IFB242: How to Use Dollar Cost Averaging with a Fixed Amount + Defining Goodwill

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Dave

0:00

All right, folks, welcome to Investing for Beginners Podcast. Today we have episode 242. We have four great listener questions that we're going to answer. And we'll go ahead and start with the first one. So here we go. Hi, David Andrew, great podcast, relatively new listener, but I enjoy this spectrum of beginning and intermediate investing discussions. My question is, how does dollar cost averaging work when your portfolio is whole stocks rather than an index slash basket fund? Well, ideally, you DCA every month, it becomes difficult to buy and rebalance hold stocks that are three, four digits, and seems impossible to do monthly for a Roth.

Are there investment platforms that let you invest fixed amounts of money into them? Stocks up deseeding into fractional shares, no love loss for index funds, but the DD due diligence for individual companies is part of the fun, Pat. So Andrew, what are your thoughts on paths? Great question.

Andrew

0:54

I agree 3d for individual companies is much of the fun. So dollar cost averaging. And if you're tuning in for the very first time, it's simply investing the same amount of money every single month. Now, where that can become a problem is, like you said, like Pat said here, if you have a stock that's like $2,000, a share, and your dollar cost averaging less than that, you can't really do that, you'd have to wait several months to buy a share.

So I use fidelity now also for a Roth as well. So they have all sorts of accounts, but they do have a Roth, and you can buy fractional shares in there. I find it interesting that as we record this in 2022, there's still a lot of brokers that don't offer this when I first started my first Roth and the count, I still have now I was not able to do fractional shares. Still, I'm not able to do fractional shares. So you do have to find a broker. And I know that fidelity for sure you can do it and they let you get down to the decimal points, I would just open an account with them. I mean, you can have multiple Roth accounts. There's nothing wrong with that.

So open one with fidelity, and that solves all your problems. Yeah, Schwab offers fractional shares as well. Right? So with Schwab, I don't know about the Roth, I have an individual with Schwab, and they let you do stock slices. But those have to be stocks in the s&p 500.

Dave

2:13

Right. So it's a little more limited, but I know fidelity is pretty broad across the board, which is kind of nice. So I guess what are your thoughts on dollar cost averaging into fractional shares as opposed to full shares? So let's say that you're buying a company that's if you're doing $150 a month, the stock trades at $320 a share? What are your thoughts on doing that instead?

Andrew

2:36

Yeah, I mean, it's a good question, it should not factor into your analysis, one bit, at the end of the day, a fraction of a share as a fraction of a share, it's still a share, it's no less of a share than the full share. So I understand when investors first started out, they kind of get really caught up in what's the dollar amount, you know, was my stock up $5? Or was it down $10, you have to get your mind set off of that.

And you have to just understand that, whether it's point two, five of a share, or 25 shares that says nothing, what really matters is what company you're talking about, and how many shares they have outstanding. So if you think of it like a pizza, like we like to say, the pizza can be sliced in the many different slices. A 14 inch pizza, whether it's slice, and eight slices, or 16 slices is still the same 14 inch pizza.

So it's the same with stocks, if you see a stock with a share price of like $3,000 per share. It doesn't mean that's necessarily expensive. It just means they sliced that pizza a lot. Why there than another company that

Dave

3:42

yeah, that's a good point. So when you're investing in companies, and you're buying a partial share, or a slice, and it's a dividend paying company, how does that factor in? Or how does that work?

Andrew

3:51

A good broker should give you dividends based on your fractional share. So if I have point two, five of a share, I should get point two, five of a regular dividend. You know, there's so many brokers out there. So you never want to say that every broker is able to do that. But if I was investing, then dividends are a part of your strategy, you definitely want to see if they're doing that or not. And a simple way to do that is just to see how many dividends did you get last month and compare that to how many shares you had beforehand?

Dave

4:23

Yeah, exactly. I know that fidelity allows me to reinvest. So drip my partial shares, because there are some companies that I have bought partial shares of and continue to do, and they allow me to reinvest them. So when the dividend is paid, I get more shares of the company that I'm buying. So it's still the all the things that we still advocate for are readily accessible, even whether you're buying, you know, one share or point seven 5% of a share.

