11 Investment Pitfalls to Avoid

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Few words better characterize today's financial markets than *uncertainty*. We believe investors need to adjust their expectations in order to adapt to the road ahead. It seems to be the nature of today's markets to subject investors to sharp price fluctuations and confusing global events that test emotional fortitude at every turn. Experience has taught us that successful investing requires discipline and the patient execution of a long-term strategy, most especially when it is emotionally difficult; in fact, that is usually the time when opportunities are greatest.

In order to help our clients chart a course in uncertain waters, we've compiled a list of mistakes investors should avoid:

Mistake #1: Failing to Follow an Investment Process

If you don't know where you're going, you may not like where you end up. A long-term investment strategy requires a personalized plan that takes into account your current and future needs, investment time horizon, appetite for risk, and appropriate allocation. This helps to ensure that no matter what the markets are doing in the short-term, you know that your investments are working towards your long-term goals. It is critical that you develop the discipline to stick with your plan. That discipline is most important when markets are pulling back and investors' fears can get the better of them.

Mistake #2: Underestimating the Benefit of Time

Each year's gains can generate their own gains the next year - a powerful wealth-building phenomenon known as compounding.

Here's an example of what a big difference starting young can make. Say you start at age 25, and put aside $3,000 a year in a tax-deferred retirement account for 10 years - and then you stop saving - completely. By the time you reach 65, your $30,000 investment will have grown to more than $472,000, (assuming an 8% annual return), even though you didn't contribute a dime beyond age 35.

Now let's say you put off saving until you turn 35, and then save $3,000 a year for 30 years. By the time you reach 65, you will have set aside $90,000 of your own money, but it will grow to only about $367,000, assuming the same 8% annual return. That's a huge difference.

Summary of Ending Account Balance at Age 65
Assumptions:
25 year-old with $40,000 salary, 40 year investment period, varying rates of return and savings

Average Annual Portfolio Return	Total Annual Savings Rate (% of Salary)				
	2%	4%	6%	8%	10%
6%	$123,810	$247,619	$371,428	$495,238	$619,048
8%	$207,245	$414,490	$621,736	$828,981	$1,036,226
10%	$354,074	$708,148	$1,062,222	$1,416,296	$1,770,370
12%	$613,673	$1,227,346	$1,841,019	$2,454,793	$3,068,366

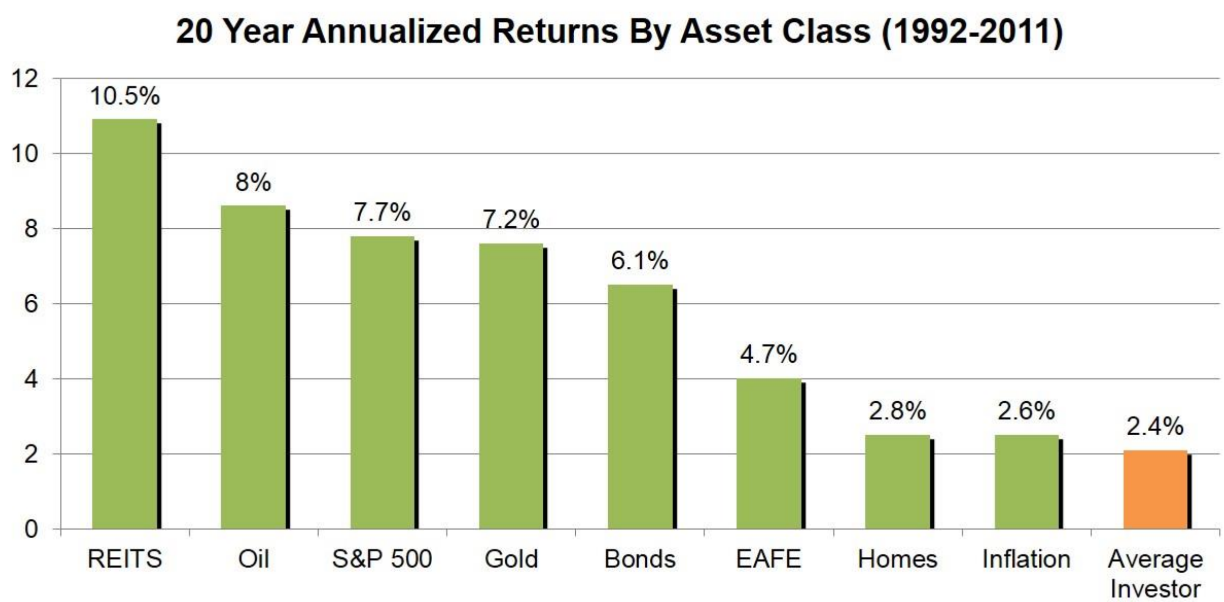
These examples are hypothetical and for illustrative purposes only. The rates of return do not represent any actual investment and cannot be guaranteed. Any investment involves potential loss of principle.

