“The best way to measure your investing success is not by gains and losses but by whether you’ve improving your overall financial plan that is likely to get you where you want to go.”- Lawrence Castillo

‘Layin it on the line’

On the most fundamental level, there are two different approaches to investing in the stock market: active and passive.

An active investor, relying on his or her personal skill, attempts to beat the market by investing in companies believed to have the most reliable long-term growth prospects. Such an investor may try and beat the market by jumping in and out at precisely the right times to maximize gains and avoid losses.

Passive investors, on the other hand, are looking to match market returns by spreading money around between different types of investments. How their money is allocated will affect their returns, but passive investors are interested in simply taking market returns and not trying to get an edge on everyone else in the market.

There is an obvious difference between the two strategies and, for most individuals, beating the market as an active investor is nearly impossible. Typical active investors, in fact, regularly underperform the market by 4-5%. Even professional investors have difficulty beating the market consistently. Most people wind up losing to the market.

That's why, when discussing what course of action is best for an individual, financial guru Ben Graham stated that an individual *"should act consistently as an investor and not as a speculator."*

INDEX INVESTING AND THE SINGLE INVESTOR

A stock index is a measurement of a segment of the stock market. These indexes are compiled from the prices of selected stocks, usually using a weighted average. Contrary to what you may think, an index (such as the S&P 500) is not the *"pulse"* of a market, but rather a tool used by investors and financial advisors to compare the returns on specific investments and to describe the moods of investors.

Indexes use a base value that represents the weighted average stock price of all the stocks comprising that particular index. The actual index number has much less importance than its percent change over time. It is this up or down movement that can give you an idea of how that particular index is performing.

Each index is calculated on an ongoing basis every day the market is open, and each reflects market conditions and the state of the economy differently. It is important to note, however, that the most referred-to stock indexes, like the **NASDAQ and S&P 500** reflect only a portion of the actual market and not the whole market. So, while indexes give you a useful snapshot of market movements and the attitudes of investors and provide you with a better historical perspective, they are not as useful as forecasting tools. Indexes tend to be most helpful as a research tool when viewed over a long historical period to determine trends and changes in investing patterns. Using an index will provide an investor with a yardstick for comparison.

Far from being the refuge of the timid and inexperienced willing to earn less on their investments, index investing has proven itself to be an incredibly effective strategy that often outperforms similar active investing strategies. 80-90% of the time, taking market returns produced by index investing produces better results than similar active strategy.

Index investing allows even those who are not *“bull market geniuses*” or who do not possess degrees in finance to make smarter decisions when it comes to growing wealth. It is perhaps the very best way to participate in market gains without having to incur excessive exposure to risk and the many expenses of more active growth strategies. Index investing lets you simplify and streamline the investment process and become more consistent.

It is this consistency that will ultimately allow you to create more wealth both in and out of the stock market.

Lawrence Castillo is a member of *Syndicated Columnists*, a national organization committed to a fully transparent approach to money management.

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