So yeah, that's great. All right. Let's move on to the next question. So we have Hulu. Just curious, how can I transfer my stocks to another brokerage? I currently Use Robin Hood. So how do we suggest that they move to another broker?

Andrew

5:05

So I'm gonna answer this in two parts, because it could be really complicated or it could be really simple. If you're with Robin Hood, maybe this applies to you. And that's a pretty simple answer. You can go on their website, they say you can do a C A T S, automated customer account transfer service. And based on what they're saying, that will transfer your shares to another broker. So maybe you're with fidelity, you would tell fidelity, hey, I have some shares from Robin Hood, I want to transfer fidelity so to start the process, and then they will contact Robin Hood. And then Robinhood will do that for you for $100 fee.

And so that's one way to do it. It gets more complicated if you're talking about retirement accounts. Because I went through this I was doing I've done several rollovers and neither of them have been pretty. So as an example, a 401k, with a previous employer. And then you want to roll that into an IRA. After you leave IRAs, another type of investment account, you have more control over they had to sell all of the stocks that were in the 401k and then take the cash and then transfer it to my new brokerage. And then I had to go and rebuy. And at the time I did it, the market was volatile. So I lost a couple of weeks.

And there were painful weeks because the market swung and there was a different very different place from where it was before. So you could be selling low and buying high, depending on what happens in that time. Unless things have changed in the last five years. He's just that's kind of one of the things he's got pick up the phone and see what your broker says about doing some sort of a rollover.

Dave

6:39

Yeah, the nice thing about the brokerages is my experience with them as the customer service has been actually quite good. And they will help you walk through how is the best way for you to move your shares. Whether it's a retirement account, or whether it's a brokerage account, different brokerages are going to have different setups, and everybody's going to be a little bit different. But by and large, I think they'll be fairly helpful getting you the information that you need, whether it's moving a 401k from like interdit, a former employer or whether you just want to move from one record to another, they're all going to have systems to help you do that painlessly as you possibly can.

But just be aware that there could be some friction like Andrew was talking about. Yes. 100% Okay. All right. So moving on for brokerages we have next question. So we have Hello, Andrew and Dave. First off, thanks for an incredible podcast and all the information you provide. I have almost finished up reading the Intelligent Investor good for you, per your recommendation and have gained an unbelievable amount of knowledge about the market compared to what I knew before, which was nothing. Could you both give your opinion on Graham's definition of dogs with the Dow the cheapest stocks listed on the Dow?

Could you also give your best description on goodwill and what that does to a company's balance sheet. Thanks again for your time and wisdom. Let's talk about the dogs of the Dow Can you explain to them to our listeners, what the dogs of the Dow is ?

Andrew

8:01

So firstly, of the Dow Jones, these are 30 Big stocks. They are generally very big market cap stocks. I mean, how would you even pick it's something to do with like supposed to be encompassing the industrial part of the economy? Something like that?

Dave

8:17

Yeah. It's typically I think, the 30 largest businesses in the country. And I think there's a committee that kind of decides who's in the Dow and

Andrew

8:25

not Yeah, I mean, it's weird because you get the big companies like Apple and Microsoft, but then some of the like Facebook's on in there. I don't want to like throw shade at the Dow or anything. But to me, it seems like a like an old way of categorizing stocks where today I don't know how I don't know how representative it is of anything other than it just kind of is a group of stocks has always been tracked, for whatever reason we're continuing to track it. But what determines if you're in it is not always 100% Clear.

In general, the stocks in the Dow will tend to pay a dividend they'll tend to be bigger, like we mentioned dogs are the Dow means the companies in the Dow who have the highest dividend yield. So if we were to use finviz.com, today, you can quickly sort all of the stocks in the US and you can look at just the Dow and then you can sort by dividend from highest to lowest. So I see Verizon, Dow, Walgreens, IBM three, Intel, Chevron, Cisco, JP Morgan and Amgen. So all like really big companies with 1000s and 1000s of employees huge, pretty big market caps. And I would say my opinion on it is I would have a different opinion on any one of these because somebody like Dow the company might not necessarily be matured. If you think that depending on where you think commodities are gonna go.

