Common Investing Errors

Uncertain times often highlight the mistakes that investors can make with their portfolios. During buoyant markets, making money may not seem difficult. However, the reckoning often comes when markets turn down. Suddenly, mistakes can become glaringly apparent. Here are some of the more common investing errors:

Overlooking Diversification — The concentration of assets in too few areas can be a common problem. Despite the broad-based market declines in response to COVID-19, certain sectors have performed very differently. Some technology companies have outperformed as a result of self-isolation practices, whereas industries dependent on travel and tourism have suffered significant short-term setbacks. Even during non-crisis times, regardless of the high quality of investments, there is always the danger that a bad quarter or certain industry developments may adversely affect equity values.

No single asset class has consistently performed at the top over time. As such, investors should maintain a healthy balance of diversification across assets.

Tax Errors — Don't overlook the effect of taxes on your investments. Remember that different forms of investment income can be taxed differently. In a non-registered account, the nominal return from dividends of an eligible Canadian corporation would be higher than the same fixed-income return on an after-tax basis. Capital gain returns are generally taxed at even lower rates. Pay attention to asset location: different income can be taxed differently depending on the type of account (i.e., registered, non-registered) from which income is generated. Using tax-advantaged accounts such as Registered Retirement Savings Plans and Tax-Free Savings Accounts may be great ways to minimize taxes.

Also important: don't be reluctant to sell a security solely because taxes will be triggered. If the fundamentals suggest change or a portfolio needs to be rebalanced, don't let the tax tail be in control.

Failure to Adjust — The financial markets are constantly changing and the prospects of specific companies, industries or even entire classes of securities can be attractive today, but not tomorrow. Be ready to adapt. Equally important, your needs may change and your holdings may require periodic adjustments as circumstances evolve. Remember, you are not marrying a particular security: the purpose of investing is to earn a solid return, not own XYZ company forever.

Acting on Emotion — Fear and greed are said to be the drivers of market sentiment. When euphoria prevails, unsavvy buyers often rush to purchase investments. In contrast, market downturns may offer bargains, yet many investors sit on the sidelines, or, worse, may liquidate portfolios.

Having an investment plan with well-defined objectives can help control emotional pressures. Working steadily towards measurable goals helps to focus on outcomes rather than the process. Other tactics may include a dollar-cost averaging program, which helps to prevent emotion from dictating investment purchases. Avoiding daily attention to the performance of investment accounts may also help to limit emotional responses.

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