Chapter Two

DIFFERENT QUADRANTS, DIFFERENT PEOPLE

Changing quadrants is often a change at the core of who you are.

"You can't teach an old dog new tricks," my highly educated dad always said.

I had talked with him on several occasions, doing my best to explain the CASHFLOW Quadrant, in an effort to give him some new financial direction. Nearing 60 years of age, he was realizing that many of his dreams weren't going to be fulfilled. His "blacklisting" seemed to go beyond the walls of state government. He was now blacklisting himself.

"I tried it, but it didn't work," he said.

My dad was referring to his attempts to be successful in the S quadrant as a self-employed consultant, and as a B when he poured much of his life savings into a famous ice-cream franchise that failed.

Being bright, he conceptually understood the different technical skills required in each of the four quadrants. He knew he could learn them if he wanted to. But there was something else holding him back.

One day over lunch, I talked to my rich dad about my educated dad. "Your father and I aren't the same people at the core," said rich dad. "While we both have fears, doubts, beliefs, strengths, and weaknesses, we respond or handle those core similarities quite differently."

"Can you tell me the differences?" I asked.

"Not over one lunch," said rich dad. "But how we respond to those differences is what causes us to remain in one quadrant or another. When your dad tried to cross over from the E quadrant to the B quadrant, intellectually he could understand the process, but he couldn't handle it emotionally. When things didn't go smoothly and he began to lose money, he didn't know what to do to solve the problems, so he went back to the quadrant he felt most comfortable in."

"The E and sometimes S quadrant," I said.

Rich dad nodded his head. "When the fear of losing money and failing becomes too painful inside, a fear we both have, he chooses to seek security and I choose to seek freedom."

"And that is the core difference," I said, signaling the waiter for our check.

"Even though we're all human beings," said rich dad, "when it comes to money and the emotions attached to money, we all respond differently. And it's how we respond to those emotions that often determines which quadrant we choose to generate our income from."

"Different quadrants for different people," I said.

"That's right," said rich dad as we stood and headed for the door. "And if you're going to be successful in any quadrant, you need to have more than just technical skills. You also need to know the core differences that cause people to seek different quadrants. Know that, and life will be much easier."

We were shaking hands and saying good-bye as the valet brought my rich dad's car around.

"Oh, one last thing," I said hurriedly. "Can my dad change?"

"Oh sure," said rich dad. "Anyone can change. But changing quadrants isn't like changing jobs or changing professions. Changing quadrants is often a change at the core of who you are—how you think and how you look at the world. The change is easier for some people than for others simply because some people welcome change and others fight it. And changing quadrants is most often a life-changing experience. It's a change as profound as the age-old story of the caterpillar becoming a butterfly. Not only will you change, but so will your friends. While you'll still be friends with your old friends, it's just harder for caterpillars to do the same things butterflies do. So the changes are big changes, and not too many people choose to make them."

The valet closed the door, and as my rich dad drove off, I was left thinking about the core differences.

What Are the Core Differences?

How do I tell if people are an E, S, B, or I without knowing much about them? One of the ways is by listening to their words.

One of my rich dad's greatest skills was being able to "read" people, but he also believed you could not judge a book by its cover. Rich dad, like Henry Ford, didn't have an excellent education, but both men knew how to hire and work with people who did. Rich dad always explained to me that the ability to bring smart people together and work as a team was one of his primary skills.

When I was nine, my rich dad began to teach me the skills necessary to be successful in the B and I quadrants. One of those skills was to get beyond the surface of a person and gaze into their core. Rich dad used to say, "If I listen to a person's words, I begin to see and feel their souls."

So as a young boy, I began to sit in with my rich dad when he hired people. From these interviews I learned to listen, not so much for words, but for core values—values that my rich dad said came from their souls.

E-Quadrant Words

A person who comes from the E (employee) quadrant might say: "I am looking for a safe, secure job with good pay and excellent benefits."

S-Quadrant Words

A person who comes from the S (self-employed) quadrant might say: "My rate is $75 per hour." Or "My normal commission rate is six percent of the total price." Or "I can't seem to find people who want to work and do the job right." Or "I've got more than 20 hours into this project."

B-Quadrant Words

A person operating out of the B (business-owner) quadrant might say: "I'm looking for a new president to run my company."

I-Quadrant Words

Someone operating out of the I (investor) quadrant might say: "Is my cash flow based on an internal rate of return or net rate of return?"

Words Are Tools

Once my rich dad knew who the person he was interviewing was at their core, at least for that moment, he would know what they were really looking for, what he had to offer, and what words to use when speaking to them. Rich dad always said, "Words are powerful tools."

Rich dad constantly reminded his son Mike and me of this. "If you want to be a leader of people, then you need to be a master of words."

So one of the skills necessary to be a great B is to be a master of words, knowing which words work on which kinds of people. He trained us to first listen carefully to the words a person used. Then we would know which words we should use and when to use them, in order to respond to that person in the most effective way.

Rich dad explained, "One word may excite one type of person while that same word would completely turn off another person."

For example, the word "risk" might be exciting to a person in the I quadrant, but evoke total fear to someone in the E quadrant.