Versus like somebody like IBM, who we've covered in a previous episode, where they very much see matured and not even mature but like Over the hill stumbling down the wrong way. On the flip side, you have somebody like Cisco, who's kind of like they were matured, but then they're transforming. And they're building this software business inside of their kind of more legacy business, which is growing at a nice rate. So it's hard for me to say definitively that you just want to paint these with a brush, because you kind of do want to take it company by company basis.

Dave

10:21

Yeah, totally. And you definitely want to take it company by company. And I think kind of grouping everything together in one basket can sometimes be dangerous. And because you're gonna have outliers, even within those groups, like Andrew was saying, you know, the company Dow may have longer term future potential than a company like let's say, Amgen, or Intel, I can speak to Intel, personally, because it's something I own. And it's something that they're going through a big air, quote, transition. And, you know, kind of like Andrew was talking about Cisco, they have a mature side of the business, but they're also evolving into a more newer type of business that could help them continue to innovate and grow into the future. And Intel is attempting to try to pull off something similar.

And when I say attempting to pull off, it's, it's gonna be an uphill slog to see if they can do it or not. But I guess, you know, for me, when I look at those companies, you know, by and large, those groupings, that companies are not companies, they feel more on the mature side of where they are, they can have a place in your portfolio, depending on what your goals are, really where you want to go, but their big claim to fame, and I guess, ideal investor is going to be somebody that's looking more for dividend income, because there are companies that are generally going to be growing the dividend, and are going to be more, I guess, solid companies that you aren't going to see go away very quickly.

But by the same token, the flip side of that is they're also not going to grow very fast. Verizon has been on the struggle bus for a few years now, because of that very thing. But they pay a great dividend, and they continue to grow the dividend. And it's not like Verizon is going to go anywhere in the next five years. But the opportunity cost that you could lose by investing in Verizon versus Company B, that could be an offsetting, you know, I guess, factor.

The other thing I guess I wanted to throw out there as congratulations for reading the intelligent investor, you know, sometimes it gets a little bit of shade is not being relevant anymore, but it's very relevant. And there's a lot of great information in there. So kudos to you for reading that. So did you have any more thoughts on the dogs of the Dow,

Andrew

12:30

I guess I would kind of try to wrap it up that the dogs of the Dow I think it depends on when you're looking at it. So when I look at the other companies in the Dow, like Apple, Microsoft, FISA, these are companies that are actually very much still growing, you wouldn't call them young, but you wouldn't call them mature either.

So if they happen to have a dividend yield that was big enough to be a dog of the Dow, then I would probably look more carefully, the current list now maybe not as attractive. So I would just kind of reinforce this idea that I will not paint the Dow with a broad brush. And however the Dow is comprised today could be very different five years from now, five years after that. I mean, it used to be a sin. And this wasn't too long ago, it used to be a sin to put any technology stock in the Dow.

And now you have apple, and Microsoft has the two biggest pieces of the Dow. So things change, like who knows what's going on with the Dow committee, just take it like you would anything else with investing in a big basket of stocks? And really, if you're going to be picking individual stocks taken on a case by case basis.

Dave

13:34

That's perfectly base, I wholeheartedly support that idea. All right. So let's move on to the second part. So could you also give your best description on goodwill? And what that does to a company's balance sheet? So what can we talk a little bit about Goodwill? What is a good definition of goodwill?

Andrew

13:52

Who wants to open their textbooks to page 54? Counting for beginners? Are there any big acquisitions lately, you can think of that would have probably carried a lot goodwill into it and MailChimp? That might be a good example. Yeah. So I don't remember how much Intuit pay, I think it was like 12 billion or something like that for MailChimp. So into it's a software company, MailChimp is a software company.

