Improving Investment Returns

Posted on: June 9, 2014

One Saturday, famed investment manager Peter Lynch was working at the office when he decided to answer the phone. The caller was a holder of his mutual fund who was calling to cash in the investment. Peter explained how he was excited about the growth prospects for the economy and his fund and asked him why. As Peter tells the story the caller said: 'Because I am breaking even!'

The fund went on to record compound growth of about 20% for a decade during the 1980's! Sadly, this investor, like many others, missed the ride. This historical under-performance by investors continues as is confirmed by recent research from Morningstar Inc.

The research confirms what many in the industry already know which is that there is often a gap between the returns earned by the funds and those earned by individual investors. This return gap has usually been attributed to ill-timed buying and selling as investors chase returns, particularly those of hot managers. This is true for both Canadian and US investors.

For example during the tech stock boom in the late 1990's, Canadian investors yanked money out of Canadian equity funds to chase the hot returns in U.S. and global stock funds. The stunning returns on the S&P 500 of 27.8% annual returns from 1994 to 1998 compared to the ho-hum returns of 10.7% for Canada's S&P TSX Composite index, was just impossible to ignore.

You couldn't have picked a worse time to make this move. With the bursting of the tech mania and the rise of the Canadian dollar, an investor who moved to U.S. stocks on Jan. 1, 1999 would still be in the red 14 years later. In contrast, those who had stayed put in the staid Canadian market earned 7.1% annually over the same time frame.

The Morningstar study dug into the reason for the endemic shortfall. It wasn't caused simply by investors chasing individual hot funds; rather it resulted from poorly timed asset allocation shifts in their portfolios. By jumping in and out of domestic and international stocks as well as bonds at the wrong time, investors hurt their own performance by chronically 'buying high and selling low'.

More recently investors are making the same behavioral mistake again. Since 2009, Canadian fund investors reversed field by fleeing equity funds and pouring into the perceived safety of bond funds. The result is that Canadian and global stocks have outperformed Canadian bond funds in three of the past four years. From January 2012 to March 2013, an investor in Canadian and global stocks enjoyed annualized returns of 8.5% and 19.0% respectively, while the Canadian bond investor earned 3.4%. It seems that investors never learn.

There are some steps investors can take along with the help of their advisor to avoid the this dreaded performance gap and more importantly avoid the damage to their retirement income goals and wealth accumulation goals.

This can include periodic portfolio re-balancing by selling the winning investments and buying the under-performing investments as part of your target asset allocation mix. Finally, stop chasing last year's winners!

Call us today for an appointment to discuss your investment goals and portfolio strategy This will ensure you are on track to achieving your lifestyle and financial goals while avoiding the dreaded investment performance gap!

Questions about your investment and portfolio strategies?

Contact our office today ! [1]

Copyright © 2014 AdvisorNet Communications Inc. All rights reserved. This article is provided for informational purposes only and is not intended to provide specific financial advice. It is strongly recommended that the reader seek qualified professional advice before making any financial decisions based on anything discussed in this article. This article is not to be copied or republished in any format for any reason without the written permission of AdvisorNet Communications. The publisher does not guarantee the accuracy of the information and is not liable in any way for any error or omission.

Tags: investment planning [2]

Source URL:https://wealthwise.ca/e-newsletter/2014/2014-06/article-2.htm?qt-tabbed_block=0

Links
[1] https://wealthwise.ca/contact-us [2] https://wealthwise.ca/taxonomy/term/20