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Putting Your Two Cents In

Participation in an investment club can net members a big payoff—in both dollars and stock market expertise.

By Verna Gates

I was either going to become a Civil War buff or get into the stock market," says Master Sgt. E. Circeo, 43. "I figured I'd make more money in the stock market." Circeo was living in Albuquerque, N.M., in 1998 and was looking for an activity in which to pour his energy. Inspired by the stock market, Circeo joined the Beardstown Ladies' Investment Club—founded in 1983 by a group of women in Illinois—Circeo's friends from his Air Force days met for

breakfast at a local motel restaurant and made the decision to get into the stock market through an investment club of their own.

An investment club is a group of people who pool money and knowledge as they wade into the stock market. Members each contribute a nominal amount, averaging between \$25 and \$200 a month to the club treasury; the pooled funds are used to purchase stocks. Each club member is assigned a portfolio to follow and is expected to make monthly reports and recommendations to the club.

Investment clubs rarely are made up of random people coming together to seek their stock portfolio. They grow from associations with coworkers, school chums, church friends, Superbowl buddies, or civic clubs. The glue is friendship and a desire for passive income, defined as money that you can sleep on.

"It just came to me that it is free money," says Circeo. "The stock market is there waiting for you. It's just a matter of money."

Once Circeo and his friends agreed to form an investment club, they had to open a bank account and apply for a tax id number. For their first investment, they purchased Home Depot and Cisco stock; today the latter is up 70 percent. Although many members have scattered—one is in Japan, one in Chattanooga, Tenn., and Circeo is in San Antonio—they conduct monthly meetings via e-mail. Such regular meetings characterize investment clubs. Most are strict about attendance, even fine errant members.

The average club gains 10 percent annually and doubles its net worth every five years. The average net worth of clubs totals \$1 million.

"Some charge a \$3 penalty, some charge \$25 if you miss a meeting," says Lt. Col. Billy Williams, Ret., who has been involved with investment clubs for 43 years. "Clubs don't want the money; they want people participating. Participation is why my two big clubs have done so well."

Thanks to his investment earnings, Williams, 66, was able to retire from a second career as a civil engineer at age 52. He believes so strongly in the clubs that he has formed a family club with all his children and grandchildren. As each child was born, Williams began contributing \$25 a month into the club on the child's behalf. His oldest grandchild, now 20, has actively participated in the club since age 10 and has gained an understanding of the power of saving and investing—as well as \$20,000 in assets.

Williams' results are impressive, especially considering that in 1961, when he first began investing in a club, he didn't know how to read a financial page. But he had seen a how-to article about investing in a club, and the club he formed with fellow civil engineers, dubbed The Highway Investors, made an average annual return of 18 percent for the 41 years of its existence. The investment club he formed 40 years ago with members of his adult Sunday school class now is performing even higher, at a 20 percent return.

Williams volunteers with the National Association of Investors Corporation (NAIC), the largest organization for clubs (available online at www.better-investing.org) as director of its Atlanta chapter. The organization includes 845 clubs, and he teaches 10 classes a year on investing.

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"We definitely need investment clubs. Some people do not require them, but most do. ... Club [the discipline to invest]," he says.

Applying the adage "two heads are better than one," investment clubs' group discussion process seems to help novice investors sort through the overwhelming amount of information that goes into a decision to invest. Participants balance each other: One might be hot to choose a popular stock, another might have seen warning signs or have other cautionary information.

The earnings cited by investment club organizations are impressive: The average club gains 10% annually and doubles its money every five years. The average net worth of clubs totals \$33,000 according to Rob Nagler, chief technical officer for Bivio (www.bivio.com), which makes accounts and products for investment clubs. NAIC alone comprises 400,000 members, according to CEO Ke Williams estimates that only about one-third of all investment clubs are affiliated with any form of organization, pushing the actual numbers past the million mark. Investment clubs were particularly popular in the 1990s, when the stock market ran wild with inflated earnings.

"There were people putting \$10,000 on some obscure name and weeks later coming out with some crazy things. People started viewing the stock market as a casino-like, make-millions-or-lose-it scheme. The mania has all gone now." Although Bryant has helped his customers start five different investment clubs, he maintains the financial tools now available via the Internet make the club unnecessary.

"In the past, brokers were the gatekeepers, and you had to pool your money so you would have to get them to pay attention to you," Bryant says. "Now, you can open an account online where brokers will give you \$200 to open an account with them. Investment clubs just don't make as much sense anymore."

Bryant points out that for all their big numbers, investment clubs do not, on average, perform as well as individual investors. He suggests clubs are more likely to pick risky, fast-moving stocks.

And while Circeo remains a firm believer in his club, he admits it has picked some losers, such as headliners Oracle and mci Worldcom. His club historically has netted an average annual return of 15 percent. However, the club's rate of return has improved since it joined the NAIC, which posts its performance evaluations in its newsletter and on its Web site, offers training, and teaches long-term investment strategies.

"The investing guide kept us out of Enron, for example. We would have bought it, I guarantee you."

Clubs do purchase losing stocks; Williams estimates that one out of every five stocks tanks. He says that would be batting .800 in baseball. Also, investment clubs might hold on to losing stocks longer than is prudent. A group can find it troubling to sell a stock at a loss and be more reluctant than the individual to dump it. Club members must take these hits, learn from them, and move on.

"You learn and earn, and hopefully transfer those skills to personal investing," says Williams.

Indeed, though his club has lost money, Circeo says he has gained personally.

"I have learned so much from my club about how to invest," he says. "I was able to pay off \$20,000 of personal debt while in the Air Force. I used my stock earnings."

Even Bryant acknowledges clubs have a place at the investment table: "If it takes investment people in the market, then it's a good thing."

Today, Circeo has used his earnings to start a new career as a Web designer, while Williams has an abundance of leisure time to read the financial page that once was as intelligible to him as a second language.