3 Mistakes Regular Investors Make in Meme Trading

Description

This year has seen big for hedge funds, as they suffer at the hands of an army of retail investors. A few have made significant gains trading meme stocks, while many have caught a falling knife. In the case of **BlackBerry** (TSX:BB)(NYSE:BB), the sharp rise has sustained so far. The tide could turn anytime, and the stock could undergo a sharp decline, as it did back in January.

Remember, meme stocks don't operate on the same principles as normal stocks. This new wave of social trading created by online zero-commission brokers has given millennials the power to trade at their fingertips. The best and most effective way to reach out to this segment of the population is through memes. It was only in 2021, the concept of meme trading appeared.

On that note, here are three common mistakes regular investors make while trading meme stocks.

Chasing the wrong rally of meme trading

Investors who saw the stock rise sharply scrambled to hop on the bandwagon swiftly. In the process, they managed to buy the stock at higher prices. Now, they will be hoping for another spike or they will have to book losses. This is a common mistake among beginner investors as well. When they see a stock price rise, they experience a fear of missing out and end up chasing the rally and buying the stock at a higher price.

Now, this strategy works for stocks that are in a long-term uptrend and have fundamentals to push the growth. But a meme-trading rally is short-lived, as the price is inflated only to book short-term profits.

Investors should exercise restraint and try and gain a better entry during a correction rather than chasing an artificial rally.

Not booking profits in the rally

The majority of retail investors are still holding on to BlackBerry after its share price went parabolic. This is the reason the stock is still hovering around $17 after hitting $24. Investors who are sitting on large gains should book some profits after such a surge in price. But, unfortunately, regular investors hold on to their gains for far too long, hoping for another spike in stock price. And that is usually their undoing.

In regular stock trading, holding the stock pays off through passive investment. While you can hold on to BlackBerry for its future growth potential, you should book some profit if you are sitting on large gains. An $18 price is something that will take years to materialize, going the fundamental way. Some investors get greedy and try to get unreasonable premium instead of booking profit quickly.

If you can’t convince yourself to sell all the stocks, divide your holdings into two or three tranches and set a different sell price. For instance, you can sell 25% of your holding for $18, 25% for $17, 25% for $16, and hold the remaining 25%. This way, you won’t miss the meme-trading rally.

Betting more than they can afford to lose on meme stocks

While betting on meme stocks, regular investors often allocate too much of their portfolio on one trade. This can be very dangerous, particularly when investing in a high-volatility stock. A sharp price drop can wipe out entire portfolios in a matter of seconds. Therefore, those looking to bet on meme stocks and a probable “gamma squeeze” should exercise restraint and only bet what they can afford to lose.

Final thoughts

Trading in meme stocks can return multifold profits, but it can also destroy your capital. If you are looking to bet, follow the above three principles and exit with small losses if you bought around the peak. It would be wise to invest your capital elsewhere if you want to build wealth in the long term.

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