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## Introduction

Wall Street is only seven blocks long, but is possibly the most important street on Earth. It has fueled some of the greatest economic expansions ever known and it has plunged millions into poverty and ruin. It is home to the oldest, largest and most respected stock exchange in America, the New York Stock Exchange. It is also home of some of the largest financial institutions led by the most cunning and ruthless money mongers in the world. This book is designed to educate you to give you a good shot at surviving the complex and confusing maze that Wall Street uses to extract a profit from the unsuspecting public.

Generations before us have fallen prey to the financial predators of Wall Street. I just finished watching the movie *Cinderella Man* where Russell Crowe portrays the true story of world champion boxer Jim Braddock. What I found fascinating was that both Braddock and his manager, Gould (not to be confused with Jay Gould, the notorious stock manipulator), invested all of their money in the stock market at the end of the 1920s just before the crash that precipitated the Great Depression. They, like many people who were attracted to the stock market at the wrong time, ended up broke. Braddock lost all of his money, a substantial sum, made as a champion boxer in the Roaring Twenties, and ended up living in bread lines and on the dole.

Both these men knew that the promoters behind the fights made all of the money in the boxing industry with the least risk financially and physically. Like most Americans, they lost in the stock market because they lacked the inside connections to the forces behind the scenes, or simply lacked the experience to know when to buy low and when to sell high with the insiders

and manipulators.<sup>1</sup> Neither of them stopped to think that perhaps there exists an industry of promotion driving the stock market that is not only based on hype, but also serves the agenda of powerful individuals in corporate America, the federal government and the equity capital industry also known as the stock market.

These two men who knew so much about boxing knew *nothing* about the stock market. Ironically, while these men suffered financially, a few individuals who were either experienced investors or “inside” and hence, “in the know”, sold out at the top after having bought low years earlier — then lived lives of luxury during the Depression. You don’t hear much about these successful investors, because they didn’t say much, and they certainly did not care to teach the public what they knew.

Times are no different today than when Braddock was struggling to raise a family. We have just witnessed an equities industry caught in scandals of inside trading, false corporate accounting records, and inside executives dumping their option-vested stock on an unsuspecting public as an insider-controlled network of stock brokerages, brokers, mutual funds and the media hyped up the “bull market of the century.” These are just a few of the savage beasts in the stock market jungle that will eat you alive financially if you don’t educate yourself and become savvy.

The recent stock market bust from 2000 to 2003 was just as severe as the crash from 1929 to 1932, except that this time the banking system did not collapse as well; people left their money in the banks and consumerism continued unabated. The settling out of the old crash was just the right time to buy back into the market.

Hopefully, this is the first book you read about the stock market. If so, you have not acquired the baggage of believing the misleading theories of the ivory tower of finance, nor the outright lies from

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<sup>1</sup> An **insider** is a shareholder who owns more than 5% of a publicly traded corporation, or an officer or director of the company. I further class them as **visible insiders** if they have to report their trading to the SEC and **invisible insiders** who are manipulators that buy individually under the reporting requirements without reporting to the SEC yet control a large enough percentage of the float as a group to manipulate the price of the stock over a period of years.

Wall Street. This book teaches you the basics of what the stock market is, what drives it, and will separate myth from fact. The knowledge you will discover in this book is based on my many years of actual investing in the stock market, many years of doctoral-level research, and many years of searching for the answer to my personal question: who really runs things from behind the scenes. The basic information and general wisdom in this book is based on the hundreds of books and articles I have read on the subject; some so obscure that you would probably never know about them if it weren't for me teaching you. This book is the foundation of your stock investing education, and hopefully the first book you read on the subject. Don't ever forget that the stock market is stochastic a word that means unpredictable so if you want a guarantee, buy a toaster!

One last comment: a friend of mine, in reviewing my home study course, told me that I occasionally write very negative things about the stock market and that positive, happy writing and marketing is what really sells. Yet, my friend agreed with the dark portrayal of the forces behind the scenes of the stock market. I thought about this for awhile and decided that if I paint you a "fairytale" picture of these potentially treacherous markets, then that would be unfair to you. You have to know who out there on Wall Street wants to legally rob you of your money or you will never succeed as a stock investor. I am no slick salesman; I am a doctor of finance, a researcher and a seasoned veteran of these markets. Let's get started on this wicked tour of the

Throughout the book, you will see little icons such as:



**TIPS:** to help you make money!



**TRAPS:** that Wall Street uses to ensnare you!

**FACT**

**FACTS:** that are fun to know!



**HUMOR:** to carry you through!

equity markets that really can potentially make you rich! I am your guide – painfully frank, brutally honest and lacking in eloquence, but I *am* your friend in the trenches. I *am* on your side, not theirs, and the information in this book is what you really need to start investing in the stock market.

