taxed. Also known as your tax bracket.

Unfortunately, all money coming out of such retirement plans would be taxed at your top *marginal tax rate* (at present as high as 39.6%), no matter how that income was derived. In essence, you lose the capital gain tax break that exists inside the plan.

Nevertheless, the longer you'll defer taxes, the better a retirement plan will work. Such plans remain particularly effective if you'll have a holding period of 20 years or more.

Tax brackets count, too. If you think you'll be in a lower bracket when you withdraw your money, perhaps after you retire, tax-deferred plans still can be very big winners.

Diversification may come easier. Your portfolio may be overweighted in shares of your employer's stock, stock options, or shares of one company given to you by family members. Selling some of those shares will reduce your exposure to one stock but may generate sizable capital gains.

long-term capital gains
profit from the sale of an asset held more than a year. Under current law, the maximum tax rate is 20%.

Now, rebalancing your portfolio becomes less expensive because you'll owe only 20% on *long-term capital gains*.

Big Break for Small Fry

Here's a vital break for parents of young children:

The tax law also provides a bargain 10% capital gains tax rate. Taxpayers in the 15% income tax bracket pay only 10% tax on capital gains. That includes single filers with less than $25,000 in taxable income (about $45,000, filing jointly).

So here's a winning strategy: If you're cashing in appreciated securities to pay college bills, give them to your children before selling.

As long as your kids are older than 13, they likely can sell the shares and pay tax at just 10%; then they can use the net proceeds for college. You and your spouse can give away $20,000 worth of assets per year, per recipient, with no gift tax consequences.

Elder Shelter

Another super strategy:

If you're helping to support elderly parents, give them appreciated securities instead of cash. Again, your parents may be able to sell and pay tax at a bargain 10% rate.

NOW FOR THE NEGATIVES

Unfortunately, there's a downside to lower rates on long-term capital gains: The *basis step-up* has come down in value.

At your death, shares you bequeath get a step-up in *basis* to current value. For example, suppose you have a portfolio of stocks you bought for $100,000, now worth $500,000. If you die tomorrow and your son inherits, his basis in those shares moves up to $500,000. He can sell them for $500,000 and owe no capital gains tax on the $400,000 profit.

The value of this tax break is smaller now (an $80,000 savings at a 20% rate) than it was under prior law (when the savings would have been $112,000 at a 28% rate).

Formerly, many investors were frozen in place: To get the basis step-up, they held on to appreciated assets until death. Now that this tax break has been devalued, you can take some gains, pay tax at 20%, and reinvest the net proceeds where opportunities seem greater.

Ironically, charitable giving also has been devalued. The same reasoning that applies to basis step-ups also applies to using appreciated assets for charitable gifts. Under the new law, such gifts save 20 cents on the dollar, not 28 cents.

Charitable giving now depends even more on your philanthropic objectives and not as much on tax savings.

basis step-up
a tax break enjoyed by heirs to appreciated property. When you inherit an asset your basis is increased to its value at the owner's death, effectively eliminating the tax on all the gains that were not cashed in.

basis
your basis in an asset is your cost for tax purposes.

DOWNPLAY DIVIDENDS

With all this emphasis on capital gains, what about dividends? Isn't it marvelous to invest in AT&T or Con Edison and receive a check every three months?

Not always. From a taxpayer's point of view, buying dividend-paying stocks is unattractive.

- ✔ Dividends are near historic lows, with the average stock in the Standard & Poor's 500 paying around 1.5%, as of this writing.
- ✔ The dividend income you receive will be taxed as ordinary income, with rates up to 39.6%. If you owe state or even local income tax, you could lose 40% to 45% of your dividends in taxes.
- ✔ That tax is due every year, even if you reinvest your dividends.
- ✔ On the other hand, when a stock you hold appreciates, no tax is due as long as you don't sell.
- ✔ Even when you sell a stock at a profit, federal income tax is capped at 20%, as long as you have held the stock more than 12 months.

BEYOND THE BORDERS

Financial planners and investment advisers routinely recommend some commitment to foreign stocks as part of a diversified portfolio. Thus, some American investors have moved into foreign stocks and stock funds, such as *global funds* or *country funds*.

global funds
investment pools that can invest anywhere in the world, including the United States.

country funds
investment pools that invest in one particular foreign country.

You don't really need foreign stocks, but history shows that there are advantages to diversification. As of this writing, the U.S. market is strong while foreign stocks have been down, but that may not be the case in the future.

As recently as 1990, the U.S. economy seemed to be flat on its back while the Japanese seemed to dominate the world and the Japanese stock market had enjoyed a long boom. Since then, the U.S. stock market has soared while the Japanese market has fallen from 38,000 to 18,000.