To be great leaders, rich dad stressed that we first had to be great listeners. If you don't listen to the words a person uses, you'll never be able to feel their soul. And if you don't listen to their soul, you'll never know to whom you are talking.

Core Differences

The reason he would say, "Hear their words; feel their souls," is because behind the words a person chooses are the core values and core differences of that individual. The following are some of the generalities that separate people in one quadrant from those in another:

1. ***The E (Employee)***

   When I hear the words "secure" or "benefits," I get a sense of who the speaker might be at the core. The word "secure" is a word often used in response to the emotion of fear.

   If a person feels fear, then the need for security is often a commonly used phrase for someone who comes predominantly from the E quadrant. When it comes to money and jobs, there are many people who simply hate the feeling of fear that comes with economic uncertainty: hence, the desire for security. The word "benefit" means people would also like some kind of additional reward that is spelled out, a defined and assured extra compensation, such as health insurance or a retirement plan.

   The key is that they want to feel secure and see it in writing. Uncertainty doesn't make them happy; certainty does. Their internal workings say, "I'll give you this if you promise to give me that in return."

   They want their fear reduced by the presence of some degree of certainty, so they seek security and strong agreements when it comes to employment. They're accurate when they say, "I'm not that interested in money." For them, the idea of security is often more important than money.

Employees can be presidents of companies or janitors. It's not so much what they do, but the contractual agreement they have with the person or organization that hires them.

2. ***The S (Self-employed)***

   These are people who want to "be their own boss" or like to "do their own thing." I call this group the "do-it-yourselfers."

   Often, when it comes to the subject of money, a hard-core S doesn't like to have his or her income dependent on other people. In other words, if S's work hard, they expect to get paid for their work.

   S's don't like having the amount of money they earn dictated by someone else or by a group of people who might not work as hard as they do. If they work hard, they expect to be paid well.

   Conversely, they also understand that if they don't work hard, then they don't deserve to be paid much. When it comes to money, they have fiercely independent souls.

The Emotion of Fear

So while the E often responds to the fear of not having money by seeking security, the S often responds differently. The people in this quadrant respond to fear, not by seeking security, but by taking control of the situation and doing it on their own. That is why I call the S group the do-it-yourself group. When it comes to fear and financial risk, they want to take the bull by the horns.

In this group you find well-educated professionals who spend years in school, such as doctors, lawyers, and dentists. Also in the S group are people who took educational paths other than, or in addition to, traditional school. In this group are direct-commission salespeople and real estate agents as well as small business owners like retail shopkeepers, cleaners, restaurateurs, consultants, therapists, travel agents, car mechanics, plumbers, carpenters, preachers, electricians, hair stylists, and artists.

This group's favorite song would be either "Nobody Does It Better" or "I Did It My Way."

Self-employed people are often hard-core perfectionists. They often want to do something exceptionally well. In their mind, they don't think anyone else does it better than they do, so they really don't trust anyone else to do it. In many respects, they are true artists with their own style and methods of doing things.

And that is why we hire them. If you hire a brain surgeon, you want that brain surgeon to have had years of training and experience, but most importantly, you want this brain surgeon to be a perfectionist. The same goes for a dentist, hairstylist, marketing consultant, plumber, electrician, lawyer or a corporate trainer. You, as the client hiring this person, want someone who is the best.

For people in this group, money isn't the most important thing about their work. Their independence, the freedom to do things their way, and being respected as experts in their field are much more important than mere money. When hiring them, it's best to tell them what you want done and then leave them alone to do it. They don't need or want supervision. If you meddle too much, they'll simply walk off the job and tell you to hire someone else. Remember, independence trumps money for this group.

They often have a hard time hiring other people to do what they do simply because, in their mind, nobody else is up to the task. Also, if this group trains someone to do what they do, that newly trained person often ends up leaving to "do their own thing," to "be their own boss," to "do things their way," or to "have a chance to express their individuality."

Many S types are hesitant to hire and train other people because, once trained, they often end up as their competition. This, in turn, keeps the S types working harder at doing things on their own.

3. ***The B (Business owner)***

   This group of people could almost be the opposite of the S. Those who are true B's like to surround themselves with smart people from all four categories: E, S, B, and I. Unlike the S, who doesn't like to delegate work (because no one can do it better), the B likes to delegate. The true motto of a B is, "Why do it yourself when you can hire someone to do it for you, and they can do it better?"

   Henry Ford fit this mold. As one popular story goes, a group of so-called intellectuals came by to condemn Ford for being ignorant. They claimed he really didn't know much. So Ford invited them into his office and challenged them to ask him any question, and he would answer it. So this panel assembled around America's most powerful industrialist and began to ask him questions. Ford listened to their questions and, when they were through, he simply reached for several phones on his desk and called in some of his bright assistants and asked them to give the panel the answers they sought.

   He ended by informing the panel that he'd rather hire smart people who went to school to come up with answers so he could leave his mind clear to do more important tasks, tasks like thinking.

   One of the quotes credited to Ford goes: "Thinking is the hardest work there is. That is why so few people engage in it."