Here is what Tom Akin, M.I.M., a close friend of mine who is a financial wizard in New York, wants you to clearly understand:

*“When I was invited to write about this book by my good friend Dr. Brown, at first I was hesitant to accept. I asked myself, “Who needs another book on stock market investing?” Almost immediately, I knew the answer: the general investing public.*

*Far from demystifying the ways of the markets, in recent years Wall Street has managed to complicate further the investing process for the average person. For example, as of this writing there are more than 9,000 different mutual funds available to the public — not to mention nearly as many hedge funds. Add to this a bunch of well-intentioned yet disorganized retirement savings legislation brought on by a failing Social Security system, and you have a recipe for disaster. Simply put: it is up to you as an individual to figure out how best to invest your money. If you do not know how or are too lazy to learn, you are in big trouble.*

*This is where Dr. Brown’s direct, yet eye-opening, view on the workings of the markets comes into play. Finally, I said to myself, here is a book which pulls no punches in describing the conflicts of interest, the existence of insider trading, and the many other traps and pitfalls*

*which await the unsuspecting investor entering the concrete jungle of Wall Street. At the same time, Dr. Brown explains the nuts and bolts of investing in a plain speaking, no-nonsense way.*

*You would do well to heed the advice within these pages by adopting the savings and investment techniques Dr. Brown recommends. Undoubtedly you will be the richer for it, both spiritually and financially. Read on and prosper!”*

## Chapter 1

### A Brief History of Stock Investing

Frances was born and raised in a family of Swedish immigrants in a small town near Atlantic, Iowa. As a youth she had the striking good looks of a beauty queen and after her first husband died, she met and fell in love with Leonard, a gentle wealthy dentist, who personally attended to William Randolph Hearst's family. She was 75 when she very happily remarried. Tragically, Leonard died a short time later and Frances received an inheritance of \$85,000



**TRAP:** The history of investing teaches us that a few people in-the-know on the "inside" track do everything they can to buy shares of a company low when the public isn't paying attention and then sell it back high after exciting optimistic rumors about the company have been leaked to the press!

in an account with a nationwide brokerage. The full service broker who managed her account was named Joe. He was known for pushing overpriced stocks on the elderly. Full service brokers have been caught doing this to get inside corporate executives out of large positions in stocks that they know are about to drop.

Frances grew concerned when she stopped getting her Pacific Power and Light dividends. When she called Joe, he reminded her that she had instructed him to sell it and buy Pacific Lighting. She replied, "You told me that you thought it was a good stock. I said I might buy it — not that I would buy it!" She didn't realize that her casual conversation with a financial counselor she trusted — her full service broker — had given Joe the authorization to sell her good stock and buy bad stock. She called him because she didn't know that

he had moved her out of Pacific Power and Light and into Pacific Lighting without her desire. She found out with an empty feeling in the pit of her stomach that he had allowed the stock to drop to nothing without ever calling her even though he had been aware of the problem the whole time. She just took his word for everything and eventually lost it all. A kind, serene and gentle old woman, she tried to complain, but Joe easily held her back. Her son, Del, died of cancer less than a year after Leonard. When Del's wife Barbara became aware of the problem, she had no idea what Frances' rights were, so the \$85,000 just disappeared under the guidance of a full service, Wall Street-endorsed thief. It was finally getting around the valley that Joe was recommending bad stock to other retirees, but since he was selective and targeted only the elderly who did not know their rights, he was never prosecuted.

If her grandson knew then what he knows today, things would be quite different — the Federal authorities don't take too kindly to full service brokers who swindle the elderly. It would still be an upward battle though. The National Association of Security Dealers (NASD) was created by the full service brokerages of Wall Street and is fully endorsed by the federal government. Every time you open an account at a full service brokerage you are forced to arbitrate through a three member NASD arbitration committee due to a mandatory clause in the account open contracts you have to sign to be able to invest in the stock market.