UPS AND DOWNS

The Japanese market's 1990s slump of more than 50% can be compared to the U.S. experience in 1929 to 1932,

when our market fell by 68%. Since then there has not been a decline of that magnitude, but the 1964 to 1981 period saw U.S. stocks stagnate.

Throughout that time frame, the annual return on the S&P 500 remained below 7% per year, which failed to keep up with inflation. If American stocks hit another such slowdown in the future, investors may be glad to have some money in other, possibly faster-growing markets.

Indeed, the question is not *whether* you'll invest in foreign economies but *how* you'll invest. If you invest in Coca-Cola or Boeing or almost any major American corporation, you have a stake in foreign business because these companies sell outside the United States. You need to decide if you're content to have that sort of a foreign stake or if you're going to invest some money directly in foreign securities.

EXPANDING THE ENVELOPE: ADRs

To some professionals, the advantage of placing some money outside the United States is not diversification. They look at foreign economies as being more options to consider when you're looking for the best investments. Just as you might be excited by the profit prospects of a certain company, so you may be optimistic about the growth potential of a given country or region of the world. If you invest only in the United States you limit yourself and stand to miss out on some great companies.

Many foreign companies trade in the United States as *American Depositary Receipts (ADRs)*, which resemble common stocks. You can pick your own stocks, selecting among the largest foreign companies, through ADRs. If you select well, you can hold on to your ADRs and enjoy untaxed appreciation until you decide to sell, at favorable long-term capital gains rates.

American Depositary Receipts (ADRs) investments that take the place of shares in foreign companies. ADRs trade in the United States on virtually the same terms as the shares of U.S. stocks.

Bank Notes

How is it possible for U.S. investors to invest in individual foreign companies? U.S. banks hold foreign shares in

custody and issue ADRs, each of which represents one share (or a specified number of shares) of the underlying foreign stock. Citibank, J. P. Morgan, and the Bank of New York are the leading issuers of ADRs.

Over 1,700 foreign stocks from dozens of countries trade as ADRs, with more joining the list all the time. Estimates put the total capitalization of the ADR market at more than $500 billion.

After they're issued, ADRs trade just like U.S. stocks, on the leading exchanges or over the counter. All transactions are handled in U.S. dollars. You collect dividends, if they're paid, and you can sell whenever you wish.

In essence, with ADRs you can control your investments while you avoid the hassles of trading foreign stocks.

POSSIBLE PITFALLS

Nevertheless, ADR investors won't avoid all the perils of investing in foreign stocks. You don't have to exchange currency to purchase ADRs, but their prices are still influenced by fluctuating currency values. The pricing of ADRs reflects the U.S. dollar value of a foreign security, so currency movements will work to your advantage when the currency of the country you're investing in drops in relation to the dollar.

However, the opposite is also true: When foreign currencies strengthen in relation to the U.S. dollar, the value of ADRs drops. For example, if you buy a Japanese company that appreciates 10% in yen but the U.S. dollar declines 5% versus the yen, your gain would actually be 5%: the 10% stock price gain minus the 5% currency loss.

Therefore, you might see a situation in which Telefonos de Mexico, the Mexican phone company, has a flat day in Mexico while the company's ADR rises or declines in the United States by 5% or 10% the same day because of currency movement. Such fluctuations may be reversed the next day, if currency trading goes the other way. Overall, ADRs tend to track the performance of their corresponding foreign securities.

Moreover, some ADRs often are thinly traded, compared with the company's shares in its home market. As a result, it may not be easy to sell them quickly. However, brokers who specialize in trading ADRs can always instruct the custodian to sell the underlying securities as a way of liquidating ADRs.

Countless Tax Collectors

Taxes are another issue that all investors in foreign stocks, including holders of ADRs, have to contend with. The dividends you receive are in U.S. dollars but the payments represent foreign dividends on the underlying stocks.

These dividends, paid in foreign currencies to the custodian bank, are then converted to U.S. currency for payment to ADR investors. Therefore, U.S. investors owe foreign taxes on these dividends.

Suppose, for example, you own 100 shares of an ADR and the company declares a dividend of 50 cents per share. Instead of a $50 dividend, you might receive $42.50 (if 15% is withheld) or even $35.

Paper Chase

In these circumstances, you have a choice. You can deduct the withheld taxes on Schedule A as an itemized deduction or you can file Form 1116 to claim a foreign tax credit. Generally, a credit is more valuable than a deduction, but the effort involved in wrestling with Form 1116 may not be worth the tax savings.

Tax Tip Until the 1998 tax year, the only way to get this foreign tax credit was to file Form 1116—a complicated, time-consuming process. Now, though, most couples with credits of $600 or less can take them directly on their Form 1040, the basic tax return. For single filers, you can avoid Form 1116 if you had no more than $300 worth of foreign tax withheld.