Leadership Is Bringing Out the Best in People

My rich dad's idol was Henry Ford. He had me read books about people like Ford and John D. Rockefeller, the founder of Standard Oil. Rich dad constantly encouraged Mike and me to learn the essence of leadership and the technical skills of business. In retrospect, I understand now that many people may have one or the other, but to be a successful B, you really do need to have both. I also now realize that both skills can be learned. There is a science, as well as an art, to business and leadership. For me, both are lifelong studies.

When I was a boy, my rich dad gave me the children's book *Stone Soup,* written in 1947 by Marcia Brown and still available today. He had me read this book to begin my training as a leader in business.

"Leadership," rich dad said, "is the ability to bring out the best in people." So he trained his son and me in the technical skills necessary for becoming successful in business—technical skills such as reading financial statements, marketing, sales, accounting, management, production, and negotiation. Throughout each lesson, he stressed that we needed to learn to work with and lead people. Rich dad always said, "The technical skills of business are easy. The hard part is working with people." As a reminder, I still read *Stone Soup* today because I personally have a tendency to be a tyrant, instead of a leader, when things don't go my way.

Entrepreneurial Development

I often hear the words, "I'm going to start my own business." Many people tend to believe that the way to financial security and happiness is to do your own thing or to develop a new product no one else has. So they rush out and start their own business. In many cases, this is the path they take:

Many wind up starting an S type of business and not a B type of business. Again, one is not necessarily better than the other. Both have different strengths, weaknesses, risks, and rewards. But many people who want to start a B type of business wind up with an S type of business and become stalled in their quest to move to the right side. Many new entrepreneurs want to do this:

But they wind up instead doing this and getting stuck there:

Many then attempt to do this:

But only a few who attempt this actually make it. Why? Because the technical skills and human skills to be successful in each quadrant are different. You must learn the skills and mindset required by a quadrant in order to find true success there.

The Difference Between an S Type of Business and a B Type of Business

Those who are true B's can leave their business for a year or more and return to find their business more profitable and running better than when they left it. In a true S type of business, if the S left for a year or more, chances are there would be no business left to return to.

So what causes the difference? Saying it simply, an S owns a job; a B owns a system and then hires competent people to operate the system. Or put another way, in many cases, the S is the system. That is why they can't leave.

For example, let's take a look at a typical dentist. A dentist spends years in school learning to become a self-contained system. You, the client, get a toothache. You go see your dentist. He fixes your tooth. You pay and go home. You're happy and you tell all of your friends about your great dentist. In most cases, the dentist can do the entire job by himself. The problem is that if the dentist goes on vacation, so does his income.

B business owners can go on vacation forever because they own a system, not a job. If the B is on vacation, the money still comes in.

To be successful as a B requires:

1. Ownership or control of systems, and

2. The ability to lead people.

For S's to evolve into B's they need to convert who they are and what they know into a system, and many aren't able to do that. Or they're often too attached to the system to let go and let other people in.

Can You Make a Better Hamburger Than McDonald's?

Many people come to me for advice on how to start a company or how to raise money for a new product or idea.

I listen, usually for about 10 minutes, and within that time I can tell where their focus is. Is it the product or the business system? In those 10 minutes, I most often hear words such as these: (Remember the importance of being a good listener and allowing words to direct you to the core values of a person's soul.)

- "This is a far better product than company XYZ makes."
- "I've looked everywhere, and nobody has this product."
- "I'll give you the idea for this product; all I want is 25 percent of the profits."
- "I've been working on this (product, book, music score, invention) for years."

These are the words of a person generally operating from the left side, the E-S side.

It's important to be gentle at this time because I'm dealing with core values and ideas that have been entrenched for years, maybe handed down for generations. If I'm not gentle or patient, I could damage a fragile and sensitive launch of an idea and, more importantly, a human being ready to evolve into another quadrant.

The Hamburger and the Business

Since I need to be gentle, at this point in the conversation, I often use the "McDonald's hamburger" example for clarification. After listening to their pitch, I slowly ask, "Can you personally make a better hamburger than McDonald's?"

So far, 100 percent of the people I've talked with about their new idea or product have said yes. They can all prepare, cook and serve a better quality hamburger than McDonald's.

Next I ask them, "Can you personally build a better business system than McDonald's?"

Some people see the difference immediately, and some don't. And I would say the difference is whether the person is fixated on the left side of the quadrant, which is focused on the idea of the better burger, or on the right side of the quadrant, which is focused on the business system.

I do my best to explain that there are a lot of entrepreneurs out there offering far superior products or services than are offered by the mega-rich multinational corporations, just as there are billions of people who can make a better burger than McDonald's. But only McDonald's has created the system that has served billions of burgers.

See the Other Side

If people can begin to see this truth, I then suggest they go to McDonald's, buy a burger, and sit and look at the system that delivered that burger. Take note of the trucks that delivered the raw burger, the rancher that raised the beef, the buyer who bought the beef and the TV ads that helped sell the beef. Notice the training of young inexperienced people to say the same words, "Hello, welcome to McDonald's," as well as the decor of the franchise, the regional offices, the bakeries that bake the buns and the millions of pounds of French fries that taste exactly the same all over the world. Then include the stockbrokers raising money for McDonald's on Wall Street. If they can begin to understand the whole picture, then they have a chance at moving to the B-I side.