Mistake #3: Trying to Time the Market

When markets are rallying or pulling back, it's often very tempting to try and seek out the top to sell, or the bottom to buy. The problem is that investors usually guess wrong, missing out on the best market plays. Does the cost of trying to time the market make a big difference in your returns? You bet it can.

For example, between 1986 and 2005, the S&P 500* compounded at an annual rate of 11.9 percent –even while weathering Black Monday, the dotcom bust, 9/11, and various booms and busts. Over that period, $10,000 invested in 1986 would have grown to over $94,000.[1]

However, according to a recent Dalbar report, the average investor's return during that period was just 3.9 percent, meaning that same $10,000 grew to just over $21,000.[2] Why? Trying to time the market. The average investor misses out because their money tends to come in near the top and come out at the bottom. Investors are notoriously bad at picking the right time to enter or exit investments; by the time an opportunity is on their radar, the "smart money" is usually nearly ready to get out. The problem is that the majority of equity gains are made in a very short amount of time. If you're not in the stock when it moves, you may miss out on the whole play.



Source: BlackRock, Bloomberg, Informa Investment Solutions, Dalbar

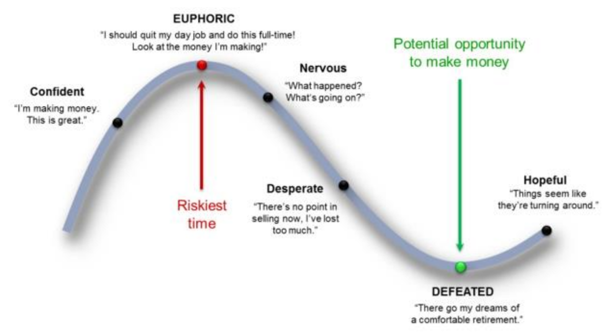
* The S&P 500 is an unmanaged index which cannot be invested into directly. Past performance is no guarantee of future results. These examples are hypothetical and for illustrative purposes only. The rates of return do not represent any actual investment and cannot be guaranteed. Any investment involves potential loss of principle.

Mistake #4: Making Emotional Investment Decisions

Emotional decision-making can wreak havoc on the most carefully designed investment plan when markets swing. A 2011 study by benefits company, Aon Hewitt, showed that boomers are especially at risk of making emotional investment decisions. Study results showed that those nearing retirement become very loss averse, and are prone to bailing on the market during declines. The problem is that these are the investors who may have the most to lose by making poor investment decisions.[3]

According to the study, the share of 55 to 60-year-old workers with less than 5 percent of their money in stocks rose from 9 percent at the end of 2007 to 14 percent at the end of 2008. Meanwhile, for those 60 plus, the percentage rose from 13 percent to 18 percent, and for the 50 to 55 age cohort, it climbed from 7 percent to 11 percent. Instead of seeing the big picture, taking advantage of the volatility, and rebalancing, many of these investors cashed out, locking in their losses; worse, most of them did not get back in for the 2009 rally.[4] While it can be difficult to rein in emotions when your life savings take a beating, running for the exits is sometimes the worst thing you can do.