Impact: If you invest in ADRs through a tax-deferred retirement plan, you can't use either the deduction or the credit. In effect, the foreign tax withheld is an outright loss. Thus, you might want to hold any ADRs in a taxable account rather than inside a retirement plan.

EASING YOUR WAY INTO ADRs

Several banks now offer dividend reinvestment plans for ADRs. For example, J. P. Morgan has a shareholder services program (800-749-1687) that includes more than 60 companies, from AMN AMRO of the Netherlands to Zeneca Group of the United Kingdom. If you become a shareholder in one or more of these companies you'll receive all of your companies' news releases, annual reports, proxy materials, and so on without any delays.

The J. P. Morgan program permits investors to purchase shares regularly—weekly, monthly, quarterly, or annually—and thus reap the advantages of dollar-cost averaging. Money for such purchases can be withdrawn automatically from your checking account while dividends can be reinvested regularly as well.

Investors in this program get quarterly statements summarizing all of their ADR activity. In this program, ADRs are held electronically so there are no certificates to store; when it comes time to sell, investors can do so with a toll-free phone call.

Ground Rules

With the J. P. Morgan program, initial purchases must be at least $250; additional purchases may be as low as $50. Investors must pay a $15 enrollment fee for each company they want to buy. Dividend reinvestments are subject to a 5% fee, up to a $2.50 cap, while direct purchases or sales are charged $5 per transaction, plus 12 cents per share (an additional $12 for a round lot of 100 shares).

With this fee structure it probably won't pay to invest only $50 at a time because the $5 fee amounts to a steep 10% of your $50. However, the fee represents a

much lower charge if you invest, say, $500 per transaction. Investing $500 in Barclays Bank, for example, while the ADR trades at $90, would generate a fee of around $5.65 ($5 plus 12 cents each for approximately five and a half shares), slightly more than 1% of the total.

To help investors keep up with ADRs, J. P. Morgan operates a web site (www.adr.com) that contains information on about 400 of the most widely held and actively traded ADRs. The site features a live ticker with current stock quotes, trading volumes, and news updates. Thus, you can stay home and literally have the world of investing at your fingertips.

MARGINAL METHODS

If you think the stock market surge of the 1980s and 1990s will continue, you can increase your profit potential by buying stocks or stock funds on *margin*. Using margin to invest will raise your returns if stocks go up but you'll also lose more if stocks fall. Indeed, during the October 1987 stock market crash many margin investors took painful losses.

margin
the amount an investor deposits with a broker when borrowing money from that broker. Margin can be in the form of cash or securities.

To decide whether to invest on margin, you should know the basics. Margin investors use borrowed money—money that's borrowed from a broker rather than from a banker. Interest rates are pegged to the broker's call rate, which is listed in the daily newspapers.

Most brokers charge anywhere from 0.5% to 2% above the broker's call rate; if that rate is 8%, margin loans would be in the 8.5% to 10% range, with the lowest rates reserved for margin loans over $50,000. Interest, which is payable monthly, is usually subtracted from the equity in your margin account.

leverage
to use borrowed money to acquire assets such as real estate or securities.

TWO FOR THE MONEY

There are, in essence, two ways to buy stocks or stock funds on margin. One way is to *leverage* borrowed money to make the initial purchase. Investing in this manner can

help you get more participation in equities if you're low on cash. For example, if you have only $5,000 to invest you can buy $10,000 worth of stocks, with a margin account.

The other way to buy stocks on margin is to borrow against securities you already hold in your brokerage account. Only securities held in *street name* can be used. This excludes securities you hold personally, in your own name.

street name
the practice of having securities held by your broker rather than keeping the certificates yourself.

THE 50% SOLUTION

Whichever approach you use, margin loans are backed by securities held in your brokerage account. For most securities, the maximum initial margin allowed is 50%: You can borrow $50,000 on margin if you have $100,000 worth of stocks, bonds, and mutual funds. For Treasury bonds held by your broker, the maximum initial margin is 90%.

Although the Federal Reserve and the New York Stock Exchange set the basic regulations, each brokerage firm has its own rules on margin. Some brokers don't allow margin on securities they consider too speculative, such as stocks selling for less than $5 per share. Moreover, you can't use margin in tax-deferred retirement accounts such as IRAs and profit-sharing plans.

LEARNING TO LOVE LEVERAGE

To see how margin can help increase your potential profits, assume you have $100,000 invested in stocks that can be used for margin. If so, maximum margin could boost your holdings to $150,000 worth of stocks.

If those stocks go up by 20% in the next 12 months, you'd have a $30,000 gain, not a $20,000 gain on a $100,000 portfolio. Even if you paid 9% interest ($4,500 on a $50,000 loan), you'd have a $25,500 net gain. Using margin would have boosted your return by $5,500.