The reality is that there are unlimited new ideas, billions of people with services or products to offer, millions of products, and only a few people who know how to build excellent business systems.

Bill Gates didn't build a great product. He bought somebody else's product and built a powerful global system around it.

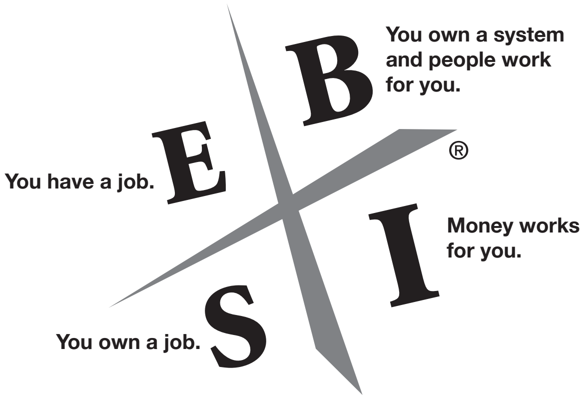
4. ***The I (Investor)***

   Investors make money with money. They don't have to work because their money is working for them.

   The I quadrant is the playground of the rich. Regardless of which quadrant people make their money in, if they hope someday to be rich, they ultimately must come to the I quadrant. It's in the I quadrant that money becomes converted to wealth.

The CASHFLOW Quadrant

The CASHFLOW Quadrant simply makes distinctions on how income is generated, whether as an E (Employee), S (Self-employed), B (Business owner) or I (Investor). The differences are summarized below.



OPT and OPM

Most of us have heard that the secrets to great riches and wealth are:

- OPT — Other People's Time
- OPM — Other People's Money

OPT and OPM are found in the B and I quadrants. For the most part, people who work in the E and S quadrants are the OP (Other People) whose time and money are being used.

A primary reason Kim and I took time to build a B type of business, rather than an S type, was because we recognized the long-term benefit of using other people's time. One of the drawbacks to being a successful S is that success simply means more hard work. In other words, good work results in more hard work and longer hours.

In designing a B type of business, success simply means increasing the system and hiring more people. In other words, you work less, earn more and enjoy more free time.

The remainder of this book goes through the skills and mindset required for the right side of the CASHFLOW Quadrant. It's my experience that being successful on the right side requires a different mindset and different technical skills. If people are flexible enough to make these changes, I think they'll find the process of achieving greater financial security or freedom easy. For other people, the process might be too difficult because many people are frozen in one quadrant and one mindset.

At a minimum, you'll find out why some people work less, earn more, pay less in taxes and feel more financially secure than others. It's simply a matter of knowing which quadrant to work out of and when.

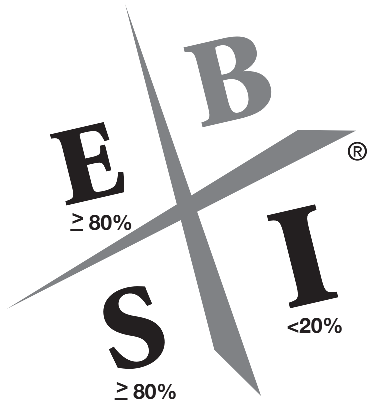
A Guide to Freedom

The CASHFLOW Quadrant is not a set of rules. It's only a guide for those who wish to use it. It guided Kim and me from financial struggle, to financial security, and then to financial freedom.

The Difference Between the Rich and Everyone Else

A few years ago, I read an article that said most rich people receive 70 percent of their income from investments, or the I quadrant, and less than 30 percent from wages, or the E quadrant. If they were an E, chances are that they were employees of their own corporation. Their income looked like this:

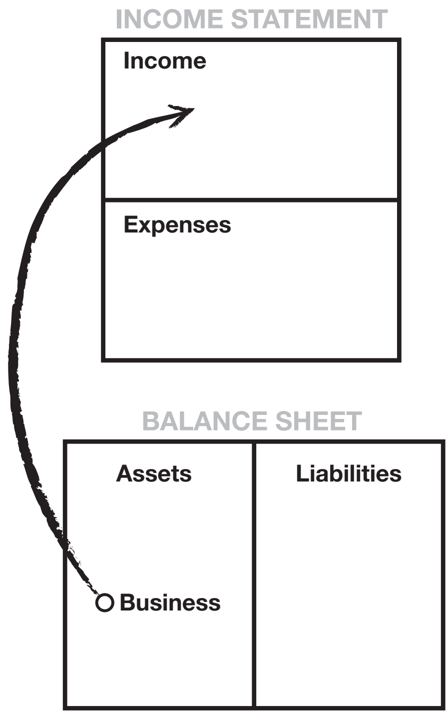
For most everyone else, the poor and the middle class, at least 80 percent of their income comes from wages from the E or S quadrants, and less than 20 percent from investments in the I quadrant.



The Difference Between Being Rich and Being Wealthy

In chapter one, I wrote that Kim and I were millionaires by 1989, but we weren't financially free until 1994. There's a difference between being rich and being wealthy. By 1989, our business was making us a lot of money. We were earning more and working less because the business system was growing without any more physical effort on our part. We had achieved what most people would consider financial success.