And as you might know, if you loosely follow software companies or accounting in general, the way that you would value a software company is not necessarily you know, it's not the computers if there were like five software developers who spent all night for three years pounding away at MailChimp, software, and it's not the value of those five computers that makes the value of the company. It's the fact that they have this website and the software that people use.

Think of it like Facebook in the same way. It's not the computers that built Facebook that make Facebook valuable. It's the fact that people use Facebook and advertisers pay to show ads to people On Facebook, so you can trust that with like a bank, for example, where if a bank brings in cash as deposits, those are that cash is real value, and you can count it on your hands, and you can count it with numbers. And so that has a very tangible value. So if a bank has 10 billion in book value, and 100 billion of that's in deposits, these are all very tangible numbers and digits that we can assign to the value of the bank. Whereas for a software company like MailChimp, they don't have that same, you can't add up these numbers of dollars per se, to come up with the value, it's a little bit more abstract.

And so I can't go in and say I'm gonna buy into it for $3,000, because you used five computers to make it, you have to pay more close to the like $12 billion to account for how much cash flow the company might be bringing in. And so that difference between whatever assets the company has in the books as digits, and then how much was actually paid for the company through the acquisition. That's goodwill.

So I don't know what their assets were before the acquisition. But if it was something like if they were worth $3 billion, once you took their assets, and you took out the liabilities, and if Intuit paid $12 billion for them, then the goodwill is that difference between 12 and three and that goodwill would be $9 billion?

Dave

16:28

Yeah, that makes sense. That's a very good explanation that's much clearer than my textbook was. So I guess a couple questions that kind of springs to mind with goodwill, then, you know, if you're curious about what this is, and kind of how it impacts the business, where would you find that?

Andrew

16:42

It's like on the company financials? Yeah, yeah. So it's on the balance sheet, that's where you would start, you could use any website like quick Fs, or stratosphere.io. And you can look at the balance sheet, and they will have a line item called goodwill, if you're in a company's annual report, you can use that trick Ctrl. F, to talk about.

And you can just directly search for where as goodwill, typing goodwill, and then we'll show you where it's mentioned in the document. And usually, there's a section for companies that do a lot of acquisitions, there's a section for explaining how they came up with the goodwill number, and that's usually in the notes, the footnotes.

Dave

17:22

So it gets How does goodwill impact a company positively or negatively? So like into it, for example, if they have a certain amount of goodwill, that they, I guess, absorb, if you will, from the purchase of MailChimp, five years from now, how does that really affect into it? Or does it?

Andrew

17:39

Yeah, it does. And it's really tricky, because it can manifest itself in many different ways. So just think about it this way, if I was trying to keep like a beginner lens on it is however much goodwill it is, that's really how much a company paid for an acquisition, right. So you don't want a goodwill that's out of control.

That's really, really high. Because if you ended up paying, let's say, $50 billion for MailChimp, and it's really only worth like $12 billion, that extra is going to come off eventually, because the accountants are gonna figure it out, and then they're gonna have to write that down. And then you're gonna take it as a loss. And so you'll see the balance sheet come down, you'll see your income or net income will come down.

So it's kind of one of those things. As an investor looking at the company with goodwill, you really don't know if that's Goodwill or bad goodwill until the acquisition plays out. I mean, that's tricky. Because management's don't really know either. When Microsoft bought LinkedIn all those years ago, there were people who thought they were crazy to pay that much for a little software company. But you look back now and you're like, my LinkedIn is worth way more than $12 billion now. So as an investor trying to take like a practical point of view, when I'm looking like kind of I would look to see everything is relative.

So if your balance sheets, if your book value is like $10 billion, and you just added for the billion in goodwill, that might be a little bit of a red flag to say, why are we have our eyes bigger than our stomach here? And we're really trying to do something aggressive, like why are you being so desperate versus the the flip side of that maybe this company accumulates goodwill over time, because they make a lot of smart, small bolt on acquisitions or things like that, that would be a lot less concerning, because relative to what they've done over time, they've had a good track record. That's kind of how I would look at it. I don't know, how would you look at it?

