Beginner Investors: The Biggest Lesson of 2018 Comes Courtesy of Warren Buffett

Description

One of the biggest mistakes a new investor could make is following the general investing public in and out of stocks at a whim. For those who haven't done their homework on what the stock market is all about, that's a sure-fire way to scare yourself out of the game for good.

I hate repeating myself, almost as much as I hate coming across as glib, but I'm going to say it again: don't follow the herd and don't even try to time the market! That's speculating, not investing, especially if you buy a stock solely because of momentum, as many newbies do when they first start.

New investors should look to leading exemplars like Warren Buffett, the greatest investor and teacher of our time, and seek to adopt his principles of investment. The man is a contrarian investor, and he's all about getting a dollar for a dime. He couldn't care less about what's deemed as "sexy" at a given point in time, because it's this chasing of sexy assets that gets most investors, even the pros, into trouble, as the public begins to realize how hideous the valuations are on such "sexy" assets.

Most importantly, Buffett doesn't bite the paradigm shift that euphoric investors believe in every time the stock markets surge to remarkably high levels.

As the bulls yell, "it's going to be different this time" in the mainstream financial media, as they usually do, other investors begin buying into the bull thesis in spite of potentially frothy valuations. The investing public continues to grow increasingly bullish, as the overly positive news cascades until the stock market eventually overruns its target, inevitably correcting back to levels that are more aligned with reality.

2018 served as a massive lesson (or reminder) for investors

It's this "reversion to the mean" that's happened countless times over in the stock market's existence, and almost every time, euphoric investors are let down as the markets, their unbalanced portfolios, and their extremely bullish theses end up crumbling. And for those who doubled down on their bets, they took a one-two punch to the gut courtesy of Mr. Market.

It's hard to believe that the S&P 500 hit an inflection point, "melting up" just one year ago today. Everybody was a raging bull on Donald Trump's corporate tax cuts and their implications on earnings and an economy that was smoking hot. It was the party that nobody wanted to miss out on, and with smart folks like Ray Dalio saying things like you'll "feel stupid" by holding cash, it's not a mystery as to why so many of today's new investors are feeling that the stock market just isn't their cup of tea.

I took the parabolic market move as an opportunity to re-instill prudence by encouraging investors follow Buffett, and not Dalio, by keeping dry powder on the sidelines in spite of the apparent paradigm shift in the stock markets.

Buffett says to "be fearful when others are greedy, and greedy when others are fearful," and if you'd adopted his principles, you'd minimize the probability of buying high and selling low — something that many rookie investors likely did in 2018.

Rookies: Here's your game plan for 2019

As a new investor, you should stick with diversified low-volatility baskets of stocks, like **BMO Low Volatility CAD Equity ETF** (TSX:ZLB), in turbulent times like these. As the fear gauge spikes, the ZLB is the one-stop-shop investment that you should be accumulating, and unlike most other securities, the securities within the ZLB are hand-picked based on numerous metrics — the most obvious being the possession of a low correlation to the broader markets.

As a new investor, you should seek to keep your portfolio's correlation to the broader market as low as possible while you remain adequately diversified. That way, you'll eliminate the degree of unsystematic risk you'll take on, and your portfolio won't suffer excessive amounts of volatility.

Foolish takeaway

If you're a beginner, adopt Warren Buffett's principles as your own, keep things simple with diversified ETFs like the ZLB, and keep your volatility low, at least until you're knowledgeable enough to stomach the rougher waters, where the bigger fish swim!

Stay hungry. Stay Foolish.

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