However, we still needed to convert the cash flow coming from the business into even more tangible assets that would generate additional cash flow. We had grown our business into a success. Now it was time to focus on growing our assets to the point where the cash flow from all of our assets would be greater than our living expenses.



By 1994, the passive income from all of our assets was greater than our expenses. At that point, we were wealthy.

Our business is considered an asset because it generated income and operated without much physical input. For our own personal sense of wealth, we wanted to make sure we also had tangible assets, such as real estate and stocks, that were throwing off more passive income than our expenses before we claimed to be wealthy. Once the income coming from tangible assets in our asset column was greater than the money coming in from the business, we sold the business to our partner. We were now wealthy.

The Definition of Wealth

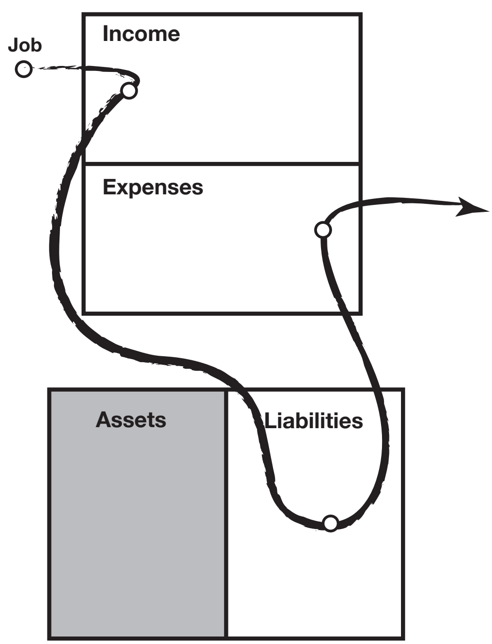
The definition of wealth is the number of days you can survive without physically working (or anyone else in your household physically working) and still maintain your standard of living.

For example, if your monthly expenses are $5,000 a month and you have $20,000 in savings, your wealth is approximately four months or 120 days. Wealth is measured in time, not dollars.

By 1994, Kim and I were wealthy indefinitely (barring great economic changes) because the income from our investments was greater than our monthly expenses.

Ultimately, it's not how much money you make that matters, but how much money you keep, and how long that money works for you. Every day I meet many people who make a lot of money, but all of their money goes out the expense column.

Every time they make a little more money, they go shopping. They often buy a bigger house or new car which results in long-term debt and more hard work. Nothing is left to go into the asset column. The money goes out so fast that you'd think they took some kind of financial laxative. Their cash-flow pattern looks like this:



Red-Line Finances

In the world of cars, there's a saying about "keeping the engine at red line." "Red line" means the throttle is keeping the RPMs of the engine close to the red line, the maximum speed the car's engine can maintain without blowing up.

Many people, rich and poor, operate constantly at the financial red line of their personal finances. No matter how much money they make, they spend it as fast as it comes in. The trouble with operating your car's engine at red line is that the life expectancy of the engine is shortened. The same is true with operating your finances at the red line.

Several of my doctor friends say that one of the main problems they see today is stress caused by working hard and never having enough money. One says that the biggest cause of health disorders is something she calls "cancer of the wallet."

Money Making Money

Regardless of how much money people make, ultimately they should put some in the I quadrant. The I quadrant is where your money makes more money. It's based on the idea that your money works hard so you don't have to work. Although the I quadrant is important to your financial health, there are other forms of investing worth noting.

Other Forms of Investing

People invest in their education. Traditional education is important. The more education you have, the better your chances may be to earn more money, depending on your choice of profession. Given that the average person spends 40 years or more actively working, college or some type of higher education may be a good investment.

Giving your loyalty and best efforts to an employer is another form of investment. In return, via contract, the employee is rewarded with a pension for life. This was a form of investment popular in the Industrial Age that is now almost obsolete in the Information Age.

Other people invest in having large families and, in turn, have their children care for them in their old age. That form of investing was the norm in the past, yet due to economic constraints in the present, it has become more difficult for families to handle the living and medical expenses of parents.

Government retirement programs such as Social Security and Medicare, which are often paid for through payroll deductions, are another form of investment mandated by law. Due to massive changes in demographics and costs, this form of investment will probably not be able to keep many of the promises it has made.

And there are independent investment vehicles for retirement that are called individual retirement plans. Often, the federal government will offer tax incentives to both the employer and employee to participate in such plans. In America, one popular plan is the 401(k) retirement plan. In countries such as Australia, they are called superannuation plans.

Income Received from Investments

Although the above are all forms of investing, the I quadrant focuses on investments that generate income on an ongoing basis during your working years. So to qualify as a person who operates as an I, use the same criteria used in all the other quadrants. Do you receive current income from the I quadrant? In other words, is your money working for you and generating current income for you?

Let's look at a person who buys a house as an investment and rents it out. If the rent collected is greater than the expenses to operate the property, that income is coming from the I quadrant. The same is true for people who receive interest from savings, or dividends from stocks and bonds. So the qualifier for the I quadrant is how much income you generate from the quadrant without working in it.

Is My Retirement Account a Form of Investment?

