Golden rules of investing in stock market

The stock market can be an excellent place to invest over the long term to create wealth. But in order to reap the benefits of investing in the stock market, investors should learn as much as possible about the market, before investing. Whether you are a new investor or have been investing in the stock market for a while, the following should help you to succeed in the market.

- ## Don't buy on tips

A retail investor is typically the last one to know of tips. Hence, he is most likely to invest when the stock has already run up and hence, at a risk to lose money. Try and get research reports from reputed brokers. Learn to read balance sheets and understand the industry the company operates in. Ignore hype and most importantly, do not depend on 'market tips' your friends always give.

- ## Don't invest in a company you don't understand

Famed investor Warren Buffett often discusses the concept of a 'circle of competence'. This circle of competence consists of all the businesses with which the investor is familiar with and thoroughly understands. An investor who has spent the last ten years as a checker at a supermarket would have an advantage when analyzing the financial statements of a grocery store chain. He or she would be able to pinpoint the strengths and weaknesses of the business, evaluate the competitive climate of the industry and compare the performance of a prospective investment against those of an excellent grocer.
Straying from the circle of competence leads a would-be-investor into the land of speculation. Therefore, never buy a stock that you don't understand.

- ## Don't confuse investing and trading

Trading is short term and investing is long term. Getting confused between the two can be a sure way to lose money. You must decide on what your ultimate goal is by participating in the stock market. Not many would argue the fact that a certain amount of skill and research is necessary to make good long-term investment decisions.
It is no different with trading. Take the time to learn what works and what does not. Learn from past mistakes and allow yourself to succeed. Use a trading base of capital that you are comfortable with and allow profits from your trading activity to be rolled into long positions, thus satisfying both strategies.

- ## Don't panic at short-term trouble when your goals are long term

Volatility is the basic characteristic of a stock in short term. Hence, capital erosion should be considered normal. The good news is, although past performance does not guarantee future results, historically, the market has always rebounded from its losses.
If there's one thing the current market has taught investors, it's that diversification is important. Individuals who ignore the time-tested strategies of asset allocation and diversification do so with potentially more risk. As long as your investments are fundamentally sound and fit your financial goals, a temporary downturn in the market should not sway you.

- ## If you need cash in short term, don't invest in stocks

In stock markets, one can benefit only if one can hold on for a reasonably long period. Like the fabled tortoise that beat the hare in the race, the investor who stays in for the long term is more likely to achieve his or her goals than the investor who chases 'hot tips' for quick profits in the stock market.
If you have a long-term perspective, you can change investments that aren't working for other alternatives. However, if you will need the money from your investment in the near future, a mistaken investment can create real problems in meeting your goals.
Investors that begin early and stay in the market have a much better chance of riding out the bad times and capitalizing on the periods when the market is rising.

- ## Don't have excessive expectation about returns

A big part of succeeding as an investor is having the right expectations about what you can achieve by putting your money into stocks. It's not a big secret that people invest because they expect to make money. Indeed, many succeed. But others are disappointed either because they overestimate the return they are likely to get or because they are unwilling to risk any of their principal to earn a higher return.
As you invest to meet your financial goals, it's critical to understand what buying securities can do for your net worth and what it may not be able to do.
Despite all the investing information that's available, it's unclear how many investors really understand the constant fluctuations of the securities markets and what they can reasonably expect to earn on their investments.
It's true that historical trends show that over time, securities, stocks in particular, tend to go up in value. But the shorter the time horizon, the more difficult it is to predict even for investment professionals, what direction the market may be headed. Only one thing is certain: The values of securities will go up in some years and just as surely as they will go down in others.

- ## Don't try to time the market

Market timing is an investment strategy where the investor makes investment decisions, to buy or sell investment securities, based upon predictions of the future.
Buying at the bottom and selling at the top is next to impossible. Take 'buy' and 'sell' calls based on your views on valuations.
Most would agree that market timing may be possible over short periods of time but it is more difficult to consistently and accurately predict stock market movements over long periods of time. For the average investor, a diversified portfolio, held for the long term, is the best strategy.

- ## Don't invest without a plan

A well thought out plan and discipline in implementing it can safeguard your portfolio from impulsive mistakes. Good financial investment advice is to have an investment plan for investment in stock. This is an important means of controlling the potential emotional roller coaster that can be associated with stock investments.
Your success with value investing will largely depend on your temperament and to what extent you can exhibit patience and discipline to make the best investments. Sticking to a plan is part of this process. While plans may vary from investor to investor depending on age, capital available and investment time-line, most plans for investment in stock should have some common elements. These elements include having a buying strategy, a selling strategy, a portfolio management strategy and a strategy for performance management and review.

- **Be diligent**

  The best way to ensure the safety of your money is to be diligent. Get yourself organized and keep your papers in order. If you are applying for an IPO, keep a copy of your application form and cheque. If you are buying and selling through a broker, check your contract notes and file them away safely. If you have all your documents in one place, it is easy for you to spot fraud and take action against it.

  Stock market investing is fraught with risks and not for the faint hearted. But facing the risk of an intelligent and calculated transaction going wrong is one thing and having to lose your money because of greed or laxity is another.