INVESTING AND TRADING

Six trading mistakes to avoid

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Being clear on why you are investing helps avoid being overwhelmed by too much information. The trading environment has changed drastically over the past 15 years. Today investors enjoy access to company information within moments of it being announced. Being able to access all this information can be a double-edged sword. While it could help in making better-informed investment decisions, it could also potentially derail you.

Mistakes investors make repeatedly

Being in the trading game, we have noticed that there are six common mistakes investors make repeatedly, namely:

- investing without a plan
- focusing on the wrong trading horizon
- getting caught up in the thrill of the trade
- not rebalancing portfolios often enough
- not investing enough quality time
- chasing recent winners

The good news is that you can avoid making these mistakes if you are aware of them and follow a disciplined approach.

1. Investing without a plan

If you don't know where you're going, any road will take you there and it is easy to go astray. Having a personal investment plan in place can help you avoid this pitfall. A plan will also help you to clarify:

- Goals and objectives – what are you investing for and what do you want to achieve from your investments?
- Risks – what risks are relevant to you or your portfolio? Your goals will determine what risks are appropriate and acceptable to your investment
- Asset allocation – what percentage of your total portfolio will you allocate to local equities, international stocks and other asset classes?
- Diversification – allocating to different asset classes will help you to diversify your portfolio.

You need to be clear about each of these before you start investing.

2. Focusing on the wrong trading horizon

Most investors are too focused on the short term and do not stick to their trading plan. If you are saving for a longer-term goal, like your retirement 25 to 30 years from now, what the stock market does in the next 12 months shouldn't be your biggest concern.

If you are investing for the long term you can afford a more aggressive asset allocation than when you have a shorter investment horizon, like saving for your child's university education, say in five to eight years' time.

3. Getting caught up in the thrill of the trade

Investors often look for easy opportunities to make money when they start trading. The 'feel-good aspect' of making money drives them to chase the next big thing.

Unfortunately, this need to make money sometimes means investors make hasty investment choices based on too little actual research. A typical example of this is getting a tip from a friend at a braai on what promises to be the next quick win. Listening to such trading tips may distract you from your trading goals and cause you to make silly mistakes. To remain true to your investment plan, ask yourself why you are trading, and whether your transactions align to your goals and objectives.

4. Not rebalancing your portfolio often enough

Rebalancing is the process of ensuring your portfolio remains in line with your investment plan and goals. Rebalancing is difficult because it forces you to sell the shares that are performing well, and consequently make up a larger portion of your portfolio than you intended, and buy more of the shares that aren't doing quite as well. For this reason, we find that many investors do not rebalance their portfolios often enough.

Rebalancing is important, because it helps to remove emotion from the trading process. If you do not follow your investment strategy and instead let emotion drive your investment decisions, you could end up deviating from and not achieving your investment plan and goals.

5. Not investing enough quality time

When you invest your hard-earned money, you need to spend time and effort on your investment strategies. You would not walk into the first car dealership you see and buy the first car on the floor. You would rather carefully research different models, compare their 'specs' and consider the costs carefully. It could take quite some time before finally committing to the right car for you.

The same applies to investing in shares. You can only make sound choices when you spend quality time investigating the companies you want to invest in. It might be a good idea to let your financial adviser do it for you should you not have the time or inclination to do this yourself.

6. Chasing recent winners

This factor has probably led to more poor investment decisions than any of the others we have mentioned so far.

Many investors select companies, strategies and sectors because their recent good performance lead them to feel that they are 'missing out on great returns'. The temptation to adjust your plan could be very real if a share or sector has done extremely well for a long time. However, the cycle could well be nearing its end and the smart money could already be moving out. You need to stick to your investment plan and rebalance to avoid this pitfall. This is the exact opposite of chasing performance.

Plan to avoid mistakes

Investors who focus on their investment objectives and plan can recognise and avoid these six common mistakes. They are more likely to achieve their investment goals because they invest with the end in mind. Sadly, none of these make for great conversation starters around the braai, which could be why many investors keep on making the same mistakes.

PSG resources that can help you trade smarter:

- Webinars
- News and articles