Regularly putting money into a retirement account is the form of investing people in the E quadrant are most encouraged to take. These retirement plans are not without risk and, even when they perform, the rate of return is never going to make you financially free. Most of us want to be investors when our working years are over, but for the sake of this book, the I quadrant represents a person whose income comes from investments during their working years. In reality, most people aren't investing in a retirement account. Instead, most are saving money in their retirement account, hoping that when they retire, there will be more money coming out than they put in.

There's a difference between people who save money in their retirement accounts and people who, through investing, actively use their money to make more money as income.

Are Stockbrokers Investors?

Many financial advisors in the investment world are, by definition, not really people who generate their income from the I quadrant.

For example, most stockbrokers, real estate agents, financial advisors, bankers, and accountants are predominantly E's or S's. In other words, their income comes from their professional work, not necessarily from assets they own.

I have friends who are stock traders. They buy stocks low and hope to sell high. In reality, their profession is trading, much like a person who owns a retail shop and buys items at wholesale and sells them at retail. There's still something they physically must do to generate the money, so they would fit more into the S quadrant than the I quadrant.

Can all of these people be investors? The answer is yes, but it is important to know the difference between someone who earns money from commissions, sells advice by the hour, or tries to buy low and sell high compared to someone who earns money from spotting or creating good investments.

There's one way to find out how good your advisors are: Ask them what percentage of their income comes from commissions or fees versus the percentage that comes from passive income from their investments or other businesses they own.

I have several CPA friends who tell me, without violating client confidentiality, that many professional investment advisors have little in the way of income from investments. In other words, "They don't practice what they preach."

Advantages of Income from the I Quadrant

So the primary distinction of people who earn their money from the I quadrant is that they focus on having their money make money. If they're good at it, they can have that money work for them and for their family for hundreds of years.

Besides the obvious advantages of knowing how to make money with money and not having to get up and go to work, there are also many tax advantages that aren't available to people who have to work for their money.

One of the reasons the rich get richer is because they can make millions and pay, legally, little or no tax on that money. That's because they make money in the asset column, not in the income column. They make money as investors, not workers.

Moreover, people who work for money are often taxed at higher rates than investors, and their taxes are withheld from their wages. They never even see that portion of their income.

Why Aren't More People Investors?

The I quadrant is the quadrant for working less, earning more, and paying less in taxes. So why aren't more people investors? The reason is the same reason many people don't start their own businesses. It can be summed up in one word: risk.

Many people don't like the idea of handing over their hard-earned money and, possibly, not having it come back. Many people are so afraid of losing that they choose not to invest, no matter how much money they could make in return.

A Hollywood celebrity once said: "It's not return on the investment that I worry about. It's the return of the investment."

This fear of losing money seems to divide investors into four broad categories:

1. People who are risk-averse and do nothing but play it safe, keeping their money in the bank
2. People who turn the job of investing over to someone else, such as a financial advisor or a mutual-fund manager
3. Gamblers
4. Investors

The difference between a gambler and an investor is simple. For a gambler, investing is a game of chance. For an investor, investing is a game of skill. And for the people who turn their money over to someone else to invest, investing is often a game they don't want to learn. The important thing for these individuals is to choose a financial advisor carefully.

Later in this book, I'll go into the five levels of investors which should shed more light on this subject.

Risk Can Be Virtually Eliminated

The good news about investing is that risk can be greatly minimized or even eliminated, and you can still receive high yields on your money, if you know the game.

A true investor wants to recoup his or her money quickly. People who have a retirement account have to wait years to find out if they'll ever get their money back. This is the most extreme difference between a professional investor and someone who sets money aside for retirement.

It's the fear of losing money that causes most people to seek security. Yet the I quadrant is not as treacherous as many people think. The I quadrant is like any other quadrant. It has its own skills and mindset. The skills to be successful in the I quadrant can be learned if you're willing to take the time to learn.

A New Age Begins

In 1989 the Berlin Wall was torn down, as was communism. This, in my opinion, signaled the end of the Industrial Age and the start of the Information Age.

The Difference Between Industrial-Age Pension Plans and Information-Age Pension Plans

The voyage of Columbus in 1492 roughly coincides with the start of the Industrial Age. The fall of the Berlin Wall in 1989 is the event that marked the end of that age. For some reason, it seems that every 500 years in modern history, great cataclysmic changes occur. We're in one such period right now.

That change has already threatened the financial security of hundreds of millions of people, most of whom are not yet aware of the financial impact of that change and many of whom can't afford it. The change is found in the difference between an Industrial-Age pension plan and an Information-Age pension plan.

When I was a boy, my rich dad encouraged me to take risks with my money and learn to invest. He'd always say, "If you want to get rich, you need to learn how to take risks. Learn to be an investor."

At home I told my educated dad about my rich dad's suggestion that we learn how to invest and manage risk. My educated dad replied, "I don't need to learn how to invest. I have a government pension plan, a pension from the teachers union, and guaranteed Social Security benefits. Why take risks with my money?"

My educated dad believed in Industrial-Age pension plans, such as government-employee pensions and Social Security. He was happy when I signed up for the U.S. Marine Corps. Instead of being worried that I might lose my life in Vietnam, he simply said, "Stay in for 20 years, and you'll get a pension and medical benefits for life."

