

Jim Cramer's

SEVEN DEADLY SINS

*Every Investor
Must Avoid*

TheStreet

There are a lot of mistakes to be made in investing; and most investors have made them. It's important, though to learn from your errors, then move on.

The markets have never been more fast-paced than they are now, and there's never been so much information so readily available to investors. Yet, somehow, we often fail to take advantage of lessons that should have been learned. Perhaps it's just human nature, and we can't help ourselves; which is part of what's been brought forth by the fascinating study of behavioral finance. While the list of possible investment related "sins" is long, below are some of the more common examples.

Not knowing what you own- While it's fine to trust your advisor if you have one, (only if that trust is warranted, and if there is no trust, find a new advisor), it is dangerous to completely abdicate all responsibility for your portfolio to someone else. Sure, you may have hired a professional in the first place because you have neither the time, nor inclination to manage your own portfolio, but you would still be very wise to have an understanding of just what it is that you own. I've seen too many cases where an investor trusted their advisor completely, never asked questions, or understood their investments, until it was too late. Often, the questions are not asked until there is turmoil, and by then, capital has already been lost.

Following the herd- It's easy, and perhaps most comfortable, to do the same things, and buy the same stocks that everyone else owns; those that everyone's talking about. That is the time to run the other way. If there's a positive buzz about a particular name, especially the latest and greatest fad, in all likelihood, the stock has been pushed higher partially because of that buzz. Be wary if your barber, plumber, brother-in-law and neighbor are all touting the same can't-miss name.

Lacking Diversification- This is perhaps the oldest piece of investment advice ever, yet it is still often ignored until it's too late. Owning too much of one company or asset class; or even too much of several investments that are highly correlated to one another is a good way to separate you from some of your capital when the markets take a hit. Just because you own several mutual funds does not mean that you are necessarily diversified. I've seen cases where an individual owned 2 S&P 500 index funds, under the guise that this provided diversification benefits. That's an extreme example. Investors tend to care less about diversification when the general direction of the market is up, and their accounts are growing nicely. Once there is a market correction, or bear market, the old adage "don't put all of your eggs in one basket" is suddenly back in vogue.

Mistaking a great company for a great stock- It's easy to fall in love with a stock, especially those that represent innovative and new products or services. Even the great Peter Lynch invested in companies brought to his attention by members of his family because they liked a particular product. But too often, investors don't connect the dots between a stock and its valuation, as Lynch would. Facebook (FB) is a phenomenon, no doubt, but the aftermath of its IPO demonstrates this point well. It was too expensive; as great as many believe the product is, and as high as the expectations are, there was a huge disconnect with the stock price and its' valuation.

Seven Deadly Sins Every Investor Must Avoid—Simple Rules to Protect One's Account

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Following a Cookie Cutter Approach to portfolio allocation- There's a rule of thumb for everything in investing; such as your "allocation to equities should be 100 minus your age" which is an oldie but a goodie. This and other one-size fits all ignore the fact that all investors are different, and not just because of age. People have different goals, different risk tolerances, and different attitudes toward investing. Some may not sleep well at night during periods of market volatility, while others see downturns as opportunities to buy low. Everyone is different, and portfolios should reflect this.

Not controlling or understanding portfolio expenses- It costs money to run a portfolio; if you are doing it yourself, you are hopefully well aware of what it's cost you in commissions, or what the underlying expenses in your mutual funds are. If you are utilizing an advisor, you may not know what it's actually costing you, and it's important to know. Fees can eat away portfolio returns, and can make a huge difference to the nest egg in the course of an investor's life.

Panicking- Sometimes it's very difficult not to want to throw in the towel during periods of market upheaval; the meltdown of 2008-2009 was a great example. That was an extreme market event, and it shocked some investors to the point that they no longer wanted to own stocks, or have any exposure to equities. You've heard the stories of folks selling out at the very bottom; not only have they lost capital, but they do not participate in the recovery. The emotional baggage can also be devastating; it's difficult for some investors to begin investing again once they've sold when conditions were the worst, then not participated in the recovery. This can be paralyzing. This also ties into # 5 above (Following a Cookie Cutter Approach to portfolio allocation). If your portfolio is properly designed to reflect your goals, and risk tolerances, then there's less likelihood that you'll panic in the first place.

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