While arbitration is a good way to resolve disputes it should still be administered by neutral organizations, using neutral arbitrators. NASD exists to protect the full service brokerages that created it because they were terrified when the Security Exchange Commission (SEC) was formed in the thirties in the aftermath of severe abuses by full service brokerages. The current system obligates you to deal with a three member arbitration panel. One member, by federal law, has to be a mandatory industry arbitrator who is far from neutral.

There has been a dramatic increase in arbitrations filed with NASD over the past few years, growing from under 5,000 in 1998

to over 9,000 in 2004. Investor representatives have raised concerns about a lack of investor protections and criticized the NASD system for requiring at least one industry arbitrator on three-member arbitration panels. Nonetheless I am confident that Frances' grandson would have found a way to trample the mandatory industry arbitrator on the panel. The nationwide brokerage would have been forced to fully repay the little old woman all the money (and then some) that their licensed broker had swindled. This is because Frances was my grandmother, and a good part of the motivation that lead me to master my

**WALLET DOCTOR SURVIVAL RULE #1**

Do not use a full service broker under any conditions. Take full responsibility for your investing and self-direct your stock buys and sells through an online discount brokerage like tdamericatrade.com, or etrade.com!

understanding of money and earn a Ph.D. in finance.

One promise I make you is that, as my student, I will teach you how to invest in the stock market in such a way

that the full service thieves of Wall Street can never damage your account! Wall Street, however, is also a place that can make you rich. Here's its history:

Centuries ago, investing was utter chaos. The roots of investment trace back thousands of years to ancient **Greece**. Ship captains offered a share of their profits to those in society who were able and willing to share in the risk of financing a trading voyage to faraway lands across the sea. Investing was an "all or nothing" gamble of personal savings. The ship might return with riches (hence the saying "my ship came in") or might be lost at sea and not return at all.

The **Romans** sold stock as well in huge civic construction projects that were beyond the means of a single businessman. Stockholders made handsome profits by investing in companies that built roads and aqueducts for the Roman government. Investment was restricted to Roman citizens. The slaves that built the projects did not benefit.

It wasn't until the 1600s that investing took a giant leap forward when the first shares of stock in a corporation were created in the **Dutch East Indies Company** in Holland. Like

the Greek seafaring merchants before them, the Dutch needed capital for international trade. This investment, however, was different because people bought a stake in the trading company — not in a single ocean voyage or civic project. **Speculation** followed because investors could sell their shares to one another over time without waiting for the “ships to come in”.

The stock price could rise or fall on the faintest of rumors, spreading panic in the world’s first stock exchange. Rising markets created new riches and market crashes wiped investors out. Those who lost money were of the wealthy class of nobles and merchants. They blamed their losses on pushy stock brokers. When the inevitable crash came, the citizens of modest means were not affected because they had not been able to invest. The general attitude of the common citizen was that the upper class were merely wealthy gamblers who had gotten what they deserved — the eventual collapse of the Dutch East Indies Company did not cause panic among the general public.

Investors’ opinions of stock brokers sunk even lower in the 1700s. In Paris, an escaped murderer sold stock. There were also other spectacular instances of fraud in the French stock market. **John Law**, one of the first “executive insiders”, working secretly with stock brokers, swindled the public with worthless shares of stock in his **Company of the West** that he fictitiously claimed owned gold mines in the then French-owned Louisiana Territory. He guaranteed a 40% return and created one of the first recorded public con jobs known as a **Ponzi scheme**. The stock was bid up in a buying frenzy and then crashed, wiping out people who bought too late as the “house of paper” collapsed.

In London, stock brokers lured investors into a Ponzi scheme with stories of a secret device that turned chicken into sheep. Sheep at the time were worth more than chickens and the value of these stocks skyrocketed until people came to their senses and stopped bidding prices up. At astronomical prices the **inside manipulators** started to sell out and the price dropped a little. Inexperienced investors on the inside

track of the manipulation started to worry as they saw the price drop and noticed that, although no business activity had taken place yet, the stock price was still ridiculously high. Pretty soon everyone realized the rises were over but it was too late. Panic set in, and the whole thing fell apart. This is how a market crash occurred then, and still occurs today in a market manipulated by insiders. I explain all of this in greater detail later in this book once I have taught you the vocabulary and concepts you need to know to fully understand the process — understanding this is vital to your investing success.