There are two emotions that you need to confront whenever you make financial or investment decisions: fear and greed. Fear can cause us to abandon an investment strategy when the outcome is not what we want. Greed can cause us to chase investment fads and take on too much risk. It's impossible to avoid feeling these emotions when making important financial decisions; however, you can recognize them, and engage your rational mind to overcome them.



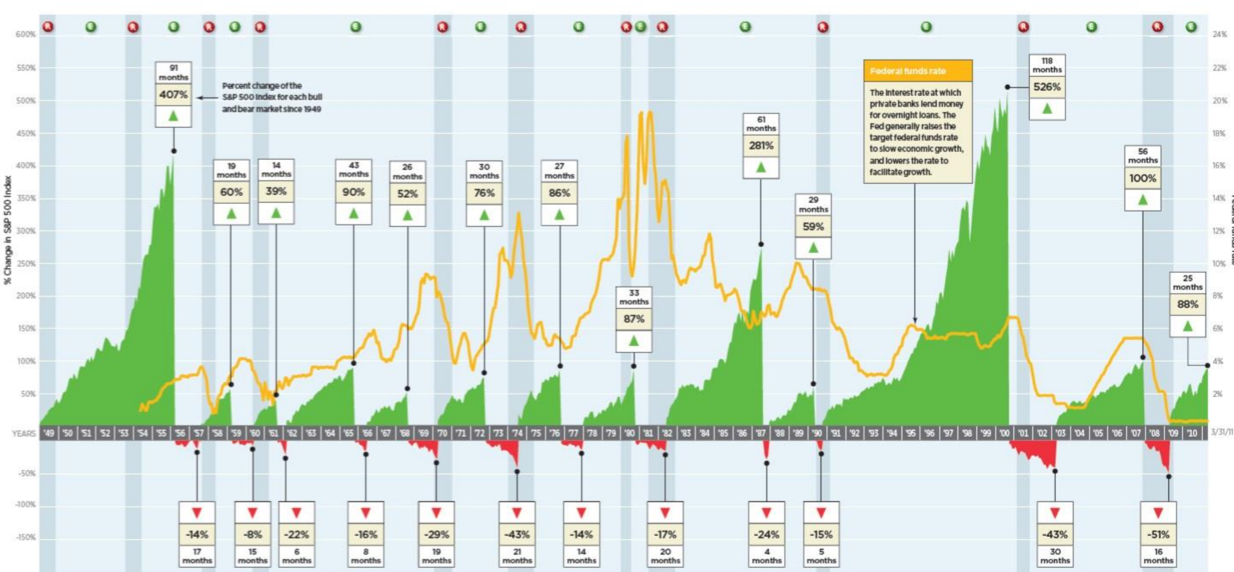
One of the major benefits of working with a financial professional is that it is our job to act as the voice of reason when emotions run high. When major investment decisions are only a click away, many investors give in to emotional decision-making and pay the price for their short-term thinking. When markets decline, remember that we are always available to answer questions, provide reassurance, and show you the opportunities that volatile markets provide.

Mistake #5: Expecting a Smooth Ride

You probably remember the heydays of the 90’s when many investors felt like they were on an elevator heading for the top floor. Today's markets are not like that, and it's a mistake to think that we will return to those conditions any time soon. In this “new normal” economy, big swings in the markets have many people scared stiff. However, even in a choppy market, with the appropriate mix of investments, there is money that could be made.

In order to help navigate the turbulent markets of today, it is critically important to structure your portfolio to seek to manage declines in down markets. This definitely does not mean to cash out when you lose confidence and re-invest when you begin to feel better about the markets (See Mistake #2 about the perils of trying to time the market). This means that during periods of market turbulence, you may need to adjust your mix of investments. It is also important to remain flexible in your investment selection, so as to take advantage of mispriced assets in a way that can both help to reduce risk and increase return potential.

However, both these techniques require active management. Regardless of your investor profile or long-term investment goals, making the most of today’s markets and holding onto your investment returns will require conviction in your investment strategy.



