Getting Started in Investing

Most people start off having some degree of problem being able to "pull the trigger", as they say in the industry. Making the first investment can be very difficult. Some people get over it fairly quickly, others take longer and some always find it difficult.

My first thought is that it is not a bad thing in a way. The people who are the greatest danger to themselves in the market are the ones with no fear. They always end up being over active and lose a lot of money. So, some degree of caution in our makeup is a sign that we have learned from experience in the market and in life. However, it is not a good thing to be so cautious that we never take a risk.

My next thought is about risk and follows on from the previous paragraph. When looked at in the abstract, theoretical way, profits (and losses, of course) are made by assuming risk. If there was no risk, everyone else would already have arbitraged away whatever profit opportunity there was. So, the nature of investing is that you assume risk. The key to success is in recognising the risk and managing it sensibly.

The way we manage risk sensibly is a big subject. However the three key techniques are

1. Market exposure - limit the total amount of your investing funds that are exposed to risk at any one time in inverse proportion to the level of market risk you perceive. So, when market risk is high, you have a lower proportion of your funds in the market.
2. Diversification - you spread your invested funds out over several positions, so that failure of one investment is not catastrophic to your portfolio.
3. Position risk - you limit the percentage of your investing capital that is risked on any one investment.

The way I invest is that I have developed an investment plan that deals with all the risks that I see in investing. I have strategies for the key architecture of my plan and tactics for how I manage investments. I know this plan works in the medium to long term, because I have tested it thoroughly. This gives me confidence that it will work, even if there are short-term periods where it does not work so well.

Having a plan like this makes decision making much easier. I have a clear framework for decisions. I find that most people who have trouble making investing decisions do not have a clear plan of what they are trying to do and how. So, everything is a big area of doubt, with which they wrestle constantly.

Now, it takes time to develop such a plan, but it is what all successful investors eventually do. There are many successful investing plans.

It is also very important to understand that investing involves losses. There is no "perfect" method to invest, where every investment is a winner. The key is only assuming reasonable risks and managing them sensibly.

The other problem some people have is that they try to follow a plan that is somehow in conflict with their attitudes, beliefs and tolerance for risk. They will continue to sabotage themselves in unconscious and subtle ways.

Finally, many investors complain that they lost money listening to a broker. There are several things here:

- We must all take responsibility for our investment. If a broker, or anyone else, suggests something, they are not taking responsibility for it being right for us. The investment will not be done unless we say to the broker that we want to place the order. At that point we must own the decision. The broker's advice is only one input to that decision.
- Listening to the broker could not have been the reason anyone loses lots of money. We only lose lots of money if our money management is deficient in some way. This comes back to the investing plan. Losses are the result of unsuccessful management of risk.
- Many investors misunderstand what a broker's role is. It is clearest in a discount broking situation - he or she does executions for you. In a full service broking situation, the broker is selling you his or her wider service. A broker is a middleman. The broker makes money by transacting business for you. The more business you transact, the more the broker makes. Everything the broker says to us or does for us is by way of facilitating our doing business through him or her. I often joke that broker is spelled b-r-o-k-e-r, but pronounced "salesman". If a broker were a brilliant investor, he or she would not be working as a client adviser. This is not to say we cannot get good advice from a broker, but we must understand what is going on and assess the inputs we get from the broker ourselves.

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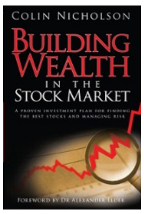

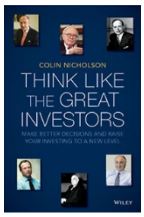

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