How Beginner Investors Can Become Numb to Extreme Volatility

Description

As the COVID-19 pandemic ravages on, many beginner investors are likely to discover that they've been overly complacent after. There's no question that stocks are potentially at risk of another "Wile E. Coyote" type of drop that could see a massive flock of beginners rushing to the exits. And like back in February and March, investors shouldn't expect the exits to be clear, as volumes could overwhelm various brokerages again, especially the free ones (you get what you pay for).

Come the next vicious market sell-off, you shouldn't assume that the markets will be open and that you'll be able to ditch your worrisome positions before the herd. Like during the crash of 1929, many investors didn't find out the extent of the damage done to stocks until much later. And by then, it was likely too late to sell, as the actual price of any given stock was probably much lower than was on that delayed ticker symbol. While you will know the price of a stock second by second, you shouldn't expect your broker to be ready and working in another massive cash-crunching rush out of the markets.

At a time like this, boring is beautiful

So, what's the solution? Don't look for a broker with a better track record of staying upright during vicious panic-induced sell-offs. Instead, take a page out of Warren Buffett's playbook by buying and holding pieces of companies you'd be comfortable holding if the brokerages were to shutter for the next day, week, month, or even the next year. As unlikely is it is to have discount brokerages out of service for weeks, months, or years, positioning yourself to not care about such outages is the best course of action for many beginners to prevent rash selling decisions when liquidity dries up.

In times of turmoil, sometimes dull is beautiful. Stick with stocks that are resilient (enough) in the face of pandemics, recessions, or depressions, such that you wouldn't be rattled if the markets were to implode again and shut down for weeks at a time. We're talking about companies with strong balance sheets and resilient operating cash flow streams — businesses that you know would be minimally affected by a worsening of this crisis.

How to become numb to off-the-charts volatility

Think of lesser-correlated, low-beta companies like **Cascades** (TSX:CAS) that deserve to trade in their own world but may not in times of panic. The company makes tissue and paper products, mostly from recycled fibres. While low correlations to the broader market go out the door, when panic-induced, cash-crunching sell-offs hit, such undeserved downward moves in robust businesses are more likely to be corrected to the upside in a timelier manner than stocks that deserve to be sold off.

Cascades was one of the babies that were thrown out with the bathwater back in February and March. Despite being a firm that was positioned to benefit from the pandemic through the panic-buying and hoarding of tissue products, the stock proceeded to decline around 18% before bouncing back very sharply, recovering all of the lost ground before sustaining a rally to fresh 52-week highs, as it should have in an efficient market.

Foolish takeaway for beginner investors

If the markets were to close for the next week, you'd probably be as cool as a cucumber holding onto Cascades stock as opposed to some penny stock or airline that could stand to crumble like a paper bag. Far too many beginner investors are investing to maximize upside when they should be investing to not scare themselves out of the markets permanently.

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Date
2025/06/28
Date Created
2020/09/29
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