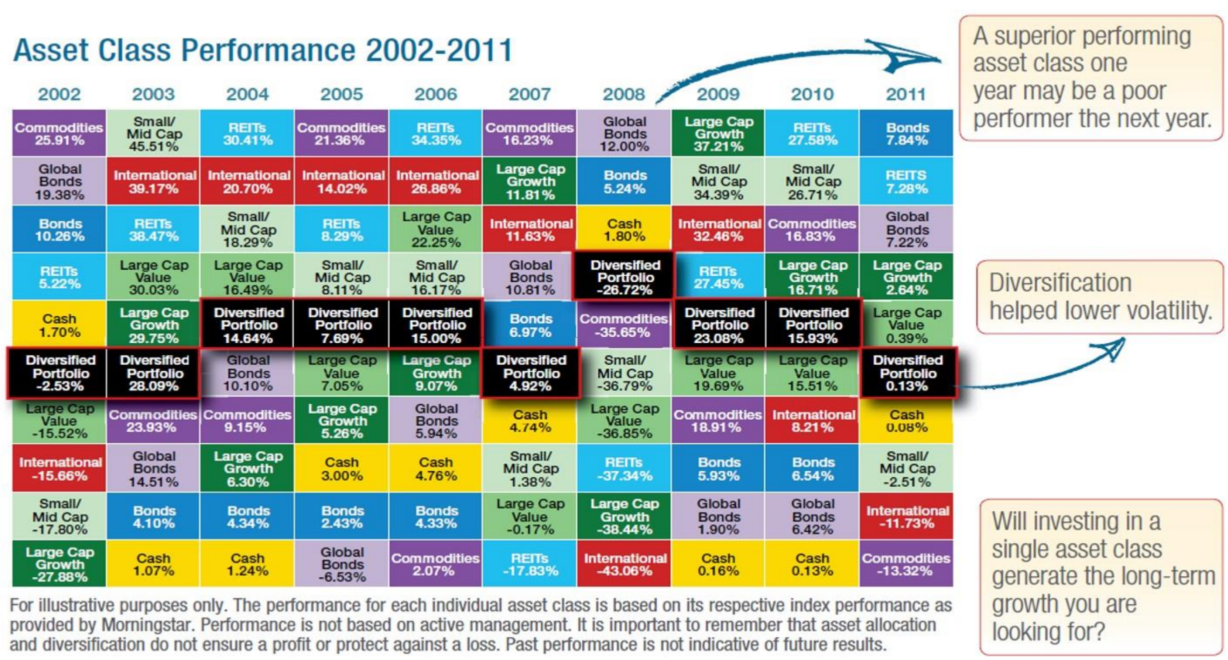
Sources: National Bureau of Economic Research, Ibbotson Associates, The Federal Reserve Bank of St. Louis, Putnam Investments, 2011. Data is as of 3/31/11, is historical, and reflects reinvested dividends. Past performance and market conditions do not guarantee future results and may not be duplicated. The S&P 500 Index is an unmanaged index of common stock performance. It is not possible to invest directly in an index. Federal funds rate data was not available before July 1954. A bull market is here defined as a period when the stock market rises for at least four straight months. A bear market is defined as a market decline of at least four months.

Not FDIC insured | May lose value | No bank guarantee

Mistake #6: Chasing Hot Performers

Chasing performance can be one of the biggest errors made by investors. That feeling of, "I don't want to miss out on this," has probably led to more investment mistakes than most care to admit. If you take the time to study past performance, you will discover that it is not a reliable way to predict future winners. The growth stocks that were popular in the 90s had been churning out double-digit returns for several years, when they suddenly went south, taking many investors' portfolios with them.

The lesson here is that if a particular asset class has outperformed for three or four years, you can know one thing with certainty: you should have invested three or four years ago. Often, by the time the average investor has decided to invest, the "smart money" has already gotten out while the not-so-savvy money continues to pour in. Don't make this mistake. Stick to your strategy, rebalance, and focus on getting into investments with great fundamentals.