Dave

19:36

I think that's a great explanation. I guess the way I kind of look at it is when companies acquire other companies or make investments in other companies, they're in essence doing the same thing that we are, is they're trying to find a good value for what they're doing. And companies buy other companies all the time.

And it's a very common experience in the market. And I think the companies that do it well They will have goodwill on their balance sheets. And that's part of the nature of what they're doing. And the companies that do it well can profit and benefit from making good acquisitions at a good price over a good period of time. And the companies that are like their, quote serial acquirers like they buy lots of other businesses, and that's kind of the nature of their business, they tend to have a really good track record of buying companies integrating them well.

And they turn the results turn out, well, over a longer period of time, when companies run into trouble. It's when like, Andrew was saying, they overpay for something like they pay 50 billion for MailChimp, when it's really only worth 12 billion. And the first initial honeymoon phase of that, if you will, won't really affect the company much, but down the road, it could. And as the company, they'll have to do what's called an impairment. And without going into the nitty gritty of it, it basically means that they have to write that asset off.

And that becomes a loss on their income statement. And the if a company is you know, imminently profitable like into it, and then all of a sudden, you got this huge negative number on their income statement. And markets don't like that much. And you know, those things can also lead to bigger troubles down the road. Because if you put all your eggs in one basket, ie, if you bought AOL back in the 90s, and that didn't work out so good for you, that's not going to be a great thing. And that can lead to management, losing jobs, and companies struggling big time, or even taking a turn for the worse and even going bankrupt.

So it really matters. It's not necessarily that a company that they buy other companies, it's more about what the price they pay. And so you have to kind of, I guess, be cognizant of that, if you will. And I'll give you example, a today in the market, Adobe bought another company that's kind of in their niche, and Twitter is all abuzz about it, because they everybody feels like they way overpaid for the company that they purchased. And time will tell you never know right away, it takes some time to but at some point that could if it doesn't work out, that could be a ding against Adobe. And so that's why it's important to guess pay attention to when companies are buying other companies and kind of be cognizant of the purchase price. And a lot of times you'll see, this is how much they paid for it. And this is what you know, the markup is if it's a public company, and so that can help give you a sense of you know, hey, this company was trading at $25. And now they're buying it for 70.

Okay, you know, that seems a little stiff. So I guess that's kind of my idea. With goodwill, it's not necessarily a good thing or a bad thing. It's just something you have to kind of be aware of, and other companies, some companies are gonna have big goodwill numbers, and some aren't. And I guess, you know, when you see a company that acquires a lot of companies, or maybe makes big purchases, maybe not regularly, but maybe semi regularly, you may see a bigger number of goodwill on their balance sheet as a percentage of their assets. And that's something just to be aware of. But if they don't have a history of having bad make bad choices, I mean, everybody's going to make a mistake once in a while it happens.

But it's it's something to kind of keep in mind. But I don't know that there's necessarily a good or bad thing about Goodwill, per se. It's just something to keep in mind. That's very well said. All right. Thank you. All right. So let's move on to the last question. So I just signed up for the Seder research letter, and I'm trying to figure out how to get started. From what I gather, it looks like I need to open a Roth IRA account, and then start adding the stock picks each month. Why a Roth versus a standard IRA, a 1099 self employed worker?

So does that make difference in what type of IRA to open? Just would like some direction on how to get started from scratch? Thanks, Ken. So Andrew, this is all you big guy. So let's talk about this either research letter and kind of getting started, what kind of account works best and so on.

Andrew

23:51

So to kind of answer the question very literally, to me, a Roth IRA is more appealing than a regular IRA, because I'm somebody who likes to delay gratification. So I'd rather pay the taxes out and then let my money compound later. And that's what the Roth lets you do.

