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8 Common Investing Mistakes to Avoid

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Investing is by no means always easy and profits are never guaranteed. There are countless books on investing and everyone has different tips and tricks that work for them. Even professional investors aren't always right even after years of practice. Additionally, every investor is different, with different investment goals, risk tolerances, and knowledge. However, there are some common mistakes that all investors should avoid, which we discuss below.

KEY TAKEAWAYS

- Mistakes are common when investing, but some can be easily avoided if you can recognize them.
- The worst mistakes are failing to set up a long-term plan, allowing emotion and fear to influence your decisions, and not diversifying a portfolio.
- Other mistakes include falling in love with a stock for the wrong reasons and trying to time the market.

1. Not Understanding the Investment

One of the world's most successful investors, [Warren Buffett](#), cautions against investing in companies whose business models you don't understand. The best way to avoid this is to build a diversified portfolio of [exchange-traded funds \(ETFs\)](#) or mutual funds. If you do invest in individual stocks, make sure you thoroughly understand each company those stocks represent before you invest.

2. Falling in Love With a Company

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3. Lack of Patience

A [slow and steady](#) approach to [portfolio growth](#) will yield greater returns in the long run. Expecting a portfolio to do something other than what it is designed to do is a recipe for disaster. This means you need to keep your expectations realistic with regard to the timeline for portfolio growth and returns.



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4. Too Much Investment Turnover

[Turnover](#), or jumping in and out of positions, is another return killer. Unless you're an institutional investor with the benefit of low commission rates, the transaction costs can eat you alive—not to mention the short-term tax rates and the [opportunity cost](#) of missing out on the long-term gains of other sensible investments.

5. Attempting to Time the Market

Trying to [time the market](#) also kills returns. Successfully timing the market is extremely difficult. Even institutional investors often fail to do it successfully. A well-known study, "Determinants of Portfolio Performance" (*Financial Analysts Journal*, 1986), conducted by Gary P. Brinson, L. Randolph Hood, and Gilbert L. Beebower covered American pension fund returns. ^[1]

This study showed that, on average, nearly 94% of the variation of returns over time was explained by the investment policy decision. In layperson's terms, this means that most of a portfolio's return can be explained by the asset allocation decision—[not by timing](#) or even security selection. ^[1]

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original cost basis. [Behavioral finance](#) calls this a "cognitive error." By failing to realize a loss, investors are actually losing in two ways. First, they avoid selling a loser, which may continue to slide until it's worthless. Second, there's the opportunity cost of the better use of those investment dollars.

7. Failing to Diversify

While professional investors may be able to generate [alpha](#) (or excess return over a [benchmark](#)) by investing in a few concentrated positions, common investors should not try this. It is wiser to stick to the principle of diversification. In building an exchange-traded fund (ETF) or mutual fund portfolio, it's important to allocate exposure to all major spaces. In building an individual stock portfolio, include all major sectors. As a general rule of thumb, do not allocate more than 5% to 10% to any one investment.

8. Letting Your Emotions Rule

Perhaps the number one killer of investment return is emotion. The axiom that fear and greed rule the market is true. Investors should not let fear or greed control their decisions. Instead, they should focus on the bigger picture.

Stock market returns may deviate wildly over a shorter time frame, but, over the long term, historical returns tend to favor patient investors.

An investor ruled by emotion may see this type of negative return and panic sell, when in fact they probably would have been better off holding the investment for the long term. In fact, patient investors may benefit from the irrational decisions of other investors.

How to Avoid These Mistakes

Below are some other ways to [avoid these common mistakes](#) and keep a portfolio on track.

Develop a Plan of Action

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Also, remember why you are investing your money, and you will be inspired to save more and may find it easier to determine the right allocation for your portfolio. Temper your expectations to historical market returns. Do not expect your portfolio to make you rich overnight. A consistent, long-term investment strategy over time is what will build wealth.

Put Your Plan on Automatic

As your income grows, you may want to add more. Monitor your investments. At the end of every year, review your investments and their performance.

Determine whether your equity-to-fixed-income ratio should stay the same or change based on where you are in life.

Allocate Some "Fun" Money

We all get tempted by the need to spend money at times. It's the nature of the human condition. So, instead of trying to fight it, go with it. Set aside "fun investment money." You should limit this amount to no more than 5% of your investment portfolio, and it should be money that you can afford to lose.

Do not use retirement money. Always seek investments from a reputable financial firm. Because this process is akin to gambling, follow the same rules you would in that endeavor.

1. Limit your losses to your principal (do not sell calls on stocks you don't own, for instance).
2. Be prepared to lose 100% of your investment.
3. Choose and stick to a pre-determined limit to determine when you will walk away.

What Are Common Investing Mistakes?

Common investing mistakes include not doing enough research, reacting emotionally, not diversifying your portfolio, not having investment goals, not understanding your risk tolerance, only looking at short-term returns, and not

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retirement accounts. These are all fairly low-risk investments that should generate some returns for the investor and will allow them to understand the fundamentals of investing.

Can You Invest With \$100?

Yes, you can invest with \$100. You can invest with any amount of money, it just depends on the specific asset. You can invest \$100 in a certificate of deposit as well as in any stock that costs \$100 or less.

The Bottom Line

Mistakes are part of the investing process. Knowing what they are, when you're committing them, and how to avoid them will help you succeed as an investor. To avoid committing the mistakes above, develop a thoughtful, systematic plan, and stick with it. If you must do something risky, set aside some fun money that you are fully prepared to lose. Follow these guidelines, and you will be well on your way to building a portfolio that will provide many happy returns over the long term.

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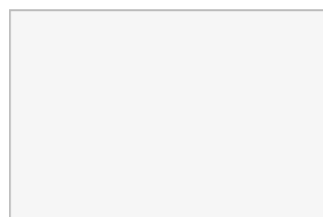
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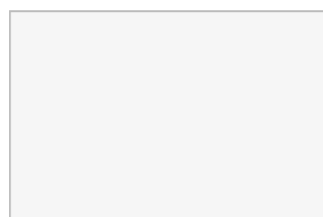
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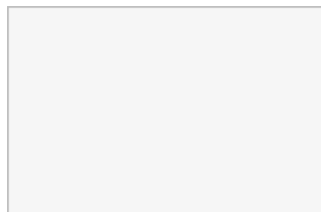
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