Asset Class Performance 2002-2011

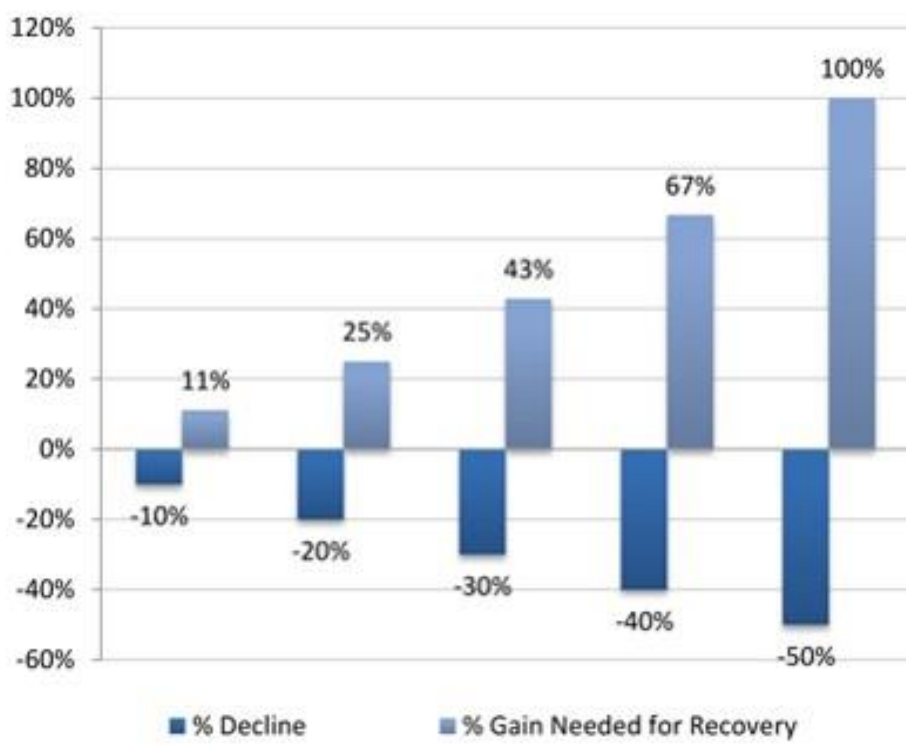
2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Commodities 25.91%	Small/ Mid Cap 45.51%	REITs 30.41%	Commodities 21.36%	REITs 34.35%	Commodities 16.23%	Global Bonds 12.00%	Large Cap Growth 37.21%	REITs 27.58%	Bonds 7.84%
Global Bonds 19.38%	International 39.17%	International 20.70%	International 14.02%	International 26.86%	Large Cap Growth 11.81%	Bonds 5.24%	Small/ Mid Cap 34.39%	Small/ Mid Cap 26.71%	REITs 7.28%
Bonds 10.26%	REITs 38.47%	Small/ Mid Cap 18.29%	REITs 8.29%	Large Cap Value 22.25%	International 11.63%	Cash 1.80%	International 32.46%	Commodities 16.83%	Global Bonds 7.22%
REITs 5.22%	Large Cap Value 30.03%	Large Cap Value 16.49%	Small/ Mid Cap 8.11%	Small/ Mid Cap 16.17%	Global Bonds 10.81%	Diversified Portfolio -26.72%	REITs 27.45%	Large Cap Growth 16.71%	Large Cap Growth 2.64%
Cash 1.70%	Large Cap Growth 29.75%	Diversified Portfolio 14.64%	Diversified Portfolio 7.69%	Diversified Portfolio 15.00%	Bonds 6.97%	Commodities -35.65%	Diversified Portfolio 23.08%	Diversified Portfolio 15.93%	Large Cap Value 0.39%
Diversified Portfolio -2.53%	Diversified Portfolio 28.09%	Global Bonds 10.10%	Large Cap Value 7.05%	Large Cap Growth 9.07%	Diversified Portfolio 4.92%	Small/ Mid Cap -36.79%	Large Cap Value 19.69%	Large Cap Value 15.51%	Diversified Portfolio 0.13%
Large Cap Value -15.52%	Commodities 23.93%	Commodities 9.15%	Large Cap Growth 5.26%	Global Bonds 5.94%	Cash 4.74%	Large Cap Value -36.85%	Commodities 18.91%	International 8.21%	Cash 0.08%
International -15.66%	Global Bonds 14.51%	Large Cap Growth 6.30%	Cash 3.00%	Cash 4.76%	Small/ Mid Cap 1.38%	REITs -37.34%	Bonds 5.93%	Bonds 6.54%	Small/ Mid Cap -2.51%
Small/ Mid Cap -17.80%	Bonds 4.10%	Bonds 4.34%	Bonds 2.43%	Bonds 4.33%	Large Cap Value -0.17%	Large Cap Growth -38.44%	Global Bonds 1.90%	Global Bonds 6.42%	International -11.73%
Large Cap Growth -27.88%	Cash 1.07%	Cash 1.24%	Global Bonds -6.53%	Commodities 2.07%	REITs -17.83%	International -43.06%	Cash 0.16%	Cash 0.13%	Commodities -13.32%

