



Warren Buffett: How Should You Prepare for the Next Market Crash

Description

The pandemic was indeed the black swan event for markets this year. The outlook was too bleak when markets crashed more than 35% in just a few weeks in March. After large ups and downs, stocks have managed to pull some gains for the year.

But we are not out of the woods yet. Even with the developments on the vaccine front and decent corporate earnings growth, big uncertainties on the economic recovery front remain. Whether we will see another crash next year remains to be seen. But investors should be prepared for the most unexpected events in the market.

Warren Buffett on market crashes

The legendary investor Warren Buffett has been playing it very safe for the last few years. In the 2016 [annual letter](#) to shareholders, Buffett stated, “Charlie [Munger] and I have no magic plan to add earnings except to dream big and to be prepared mentally and financially to act fast when opportunities present themselves. Every decade or so, dark clouds will fill the economic skies, and they will briefly rain gold. When downpours of that sort occur, it’s imperative that we rush outdoors carrying washtubs, not teaspoons. And that we will do.”

Market crashes indeed dent your portfolios and rob you of your unrealized gains. But what they bring is worthy opportunities that one might not get during the usual course of investing. That’s why savvy [investors don’t panic in crashes](#) but rather pounce on the opportunities.

Keeping a decent cash balance just to plough in during the market crashes would be advisable. In his 2018 letter, Warren Buffett said, “I will never risk getting caught short of cash.” And that’s why his financial fortress **Berkshire Hathaway** is sitting on a cash pile of almost \$150 billion. With such a huge cash hoard, he will probably have the last laugh if markets do crash next year.

But how can everyday investors like you and me can play the crash?

One can consider investing in defensive stocks that generally have a low correlation with broader markets. Consider top Canadian utility stock **Fortis** ([TSX:FTS](#))([NYSE:FTS](#)). It is a classic defensive stock that pays stable dividends.

It generates a large portion of its earnings from regulated operations, which provides [long-term stability](#). Utility stocks like Fortis are generally perceived as recession-proof, because they generate stable returns even in market downturns.

Fortis stock has delivered average annual total returns of 14% in the last two decades, notably outperforming the TSX Composite Index.

Gold

The yellow metal remains one of the attractive investment avenues for the next year. Rather than sitting with the commodity itself, I think gold miner stocks offer larger growth potential.

The world's second-biggest gold miner **Barrick Gold** ([TSX:ABX](#))(NYSE:GOLD) looks attractive at current levels. Berkshire Hathaway holds 12 million shares of Barrick Gold as of September 30, 2020.

As developed economies release large stimulus packages amid the gruesome pandemic, this creates more debt and pressurizes the dollar. Thus, the yellow metal increases when the dollar goes down.

Gold miners like Barrick more than doubled their earnings this year due to higher gold prices. The trend might continue next year with a positive outlook for the yellow metal.

Bottom line

A market crash is a part of an investing game. Those who panic and sell might avoid a momentary loss, but they also give up the huge gains. Only those who stay with their stocks amid the downturn get to reap big rewards in the long term. The 2020 market crash and the subsequent rally just proved that.

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Author

vinitkularni20

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