Although still in use, such pension plans are becoming obsolete. The idea of a company being financially responsible for your retirement and the government picking up the balance of your retirement needs through pension schemes is an old, outdated idea.

People Need to Become Investors

As we move from defined-benefit pension plans (or what I call Industrial-Age retirement plans) to defined-contribution pension plans (or Information-Age pension plans), the result is that you, as an individual, must now be financially responsible for yourself. Amazingly, few people have noticed the change and understand its ramifications.

Industrial-Age Pension Plans

In the Industrial Age, a defined-benefit pension plan meant that the company guaranteed you, the worker, a defined amount of money (usually paid monthly) for as long as you lived. People felt secure because these plans assured a steady income.

Information-Age Pension Plans

But in 1974, the rules changed with the passage of the Employee Retirement Income Security Act (ERISA). Suddenly, companies were no longer guaranteeing financial security at the end of your working days. Instead, employers began offering defined-contribution retirement plans. "Defined contribution" means that you only get back what you and the company have contributed while you were working. In other words, your pension is defined solely by what has been contributed. If you and your company put no money in, then you get no money out.

The good news is that, in the Information Age, life expectancy has increased. The bad news is that you might outlive your pension (if you even have one).

Risky Pension Plans

What many people don't understand is that whatever you and your employer put into the plan is no longer guaranteed to exist when you decide to pull it out. This is because plans like the 401(k) and the superannuation are subject to market forces. In other words, one day you could have a million dollars in the account. But, if there were a stock-market crash, which every market occasionally has, your million dollars could be cut in half or even wiped out. With defined-contribution plans, the guarantee of lifelong income is gone.

People today, who retire at age 65 and begin to live on their defined-contribution plan, could run out of money by, let's say, age 75. Then what do they do? Dust off the resumé?

And what about the government's defined-benefit pension plan? Well, in the United States, Social Security is expected to be bankrupt by the year 2037, with Medicare bankrupt by 2017. Even today, Social Security doesn't provide much in the way of income. What will happen when 77 million baby boomers begin to want the money they paid in, but it's not there?

In 1998, President Clinton's popular cry of "Save Social Security" was well received. Yet as Democratic Senator Ernest Hollings pointed out, "Obviously, the first way to save Social Security is to stop looting it." For decades, the federal government has been responsible for "borrowing" the retirement money for expenditures: a government-sanctioned Ponzi scheme.

Many politicians seem to think that Social Security is income that can be spent, rather than an asset that should be held in trust.

Too Many People Counting on the Government

I write my books and create products, such as the educational *CASHFLOW* board game, because the Industrial Age is history, and we must prepare for the opportunities of the Information Age.

My concern as a private citizen is that, from my generation forward, we aren't properly prepared to handle the differences between the Industrial Age and the Information Age. A case in point is how we prepare financially for our retirement years. The idea of "go to school and get a safe, secure job" was a good one for people born before 1930. Today, everyone needs to go to school to prepare for a job or career, but we also need to know how to invest—and investing is not a subject taught in school.

One of the problems created by the Industrial Age is that too many people are dependent upon the government to solve their individual problems. Today we're facing even bigger problems because we have delegated our personal financial responsibility to the government.

It's estimated that by the year 2020, there will be 275 million Americans, with 100 million of them expecting some kind of government support. This will include federal employees, military retirees, postal workers, teachers, other government employees, and retirees expecting Social Security and Medicare payments. They're contractually correct in expecting government support because, in one way or another, most have been investing into that promise throughout their working lives. Unfortunately, there were too many promises made for too many years. Now the bill is coming due.

I don't think those financial promises can be kept. If our government begins to raise taxes even higher to pay for those promises, those who can escape will escape to countries that have lower taxes. In the Information Age, the term “offshore” won’t necessarily mean another country as a tax haven. Offshore could mean cyberspace.

A Great Change Is at Hand

I recall President John F. Kennedy warning, “A great change is at hand.” Well, that change is here.

Investing without Being Investors

The change from defined-benefit to defined-contribution pension plans is forcing millions of people throughout the world to become investors, with little investor education. Many people who have spent their lives avoiding financial risks are now being forced to take them. Most will find out when it comes time to retire whether they were wise investors, or careless gamblers.

Today, the stock market is fueled by many things, one of which is non-investors trying to become investors. Their financial path looks like this:

A large majority of these people, the E's and S's, are people who by nature are security-oriented. That's why they seek secure jobs or start small businesses they can control. Because of the defined-contribution retirement plans, they're migrating today to the I quadrant where they hope they'll find security when their working years are over. Unfortunately, the I quadrant is not known for its security. The I quadrant is the quadrant of risk.

Because so many people on the left side of the CASHFLOW Quadrant come looking for security, the stock market responds in kind. That's why you often hear the following words:

1. ***Diversification***

   People who seek security use the word "diversification" a lot. Why? Because the strategy of diversification is an investment strategy for "not losing." It's not an investment strategy for winning. Successful or rich investors don't diversify. They focus their efforts.

   Warren Buffett, possibly the world's greatest investor, says this about diversification: "The strategy we've adopted precludes our following standard diversification dogma. Many pundits would therefore say the strategy must be riskier than that employed by more conventional investors. We disagree. We believe that a policy of portfolio concentration may well decrease risk if it raises, as it should, both the intensity with which an investor thinks about a business and the comfort level he must feel with its economic characteristics before buying into it."