For illustrative purposes only. The performance for each individual asset class is based on its respective index performance as provided by Morningstar. Performance is not based on active management. It is important to remember that asset allocation and diversification do not ensure a profit or protect against a loss. Past performance is not indicative of future results.

Mistake #7: Overlooking Downside Risk

Many investors focus primarily on the upside potential of an investment. While the upside is important, paying close attention to the downside potential is equally, if not more, important.

Simple math demonstrates the paramount importance of effective risk management in investment portfolios. A loss of 20% requires a gain of 25% just to break even. In order to recover from a 50% decline, a portfolio must increase by 100%, or double its value.



Mistake #8: Improperly Addressing Investment Risk

Experience has taught us that there are four basic ways to address risk: ignoring it, avoiding it, managing it or transferring it.

Here's an example we can all relate to. If you choose to drive a car, you have four choices related to managing the risk associated with that activity:

- Ignore: e.g. "If I crash, I'll just buy a new car."
- Avoid: "I won't drive at all."
- Manage: "I'll drive defensively with my hands at 10 and 2." (Despite your best efforts to do this, it still doesn't mean you might not get t-boned.)
- Transfer: "I'll buy car insurance." We commonly recommend using a variety of insurance instruments to help our clients transfer their risk. This may include insured investments, life insurance, insurance to cover future medical expenses, and so on. (Note: Most investments are not FDIC insured or guaranteed by any government agency. Any guarantees are based on the claims paying ability of the underlying insurance company.)

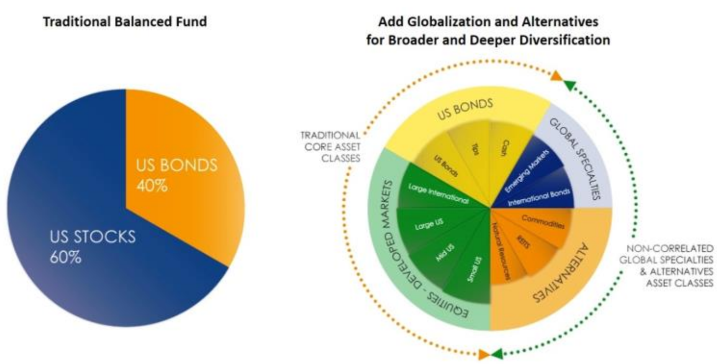
When it comes to investing, deciding whether to ignore, avoid, manage or transfer risk will vary from person to person. Our job is to educate you about your options and help you make an informed decision.

Mistake #9: Failing to Achieve True Diversification

Warren Buffett once said that diversification* is a “protection against ignorance,” meaning that when it comes to investing, there’s no way to know everything about an investment and no way to predict the future. Even the Sage of Omaha makes poor investment decisions, and diversification prevents one error or bad investment from taking down his whole portfolio.