## WALL STREET

Despite unscrupulous brokers and numerous Ponzi schemes, stocks helped make Europe the colonial and economic powerhouse of the world. Stocks would do the same for the United States of America beginning on a short muddy footpath named Wall Street. **Wall Street** was so named when New York was a tiny colonial outpost. Pilgrims in 1653 built a wall to keep out Indians. About 100 years later, the wall was gone but the path that ran along side it had become the center of New York City's commerce and society. The heart of the young city already had a dark side. On Wall Street was the auction block to sell slaves and the pillory for public humiliation<sup>1</sup>. **George Washington** was sworn in as the first U.S. president on Wall Street in 1789.

Wall Street was where merchants met underneath a buttonwood tree to auction off stocks, mainly in banks and mines, while collecting a commission on every sale. This informal open air stock market lasted until 1792, when 24 merchants signed a document called the "**Buttonwood Agreement**." The pact was intended to avoid government regulation of street auctions and it blocked newcomers from entering the stock brokering business.

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<sup>1</sup> A pillory is a wooden framework erected on a post, with holes for securing the head and hands, formerly used to expose the offender to public derision. Today we have newspapers, radio and television media that serve much the same function when not promoting the inside interests of Wall Street!

This formed the **New York Stock Exchange Board**, where the brokers met inside the **Tontine Coffee House** for two informal stock auctions per day — the public was not allowed to participate. If you wanted to trade in stock, you had to hire a broker to do it. This made the stock market less open and caused the public to be less informed about what was going on inside. In the original open auction system, where everybody could hear everything, people knew a lot more. As is the case even today, what is good for Wall Street is frequently not good for you.

The new coffee house auctions were indoor sessions where auctioneers sold stocks one by one, allowing brokers to regulate themselves to prevent more flagrant forms of fraud and abuse that occurred regularly on the street outside. Only stocks of real companies were traded, and the sales were recorded. These procedures created a false air of respectability and stock brokering became perceived as a reputable profession.

During the auctions, prices for shares of stock were quoted in increments of an eighth of a dollar or just **eighths**. This practice can be traced back to a time when people carried Spanish milled dollars and cut them into pieces of eight. In the beginning, only 30 companies were traded inside the exchange — banks, cargo insurance companies and construction firms that built bridges and piers — yet only a handful of fearless investors dared buy them. The general public was afraid of the stock market because, unlike bonds, if the company went bankrupt the stockholders lost everything. Stocks were for two types of people; outright speculators or people trying to take control of the company.

The struggle for respectability on Wall Street brought only a short period of limited success to the brokers and auctioneers that controlled it. With time, the less reputable trading of stocks resumed out front on the street among the brokers who weren't allowed to join the exchange board. Disputes between these **curb trading** stock brokers were settled with fists.

In 1832, a new invention allowed news to flash across the

United States called the **telegraph**. In the world of finance, information is power and the telegraph was a godsend. The telegraph's inventor, **Samuel Morse**, opened a demonstration office near the stock exchange charging 25¢ to see his device — the equivalent of \$5.43 in 2006! It wasn't long before Wall Street was a tangle of telegraph wires. The telegraph turned New York into America's financial capital by eliminating the need for regional markets in other cities. The **stock ticker** was the next innovation created in 1867 by **Thomas Edison**. The ticker printed telegraph signals on a narrow paper tape — the **ticker tape** — that carried current prices to brokers throughout the nation. For the first time since the Buttonwood Agreement, people outside the exchange knew what was going on in the stock market. On Wall Street, "**bulls**" became the term for people who expect stock prices to rise. Alternatively, "**bears**" were those who anticipated drops in the market. Many bears used declines to outwit other investors.

### **The First Economic Expansion**

America's westward expansion detonated an explosion of trading activity and technology that sped up the pace of business beyond anyone's wildest dreams. The markets were completely unregulated by the federal and state governments and Wall Street was (and still is) no place for amateurs. The bulls included colorful characters like **Hetty Green**. The woman's severe appearance and miserly character earned her the nickname "the witch of Wall Street." Hetty, bitter from being swindled out of her inheritance by an insensitive male-dominated court system, eventually became the world's richest woman by making shrewd investments in railroads. Hetty Green amassed a fortune of \$100 million dollars by investing in railroad stocks and real estate. Throughout her life, she employed a crude system of investigation before making any investment. She personally went to persons known to be enemies of the company directors or sellers of real estate. A money-wise and tough woman, she learned every-