   In other words, Warren Buffett is saying that portfolio concentration, or focusing on a few investments rather than diversifying, is a better strategy. In his mind, concentration rather than diversification requires you to become smarter and more intense in your thoughts and actions. His article goes on to say that average investors avoid volatility because they think volatility is risky. Warren Buffet says instead, "In fact, the true investor welcomes volatility."

When Kim and I were escaping from financial struggle to financial freedom, we didn't diversify. We concentrated our investments.

2. ***Blue chip stocks***
   Security-minded investors usually buy blue-chip companies. Why? Because in their mind, they're safer. While the company might be safer, the stock market is not. These stocks won't protect your money in a market free fall.

3. ***Mutual funds***
   People who know little about investing feel more secure turning their money over to a fund manager who they hope will do a better job than they can. This is a smart strategy for people who have no intention of becoming professional investors. But the problem is that, as smart as this strategy is, it doesn't mean that mutual funds are less risky.

Today, the market is filled with millions of people who, by nature, are security-minded. But, due to the changing economy, they are being forced to cross from the left side of the CASHFLOW Quadrant into the right side, where their brand of security doesn't really exist. That causes me concern.

Great Economic Upheavals Coming

The stage is set for a great economic upheaval. Such upheavals have always marked the end of an old era and the birth of a new one. At the end of every age, there are people who move forward, and other people who cling to ideas of the past. I'm afraid that people who still believe their financial security is the responsibility of a big company or big government will be disappointed in the coming years. Those are ideas of the Industrial Age, not the Information Age.

No one has a crystal ball. I subscribe to many investment news services and each one says something different. Some say the near future is bright. Some say a market crash and major depression are right around the corner. To remain objective, I listen to both sides, because both have points worth listening to. I do not play fortune-teller, trying to predict the future. Instead, I work at staying educated in both the B and I quadrants and being prepared for whatever happens. A person who is prepared will prosper no matter which direction the economy goes, whenever it goes.

If history is any indicator, a person who lives to the age of 75 should anticipate going through one depression and two major recessions during his or her lifetime. My parents went through their depression, but the baby boomers have not—yet.

Today we all need to be concerned with more than just job security. I think we must also focus on our own long-term financial security and not leave that responsibility to a company or the government. The times officially changed when companies said that they were no longer responsible for your retirement years. Once they switched to the defined-contribution retirement plan, the message was that you were now responsible for investing in your own retirement. Today, we all need to become wiser investors, always aware of the ups and downs of the financial markets. I recommend learning to be an investor rather than giving your money to somebody else to invest for you. If you simply turn your money over to a mutual fund or to an advisor, you may have to wait until you're 65 to find out if that person did a good job. If they did a lousy job, you may have to work for the rest of your life. Millions of people will have to do just that because it will be too late for them to invest or learn about investing.

Learn to Manage Risk

It is possible to invest for high returns with low risk. All you have to do is learn how it's done. It is not hard. In fact, it's much like learning how to ride a bike. In the early stages, you may fall down, but after a while, the falling stops and investing becomes second nature, just as riding a bicycle is for most of us.

The problem with the left side of the CASHFLOW Quadrant is that most people go there to avoid financial risk. Instead of avoiding risk, I recommend learning how to manage financial risk.

Take a Risk

People who take risks change the world. Few people ever get rich without taking risks. Too many people have come to depend on government to eliminate the risks of life. The beginning of the Information Age should have ushered in an era of smaller government because big government is frankly too expensive to maintain. But rather than becoming savvy, educated investors, millions of people around the world have bought into the archaic idea of entitlements and pensions for life. This simply isn't feasible. The Information Age means we all need to become more self-sufficient, grow up and take personal responsibility for our retirement.

The idea of "study hard and find a safe, secure job" is an idea born in the Industrial Age. We're not in that age anymore. The times are changing. The problem is that many people's ideas have not changed. They still think they're entitled to something. Many still think that the I quadrant is not their responsibility. They continue to think that the government, big business, a labor union, their mutual funds, or their family will take care of them when their working days are over. For their sake, I hope they're right. These individuals have no need to read further.

Rich Dad's CASHFLOW Quadrant was written to help individuals who want to make the move from the left side to the right side but don't know where to start. Anyone can make the move with the right skills and determination.

If you've already found your own financial freedom, I say, "Congratulations." Please tell others about your path and guide them if they want to be guided. Teach them, but let them find their own path, for there are many paths to financial freedom.

Regardless of what you decide, please remember this: Financial freedom might be free, but it doesn't come cheap. Freedom has a price, and to me it's worth that price. The big secret is this: It takes neither money to be financially free, nor a good formal education. It also doesn't have to be risky. Instead, freedom's price is measured in dreams, desire, and the ability to overcome disappointments that occur along the way. Are you willing to pay the price?

One of my fathers paid the price. The other didn't. But he paid a different kind of price.

The B-Quadrant Quiz

Are you a true business owner?

You are if you can answer "Yes" to the following question:

Can you leave your business for a year or more and return to find it more profitable and running better than when you left it?

❍Yes

❍No