The first step of a diversification plan consists of diversifying between asset classes. This means maintaining a good mix of stocks, bonds, cash, and perhaps some other types of alternative investments like real estate, or other investments that are a good fit for your goals and investor profile. The problem is that many investors have a tendency to chase performance by aggressively investing in a single class of investment: stocks when the equity markets are rallying, and bonds or cash during a market decline. This lack of diversification can play havoc with a portfolio during times of market turbulence.[5]

The second part of a properly diversified portfolio is diversifying within an asset class. One of the most critical mistakes many working investors make is to have too much (more than 10-15 percent of their portfolio) in their company’s stock, which can spell disaster if it takes a turn for the worst – imagine, losing your job and your retirement savings in one fell swoop. For example, it’s important to have a good mix of small-cap, large-cap, international, and sector-diverse equities in a portfolio*. While a certain stock or sector might be affected by a market decline, a gain in another might offset it.



Diversification does not ensure a profit or guarantee against loss; it is a method used to help manage investment long term risk.

*Alternative investments may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses. Investing in small-cap companies may involve greater risk in price volatility and potential reward than investing in larger, more established companies. International investing presents certain risks not associated with investing solely in the United States. These include currency fluctuations, political risks, accounting procedure differences and the lesser degree of public Information required to be provide by non-U.S. companies.

Mistake #10: High Withdrawal Rates in Retirement

When it comes to determining whether or not we are financially prepared to retire, the typical question is, *"Do I have enough money?"*

However, the real question is not how much money we have, but rather, *"What percentage of savings can I withdraw annually to satisfy my income needs throughout retirement?"* A high withdrawal rate can diminish your portfolio if you happen to face a prolonged bear market early in retirement. After a few years of "selling low," you're left with too small a portfolio to benefit fully when the market *does* come back.

This poorly-timed-bear-market concept is known in finance as "sequence of returns risk." Ignoring it completely will cause you to underestimate the amount of savings you'll need in order to retire.

WHAT ARE THE CHANCES MY MONEY WILL LAST THROUGHOUT RETIREMENT?

	ASSET ALLOCATION				
ANNUAL WITHDRAWAL RATE	100/0	80/20	60/40	40/60	20/80
3%	94%	97%	98%	99%	99%
4%	83%	86%	89%	91%	92%
5%	67%	69%	68%	63%	49%
6%	50%	49%	42%	29%	10%
7%	35%	31%	22%	9%	1%
8%	24%	18%	10%	2%	0%

Figure 1 summaries a study performed by T. Rowe Price Associates, Inc. It shows the probability of successfully sustaining a given withdrawal rate over an assumed 30 year retirement. Success is defined by having one dollar left in the account at the end of the retirement period. The results are hypothetical in nature and are based upon Monte Carlo analysis of 5 model investment portfolios made up of different allocations to stocks, bonds and short term bonds. The given withdrawal rate are assumed to be taken out in their entirety on the first day of year one, and then adjusted upwards by 3% for Inflation.

Mistake #11: Ignoring the Impact of Taxes

When looking at investments, one of the key rules to keep in mind is that you should always be looking at the after-tax return of an investment. At first glance, a 5 percent return beats a 3 percent return any day of the week. However, if the 5 percent return were from taxable stock dividends and the 3 percent came from tax-free municipal bonds, then the situation changes. For example, a hypothetical $10,000 investment might be worth $17,908 after 10 years at a 6 percent annual return. However, after accounting for hypothetical state and federal taxes (5 percent and 25 percent, respectively), you would only take home $11,228, pushing your annual return down to just 1.2 percent.[6] It never pays to ignore taxes.

You should consider the impact of taxes whenever you buy or sell investments, develop a financial plan, discuss your estate or philanthropic plans, or give gifts. Remember that the federal government taxes investment income, like dividends, interest, and rent on real estate, as well as capital gains. This is why it's critical to structure your investments in a tax-efficient manner to avoid having the taxman take a big bite out of your gains.