CULTIVATING THE TAX CODE

After-tax, the results may be even better.

- ✔ Interest on margin loans can be deducted against taxable investment income.
- ✔ If you're able to deduct your margin loan interest, your real cost of money may be only around 5%.
- ✔ In the meanwhile, any appreciation on the stocks you hold will build up untaxed until gains are realized, and even then those gains may be favorably taxed as long-term capital gains.

The best of all possible worlds, then, would be for you to borrow at 5%, after-tax, to earn 15% or 20%, tax-deferred.

DEPENDABLE DEDUCTIONS

Thus, when you take margin loans for successful stock market investments, you may be using deductible dollars to buy assets where the unrealized appreciation is tax-deferred and likely to be taxed later at favorable rates. The trick is to make sure your margin loans are fully deductible.

How can you do that?

- ✔ Use margin loans solely to buy securities. If you use the loan proceeds to buy a car or pay college tuition the interest won't be deductible.
- ✔ Make sure you have enough *investment income* to offset fully the margin loan interest you pay. Investment income includes interest and dividends but you can elect to include capital gains, too, if necessary.

investment income
dividends, interest, and, in some cases, capital gains.

What if you have to pay $10,000 in margin loan interest and receive only $7,000 in investment income this

year? The extra $3,000 can be carried forward and deducted against investment income in the future.

MARGIN AND MUNICIPAL BONDS DON'T MIX

If you're a margin investor, you also might want to move from tax-exempt bonds to Treasuries because margin interest isn't deductible if it's used to "purchase or carry" municipal bonds or muni bond funds. Suppose, for example, municipal bonds represent 10% of the assets in your brokerage account. If you incur $10,000 worth of margin interest you can write off no more than $9,000.

Even if you keep your munis in a separate account, the Internal Revenue Service (IRS) might contend that the loans helped you carry the bonds. You're required to report tax-exempt interest income on page 1 of your tax return, which makes it easy for the IRS to match up this income with deductions for investment interest that you paid.

STOCKS FALL, BROKERS CALL

Therefore, tax benefits can amplify the benefits of investing on margin—if your stocks go up. Unfortunately, your stocks are not guaranteed to gain 15% or 20%, or any amount at all. When stocks fall, losses are magnified by margin loans, and when stocks fall sharply, investors using margin have to face the prospect of *margin calls*.

margin call
a demand from a broker to add more cash or securities to your margin deposit.

Suppose you borrow $50,000 against your $100,000 portfolio and your stocks fall by 10%, so they're worth $90,000. Your broker likely won't worry much, with $90,000 worth of assets securing a $50,000 loan.

However, if your stocks keep sinking and their value dips to $70,000, your broker will start to be concerned. (Many brokers have an informal rule that a 28% drop on 50% margin accounts will generate a margin call.) When

you get a "house call," your broker will ask you to reduce the outstanding loan balance by putting in some cash or to increase the collateral by putting more securities into your margin account.

What if you don't comply? Your broker can sell your securities and use the proceeds for loan repayment. Usually you'll have a week to meet a market call but that may not be the case in volatile markets. In the 1987 crash many margin investors had their stocks called away before they had a chance to cover.

PROCEED WITH CAUTION

Using maximum (50%) margin may expose you to margin calls because a 28% drop in the price of a stock is not that unusual. If you'd like to be on safer ground, yet still have a chance for extra returns, you can use less margin.

- ✔ Borrow 33% and you won't get a margin call until your account value falls by 50%, which is less likely to happen.
- ✔ At 20% margin, you're not apt to get a call until there's a 70% loss of value—and it's likely you will have bailed out of the stock before that point.

Therefore, if you have a $100,000 portfolio and you borrow to bring it up to $120,000, say, or $133,000, you'll have more market participation without much risk of having to dip into other assets to meet margin calls. You need to monitor your stocks carefully when you buy on margin. Set your lower limits in advance and sell at a loss if your stocks fall to that level.

Impact: Using low margin levels may enable you to keep your loan in place indefinitely. You'd have a long-term loan outstanding at a reasonable rate, after-tax, while you plow the money into stocks, where the long-term returns are likely to exceed your cost of debt service.

RISKY BUSINESS

What are the risks of this strategy? Using margin is still using margin, whether it's 20% or 50%. If your stocks go down, your losses will be magnified. You need a strong stomach to use margin to invest in stocks.

Long-term investors with well-balanced stock portfolios are likely to post superior returns over most time periods. Using margin will enhance any gains because you'll have more stock in play. As long as you can ride out the downs, you'll be in a position to cash in on the ups. If you use margin in moderation rather than to the max, you may well have a smoother path to higher stock market profits.