How to Invest Your First $1,000

(This article is intended for a yield-hungry individual willing to take more risk than a standard risk-averse investor).

Congratulations! You have officially saved up $1,000 to put into the stock market. And I bet you're probably wondering, "Where should I invest?".

Here are some common answers: Apple, Amazon, Facebook, Google (Alphabet)…other big names

Yep, that's the average individual's response, and I want to deconstruct it to reveal some interesting insights behind the average investor's market sentiment.

So, why these large companies? For starters, most people understand and are acquainted with these businesses, use them on a regular basis, and are very familiar with what these companies do. Fair enough, this saves a lot of time spent researching and understanding other business and revenue models. They have historically strong performances, delivering attractive returns over long holding periods. But most probably, you have heard several people advocate for these companies.

The novice investor reveals some interesting things about her behavior. Firstly, she is unwilling to spend the hours researching new companies and understanding alternate business models. Fair, as most people will assign that duty to their financial advisor or investment manager. Moreover, people rely on word of mouth. This precludes the ability to conduct thorough due diligence and possibly, develop a contrarian point of view to public opnion. Investor just want positive returns over long periods (as is expected).

If we dig a little deeper, we know that a lot of people have probably heard of Amazon, but how many know about Beacon Roofing Supply, Inc.? I'm guessing not as many. Well, guess what? The same rules apply in the world of sell-side analysts. You will probably see 40+ analysts covering the big companies like Apple and Alphabet, but far fewer looking for smaller ones.

Applying an efficient market hypothesis lens, which simply states that there are 3 forms of efficiency regarding information being discounted into a stock price, we can draw some notable conclusions. For stocks that are highly popular, being studied by many smart analysts, there is probably more information being integrated into that stock price as opposed to a smaller, less-covered equities. More broadly, more analysts mean more theses. More theses mean more ideas, and all of that is being discounted into the stock's price. If that's the case, there is much less room for error, and your investment thesis might already be considered (and in some cases, refuted).

So, if you are looking to invest your first $1,000 in the next big hit, you might want to start out small. There are thousands of equities in the world and the U.S alone, and there are only so many analysts. You might consider finding stocks with less coverage, lowering Enterprise/Equity Values, that don't have that much analysis by the big banks.

Yes, they exist. You just need to keep your eyes open. You can do a Bloomberg screen using the <EQS> function and adjust your search to your parameters, or even just plug away at Google.

I have written a few pieces on determining potential investment opportunities using fundamental analysis from both a top-down and bottom-up approach. Kindly refer to them using these links:

https://news.wealth365.com/from-the-top-down/
https://news.wealth365.com/bottom-millennials-guide-fundamental-investing/

You should form your independent investment idea, and then consult the existing opinions. Determine why yours is different and if it is logically sound. You want to steer clear of any "gut" reactions, as investing has the potential to turn into a brawl between facts and feelings. If you think you have a new, fresh idea that has the potential to manifest into a lucrative investment, consider the risks that would impede your idea from turning into reality. Everything is subject to risk, even risk itself.

However, before you go into the depths of research and hours reading company filings, I want you to remember what your money means to you and your ultimate goals. Are you sensitive to capital losses, or are you willing to risk it to achieve handsome returns? Is volatility something you can stomach, or are you seeking a more stable investment relative to market fluctuations? Are you willing to endure periods of loss for long-term gain, or would you rather mimic the market? These are just some of the considerations you should take into account before putting your money into a company. If you are confident and believe your money is important to you, than you should place it in the hands of a firm that will treat it with equal respect and help you grow your investment.

If you have considered the following, spent your time efficiently and effectively conducting your due diligence, have constructed a strong and substantiated investment opinion, and established your investment horizon, then you have successfully completed the basics. There is so much that goes into an investment decision for an astute investor, and the more time you spend trying to understand a business, the less surprised you'll be to minor fluctuations. Remember that in the short-run, prices are driven by supply and demand, and how much investors are willing to buy or sell a specific security at. There are several day traders, hedge funds, and algorithmic trading firms selling thousands of securities in hopes of attaining marginal profits to cover capital gains taxes that it may skew your opinion. This is known as "noise". And if you are too busy trading noise, how will you be able to see?

Leave that up to the technical analysts and quantitative firms who create channels and trendlines to minimize capital losses. You don't want to swing on the ups and downs of market sentiment, but rather, stay strong on your investment thesis, believing it will manifest into a true capital gain driven by fundamental strength. This is the marker of a good investment and one that will achieve long-term capital growth for the investors that dedicate their money in helping the company achieve its true potential.

In sum, great investment ideas exist under rocks. You need to be willing to turn a bunch of them until you find your diamond. But most importantly, tune out the noise.

To your success,

Bryan Baratian