The tax situation for many Americans changed under the American Taxpayer Relief Act of 2012. The Act was designed to resolve the so-called fiscal cliff by addressing the expiration of many temporary tax cuts. While the Act retained the tax breaks of the Bush Tax Cuts for most Americans, it instituted higher tax rates at upper income levels.

Though this strategy is not right for everyone, for some of our clients, we are shifting a portion of their investments to assets that generate federally tax-exempt income, such as municipal bonds. We are also discussing other strategies for reducing the impact of taxes on their income and investments. If you are concerned about the impact of taxes on your future, we strongly encourage you to speak with us and your tax professional to determine what options may be available to you.

Note: While taxes are not something you should ignore, your investment strategy should be based on your investment goals, appetite for risk, and time horizon.

*Municipal bonds are subject to availability and change in price. They are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise. Interest income may be subject to the alternative minimum tax. Municipal bonds are federally tax-free but other state and local taxes may apply.

The Bottom Line

We educate our clients on the opportunities that market turbulence sends our way and keep them focused on their long-term goals, not on short-term gyrations. As financial advisors, we spend our careers charting courses through turbulent markets and attempt to help achieve results for our clients. As professionals, it's our job to stay on top of ever-shifting economic, financial, and legal issues so that our clients don't have to.

Quite simply, the old days of achieving steady returns through cookie-cutter approaches appear to be over. We believe that successfully navigating the turbulent investing world of today requires training, prudent management, and commitment to a long-term, active investing strategy.

Investors who recognize and avoid these eleven common pitfalls may give themselves an advantage in pursuing their investment goals, particularly in times of economic uncertainty and market turbulence.

While it is impossible to predict which direction markets will go, generally, each downside contains an upside potential somewhere else. We focus on seeking out this upside potential and diversifying* our clients' investments into different asset classes. Our goal in doing this is to seek to help them smooth out the highs and lows, avoid the worst-case scenarios, and take advantage of the many opportunities that exist.

Above all, we want to help our clients relax and enjoy the lifestyle that they have worked to build, knowing there is an experienced, vigilant hand at the tiller. If you ever have questions or concerns about your portfolio, we are at your service.

Warm Regards,

Call today for a free consultation (866) 623-3900, or visit www.beaconwealthwv.com.

Footnotes, disclosures, and sources:

Securities offered through Sammons Securities Company, LLC, Member FINRA/SIPC. Fee-based investment advisory services offered through Sigma Planning Corporation, a registered investment advisor. Beacon Wealth Management operates independently of Sammons Securities Company, LLC

*Neither diversification nor asset reallocation can ensure a profit or protect against a loss.
Investing involves risk including the potential loss of principal. No investment strategy can guarantee a profit or protect against loss in periods of declining values.

Past performance does not guarantee future results.

You cannot invest directly in an index.

Consult your financial professional before making any investment decision.

Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

All information is believed to be from reliable sources; however, we make no representation as to its completeness or accuracy. Please consult your financial advisor for further information.

Investing in small- and mid-size companies may involve greater risk in price volatility and potential reward than investing in larger, more established companies.

International investing presents certain risks not associated with investing solely in the United States. These include currency fluctuations, political risks, accounting procedure differences and the lesser degree of public information required to be provide by non-U.S. companies.

The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

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We have not independently verified the information available through the following links. The links are provided to you as a matter of interest. We make no claim as to their accuracy or reliability.

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[1] Source: Yahoo Finance

[2] http://www.qaib.com/public/default.aspx

[3] http://www.forbes.com/sites/janetnovack/2011/09/26/study-boomers-making-more-401k-investing-mistakes-than-younger-folks/

[4] http://www.forbes.com/sites/janetnovack/2011/09/26/study-boomers-making-more-401k-investing-mistakes-than-younger-folks/

[5] http://news.morningstar.com/articlenet/article.aspx?id=310230

[6] AARP Investment Return Calculator