You shield yourself from a layer of tax by paying taxes today, and then investing and then you never get taxed on that ever again. So that's why I like the Roth just kind of bigger picture I guess to why this big focus on the Roth and the leather is it really came down to I personally believe that so many more people can get started in the stock market than think they actually can. And if you're listening to this, I'm talking to you because if you're listening to this, you're listening probably on the cell phone and whether you probably have an iPhone and if you don't, you know will excuse the few to three few of you doubt your bill for your iPhone, you know, when you factor in the network and your phone could be somewhere close to $150 on month.

So to me $150 A month is a very reasonable goal to set to, to invest, and to figure out how can I reduce my expenses to that amount, and at least commit to doing that much every month. Because I'll tell you that if you don't set a habit to say, You know what, I'm just gonna wait. And if I have any extra money at the end of the month, I'm just gonna wait and then I'll put that in the market, it's not going to happen. And, okay, maybe it does happen for you, good for you. But you will probably make way more progress.

If you stick to something that's reasonable. And you just month after month after month, you're putting that in. And so that's why whether you're doing $150 a month, or $1,500, a month really doesn't matter, you have to have something that you're going to stick to. And when you have that tangible goal, it forces you to buy, regardless of what the markets doing. Because people all the time will say, Well, I don't want to buy it's too expensive. Or why don't want to buy, there's too much inflation, or I don't want to buy there's a recession coming up, there's always gonna be a reason why you don't buy.

And guess what, when you have $1 cost averaging plan that says I'm putting in $150 a month every time you're buying even when people aren't, and that's what makes a difference over time, you can talk to so many different investors, and they'll tell you, it's time in the market. And this just putting money in putting money and putting money and you do that long enough, you're gonna become wealthy, you're going to build wealth, it's just it's going to happen.

So the last kind of thing that I feel like is a really good reason to pick a number and stick to it. And then you can always add a cherry on top or icing on the top of the cake, if you want to. When you commit to a number and say I'm going to do this every month, what it does is it lets you enjoy your life guilt free, because I don't care if you're like broke, or even if you feel like you're killing it, there is this treadmill of finance that is so easy to fall into, where you can always feel like you're not doing enough, I gotta put in more, I gotta put more and then you can't enjoy the things that money are even supposed to provide for you. So when you have a set amount where you can say, you know, I did good enough this month, it allows you to have a sense of financial freedom today.

Because you know, you're making progress, hey, I'm not going to be this perfect person who sacrifices every dollar I can to become Uber wealthy in the future, but you know, you're on a plan, you're gonna stick to the plan, you're gonna have results, and then you can enjoy, you know, spending without guilt. Because, you know, why are they doing what I'm supposed to do now I have this extra money, and now I can spend it. I think that's kind of a part of dollar cost averaging, maybe we don't talk about a lot that really makes a big impact on your overall health. And, you know, we talked about the path to financial freedom, you got to take some of that financial freedom for yourself today.

So if you are able to choose where your money goes like that, and you're able to maybe make sacrifices, that's also you're also able to enjoy it in a way. And if you can do that now, it keeps you from chasing the most expensive stocks, or from feeling bad when you see Tesla go to, you know, $3,000 a share. I mean, it's not going to shield it perfectly. Of course, you always feel a little bit of FOMO. But it feels so much you don't feel nearly as bad about it when you feel okay with yourself. And that only comes from having a plan and sticking to it and being okay. That it's like, you know why I did what I said I was gonna do, and I did the best I can. And that gives you a peace of mind that you can't get any other

Dave

28:36

way. Return brother preach on. Yeah, that's perfect. All right. Well, I think that is probably the perfect place to go ahead and wrap up our conversation for today. I wanted to thank everybody for taking the time to send us those fantastic questions, please keep them coming. Those are great. It's a lot of fun. And hopefully you guys get some good information from our discussions. If you are curious about anything that we were talking about today, please go to our website, ie investing for beginners.com.

There's a great big, big search bar at the top of the page that can help you find anything that you're curious about regarding the stock market. So if you want to know more about Goodwill, and you're like I don't know what that is, just go to our website, e investing for beginners.com and type in goodwill.

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