

Stock Market: Avoid These Common Mistakes

It's easy to have confidence in investments made during bull markets: share prices climb and any losses from poor decisions are usually recovered fast. But times of increasing market volatility tend to magnify mistakes, and many investors may lose confidence in their decision making.

Let's take a quick look at some of these common, but generally avoidable, mistakes.

1. Timing the Market

During a downturn in the market, investors who regularly contributed to their portfolios when the market was rising often decide to stop investing until conditions improve. This can prove to be a costly mistake.

Not only is it impossible to time the ups and downs of the market with consistent success – by sitting on the sidelines during a down market, you could miss out on an opportunity to buy stocks and other investments at lower prices. In good times and bad, long-term investors should carefully consider the merits of dollar-cost averaging. By continuing to make investments of the same dollar value at regular intervals, investors can buy more shares when prices are low, fewer when prices are high.

A periodic investment plan such as dollar-cost averaging does not assure a profit or protect against a loss in declining markets. Also, since such a strategy involves continuous investment, investors should consider their ability to continue purchases through periods of low price levels.

It is also important to continue to make contributions to your 401(k) plan or similar employee-sponsored retirement plan. These contributions often “earn” matching funding from your

employer, providing additional earnings potential.

2. Skipping the Research

Determining whether an investment is appropriate for your portfolio requires research. There are more companies and investment products to invest in today than ever before, and you need to gather information before you can determine which investments might have potential for growth.

Before making an investment decision, it's helpful to evaluate it in the context of comparable opportunities. At a minimum, you should find two articles (from different authors) about the company or investment product and review the company's website.

Both the investor relations section and news announcements found on the website can provide useful information. You should also review financial statements and carefully investigate anything that looks vague or unusual.

Not only can doing your homework help you to make informed investment decisions, it can also help you to feel comfortable with the holding in spite of temporary ups and downs.

3. Chasing Past Performance

Yesterday's hot stock may have already topped out. Today's innovative start-up may not have the wherewithal to stay in business. So it's important to base investment decisions on more than past performance and a few headlines.

You should invest with the future in mind. If there is strong growth potential, and the fundamental likelihood of the company's success looks good to you, then it may make sense to invest even after a successful run. Keep in mind, however, that past performance is no guarantee of future results.

4. Trading Too Often

Frequent trading often reduces the total return of your portfolio. In addition to the trading fees and taxes that it

may incur, frequent trading does not reflect a long-term outlook and thoughtful investment strategies – neither timing the market nor running from losses enhances your portfolio's performance.

5. Selling Low, or Not at All

Before selling a stock or investment product that has tumbled, it's important to do some additional research to understand why it fell. This research will help you anticipate the holding's potential for recovery. If the setback appears to result from a temporary problem that can be easily overcome, you may even want to consider buying more while the price is low.

Conversely, it's also important to know when to take a loss. It hurts to lose money, but a little pain now may pay off in the long run. If your company or investment relies on an industry that is likely to remain weak for several years, consider selling to avoid any additional losses.

Learning from your own past mistakes, as well as from those made by others, is an important step toward becoming a better investor.

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