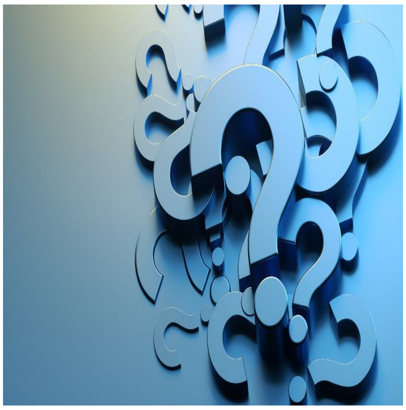

Should You Follow Warren Buffett’s Advice to Buy the Broad Stock Market?

Description

During the last Berkshire Hathaway annual shareholders meeting, Warren Buffett said that the best thing to do for most people is to buy the stock market rather than picking stocks. It’s not the first time he gives this advice to investors. Is it something you should apply? Let’s look at the reasons why Buffett is saying this.

Buying the market gives you diversification

Warren Buffett thinks that the average investor should buy the broad stock market and hold it for a long period rather than following others’ stock-picking advice.

Americans who want to invest in the overall market buy the **S&P 500**. Here in Canada, we have the **S&P/TSX Composite**. This stock market index tracks the performance of Canada’s largest companies by market capitalization on the TSX. You can invest in the S&P/TSX Composite through an ETF like the **iShares Core S&P/TSX Capped Composite Index ETF**.

One of the big benefits of buying the TSX is diversification. Diversification is important to lower your risk of losing money. When you buy an ETF tracking the TSX, you buy about 250 stocks in just one fund, so it’s a fairly simple way to gain exposure to many different companies. Plus, ETFs charge low fees.

However, if you pick individual stocks, you have to choose them one by one. To have a diversified portfolio, you have to buy several stocks – ideally at least 20. It costs more than buying the broad market and you are less diversified. Plus, picking stocks involves time doing research.

You can beat the market by buying individual stocks

However, there are downsides to just buying the whole stock market. You could get richer quicker by picking stocks. Taking the time to do your research and pick quality stocks could allow you the beat the market. Owning individual stocks is riskier than buying the index, but your return can be much higher.

The TSX is highly concentrated in financials and energy stocks, which haven't performed well in 2020. Consumer stocks have performed better, but their weight in the index is small. By picking stocks yourself, you can choose the winners and invest more in them.

For instance, **Dollarama** (TSX:DOL) has been less hit than the broad stock market during the pandemic. While the TSX is down 13% year-to-date, Dollarama stock only fell by 1%.

Dollarama sells essential products at low prices, which people are looking for during a recession. Dollarama's stores with street access remained open during the pandemic, as it has been recognized as an essential business in Ontario and Quebec.

While the dollar chain's sales are expected to be flat in fiscal 2021, they are expected to increase by more than 10% in 2022. Earnings are estimated to fall by about 3% but are expected to soar by more than 27% in 2022.

Dollarama's weight in the **iShares Core S&P/TSX Capped Composite Index** ETF is less than 1%, so it doesn't impact much the ETF price. But if you invest let's say 10% of your portfolio in Dollarama, its good returns will impact your portfolio and you can beat the market. This is the kind of stock you can just buy and then hold for years.

Who said it was hard to beat the market? Warren Buffet did it by buying solid undervalued companies and you can do it too.

CATEGORY

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