

## New Investor Center



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### 10 investing basics from Buffett

The Oracle of Omaha became the world's richest person by adhering to simple but critical tenets. Here are his rules for smart living and savvy investing.

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By [Michael Brush](#)

MSN Money

Last year's market madness didn't just flush away \$7 trillion in wealth.

It also washed away a lot of investors' confidence and left them stumped about the best position to take now. "Somewhere between cash and fetal," quips one pessimist.

In such downbeat times, let's consider a dose of optimism, wisdom and insight: the basics as taught by that perennial investing Yoda, [Warren Buffett](#).

For new investors or those now starting over, there's good news here because Buffett's investment success comes from some easy-to-grasp human qualities as much as sophisticated expertise in [balance sheets](#).

Buffett would be the first to say his homespun and positive philosophy played a big role in his becoming the richest person in the world (before he gave most of his loot away).

Changing your basic psychology can be tough, so new investors may have a leg up here because they don't have ingrained bad habits. But for anyone, a psychological makeover is worth the effort if you hope to recover your losses in the market's next leg up -- and then make the right moves for the rest of your life.

My tour of the essence of Buffett's wisdom starts with the simple psychological lessons taught by the master, many of which are applicable in life outside investing.

#### Lesson No. 1: Be frugal

If the economic downturn is forcing you to live simply, look on the bright side: It's making you more like Buffett.

Buffett lives in the same modest house in Omaha, Neb., that he bought more than five decades ago. He drives his own car.

How does this make him a better investor? First, it gives him more to invest.

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Second, a frugal investor will demand this quality from managers. Buffett is leery of corporate waste. Excessive executive pay or silly perks are red flags. Buffett once quipped that companies stack pay committees with "sedated Chihuahuas."

Third, frugal people don't need fast returns to support extravagant lifestyles. This leaves them free to think more clearly about when to buy and sell stocks, making them much better investors, believes Stephen Shueh, a Buffett expert and managing partner of Roundview Capital in Princeton, N.J.

#### Lesson No. 2: Wait for the 'fat pitch'

Resist the itch to constantly buy or sell stocks.

"Lethargy bordering on sloth remains the cornerstone of our [investment style](#)," quipped Buffett in his 1990 annual report to [Berkshire Hathaway](#) ([BRK.B](#), [news](#), [msgs](#)) shareholders. Have the patience to wait a long time until some market turbulence brings the "fat pitch," as Buffett calls it, or stocks of great companies trading at really cheap valuations.

#### Lesson No. 3: Be a contrarian

A great way to make money is to go against the crowd. "We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful," Buffett explained in a 1986 letter to shareholders.

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So be skeptical of the conventional wisdom. Not because the crowd is always wrong but because

the crowd's wisdom is probably already reflected in market prices, says Todd Lowenstein, a portfolio co-manager of the **HighMark Value Momentum Fund** ([HMVMX](#)).

When the investing public is extremely negative, it's usually a good time to buy stocks. When investors are confident, be careful.

#### Lesson No. 4: Stick with what you know

One of Buffett's basic rules is: If you don't understand a company's product or how it makes money, avoid it. He calls this "staying within your circle of confidence."

This isn't always easy. During the late 1990s boom, Buffett famously avoided tech companies, confessing that he could not understand what they did. He looked dumb until the bubble burst. "Ultimately, when it came full circle, he was proven right," Lowenstein says.

#### Lesson No. 5: Don't depend on others to say you're right

If you are in need of constant affirmation about your investment decisions, particularly from the stock market, you won't be able to invest like Buffett, points out **Legg Mason** ([LM](#), [news](#), [msgs](#)) money manager Robert Hagstrom in his book "[The Warren Buffett Way](#)."

That's because Buffett makes outsized returns by purchasing disliked [value stocks](#) that are so beaten down they're often virtually ignored by the talking heads. They won't be on TV every week telling you that you made the right choice.

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