Too much of a good thing

Investment Strategy Team

As an investor, you no doubt want to build your portfolio with quality investments. From time to time, you may be tempted to load up on a particular investment. But remember that too much of a good thing can actually be bad.

Diversification is important

If you put too much of your money into one particular investment or type, you may be exposing your portfolio to unnecessary risks. All investments carry some type of risk. The key is deciding which risks are worth taking. What's considered the best investment today may not be so tomorrow. Therefore, we suggest a more balanced approach.

What are your financial goals? Are you comfortable with risk and have a long time horizon for investing? Or is your focus on achieving near-term goals and therefore you prefer lower-risk investments? Your risk tolerance will help shape your investment decisions, but regardless of your risk tolerance, we believe certain risks aren't worth taking.

Owning a portfolio made up of just a few securities can pose serious risks to achieving your financial goals. You can't afford to risk your important goals — such as a comfortable retirement or your child's college education — by putting all your money into just one or two stocks or bonds. Simply put, you need to diversify.

The risk and reward trade-off

Stock prices go up and down — by the year, by the day and by the hour. They always have and always will. While stocks tend to fluctuate more than bonds, they also tend to provide greater return potential over the long run.

How can you take advantage of the potential for reward while aligning your portfolio's risk with your financial goals? By building a diversified portfolio of quality investments and focusing on the long term.

If you always knew what the next hot stock would be, you would most likely enjoy tremendous success as an investor. But no one can really predict such things. In fact, a stock's return can vary tremendously over a short period.

If you owned only a few stocks, you'd likely see a wide array of returns relative to the entire universe of stocks. However, diversifying your portfolio across a variety of stocks can help narrow the range of potential returns. In addition to diversifying across equities, investing in other asset classes, such as bonds, can further enhance portfolio diversification.

The optimal mix of equity and fixed income should be based on your unique situation and financial goals. We believe that, over the long term, investing across multiple asset classes can help reduce dramatic swings in your portfolio value and put you in a better position to achieve your long-term goals.

Why not diversify?

Statistics show that diversification can help reduce investment risk. But many people still choose to put many of their financial resources into just one stock, or at most a few stocks. Do any of the following sound familiar?

- **You're emotionally tied to a company.** There's nothing wrong with showing loyalty to a company to which you have some ties or a business at which you may have worked. But as an investor, you need to use your head, not your heart. Also, just because a company is strong today doesn't mean it will always be a good investment.
- **You've inherited stock from a family member.** Your relative would want you to make decisions that are in your best financial interest — which could include selling some of the stock to help diversify your portfolio.
- **You're happy with a stock's performance, and you believe it has great upside potential.** It's a good feeling when a stock has been a strong performer, but that doesn't guarantee future performance. Even when the outlook for a company or an industry is favorable, it's almost impossible to say which stock has the most upside.
- **You don't want to pay capital gains tax.** Taxes are a factor in many investment decisions — but they usually shouldn't be the driving factor. You may be better off selling a stock and using the proceeds to buy other investments than you would keeping the stock just to avoid paying capital gains taxes. If you're concerned about taxes, you could spread out your tax liability by selling a portion of the stock each month. Be sure to consult with your tax advisor about your situation.

Ask yourself these questions

We believe putting most of your financial resources into just one investment is risky business — and one of the biggest mistakes you could make. If you're in this position, ask yourself:

- What advice would I give a friend or family member who had too many eggs in one basket?
- Am I holding on to this investment for emotional reasons or to avoid paying taxes?
- Are there other investments that might offer similar upside potential, yet help me diversify my portfolio and reduce risk?

After thinking about these questions, talk with your financial advisor. They can help you rebalance and diversify your portfolio as necessary to help you reach your long-term goals.

Ultimately, diversification doesn't guarantee a profit or protect against loss in a declining market, but we believe it can help you weather the market's ups and downs — and that's a big advantage for any investor.

Hot stocks gone cold

It's bad enough to get burned by a stock. It's even worse when much of your portfolio is tied up in that single stock. Although the outlook for any company may seem bright at any time, it's impossible to predict performance or anticipate changes in the economy. This table shows some examples of companies that were once considered great but quickly became bad investments.

	1990s		2000s		
	Boston Chicken	**Conseco Inc.**	**Enron**	**PG&E**	**SVB Financial Group**
Stock price at its high	$41	$57.75	$90	$71.56	$755.03
Date of peak	12/3/1996	4/6/1998	8/23/2000	9/11/2017	11/3/2021
Time from high to 95% decline	18 months	43 months	15 months	26 months	17 months
Status today	Bankrupt	Exited Chapter 11 bankruptcy	Bankrupt	Exited Chapter 11 bankruptcy	Chapter 11 bankruptcy

Source: FactSet and Edward Jones.

These stocks are extreme examples of "riches to rags" investments. Yet they clearly illustrate the danger of putting too much money into any one investment.

Diversifying a stock portfolio

To help balance a portfolio of individual stocks, we believe you should own at least 25 to 30 stocks in different industries, or 15 stocks in different industries if you also own equity mutual funds or exchange-traded funds (ETFs). If it's not practical for you to own this many stocks, owning well-balanced mutual funds or ETFs can help you achieve broad equity diversification. In addition, we believe including equities from a variety of regions, such as domestic and international markets, along with a variety of company sizes, such as small-, mid- and large-cap, can further enhance diversification.

Diversify systematically

If you'd like to diversify your portfolio but don't want to sell stocks all at one time, Edward Jones can help. Your financial advisor can help develop a plan to sell a portion of stock at specific intervals based on your unique financial and tax situation. This can help reduce your concentration risk over time while keeping your long-term goals in focus.*

This program may be appropriate if you need to:

- Reduce the amount you own in a single stock — You can use the proceeds to invest in different securities automatically, boosting your diversification.
- Receive a steady income stream — If you choose not to reinvest the proceeds of your stock sales, you can use the money to supplement your cash flow.

When you're tempted to overload on a good investment, remember the importance of keeping a balanced perspective. Your financial advisor can help you set up a portfolio that works with your situation, your goals for the future and your comfort level with risk.

*The monthly automatic sale of your securities may produce a taxable event. Please consult your tax advisor regarding the effect this program may have on your taxes. Systematically selling investments should be reviewed regularly with your financial advisor. In extended periods of declining stock prices, it is possible to deplete your stock position. Not available for all stocks. Edward Jones, its employees and financial advisors do not offer tax or legal advice. Please consult with a qualified tax or legal advisor about your situation.

