Investor Know Thy Self

BY KELLEY KEEHN

It's been a wild ride in the markets this year! And, if you went into the pandemic not fully understanding the impact of volatility, you likely have a good sense of it as we near the close out the year.

It's often said that we're much less risk adverse when investing in a bull market (stocks heading up in value) but as soon as it turns bear (stocks heading down in value), our true tolerance is revealed. That can be incredibly devasting to your portfolio if you become panicked during a market crash and sell.

According to the 2020 CSA Investor Index, despite the economic environment in 2020, only 48% of respondents reviewed their risk tolerance within the last year, down from a high of 62% in 2006.

Risk tolerance missteps

According to Louis Morisset, Chair of the Canadian Securities Administrators (CSA), "a common error people make is not aligning their risk tolerance with their financial situation or current needs. That can lead to problems, especially during difficult or turbulent economic times. Investors are encouraged to develop a financial plan and to consistently assess their needs and risk tolerance."

Lucy Becker, Vice President, Public Affairs and Member Education Services with the Investment Industry Regulatory Organization of Canada (IIROC), cautions that investors should consider their emotional willingness to accept risk and their financial ability to absorb loss. "Generally, people like to look on the bright side and think about what they stand to make rather than what they stand to lose. All investments carry some degree of risk and – be they stocks, bonds, mutual funds, and exchange-traded funds – they could potentially lose some or even all their value if market conditions change. As such, it is important to understand the types of risk that may impact your investment returns before determining and implementing your investment strategy and your risk tolerance."

Advice or DIY?

Morisset notes that, "a registered investment adviser can help investors set goals and develop a long-term investment plan, and a crucial part of this process should include assessing risk on a regular basis. If an investor's risk profile changes, an adviser is there to help adjust the plan accordingly."

Becker encourages DIY (do-it-yourself) investors to ask themselves some key questions. "First and foremost: Are you comfortable with not receiving advice about your investments? DIY investors have to determine if the choices they are making are suitable for them." Becker also points out that since the start of the pandemic, "IIROC's Complaints & Inquiries team has seen a dramatic surge in contacts from DIY investors who are using Order-Execution Only (often called discount or online brokers) to invest. More than half (57%) of those who have contacted IIROC for information and/or help over the past three years are over the age of 55, even though we often think younger Canadians are more interested in online investing. "

Some common mistakes IIROC has seen some investors making include situations where they:

- over-extend themselves financially with borrowing (margin/lines of credit/credit card funds)
- invest in complex products or engage in complex trading strategies without adequately understanding the features, benefits, and risks of such products/strategies
- misinterpret investment research and subsequently "bet the farm" and lose
- use online discount brokers to pay lower fees without considering whether this strategy is right for them

Investment fraud & ill fitted advice

The greatest risk to your wealth creation and preservation - other than not understanding and adhering to your risk tolerance - is the danger of fraud. Investors need to understand what a realistic rate of return is currently. There's no guaranteed investment paying more than a couple of percentage points at the moment.

The CSA Investor Index revealed that 64% of survey respondents reported never conducting a background check on their financial adviser. "Protecting yourself starts with checking registration", cautions Morisset. "The individual and firm's registration category tells you what products and services they can offer, if there are any restrictions (or terms and conditions) imposed on them by the regulator, and if there is any disciplinary history you may want to be aware of. You can visit www.aretheyregistered.ca to conduct a free search."

Becker wants you to be aware that choosing an investment advisor is a big decision. "It is wise to ask your advisor some basic questions to understand what products and services the advisor is licensed to offer, the requirements they must meet to be licensed and who regulates them – especially if something goes wrong."

When people shop for a vehicle, a home or even a vacation, they do some due diligence to protect themselves and their money – so it also makes good common sense to do the same when choosing or changing advisors.

IIROC provides an online searchable database that lets investors to learn about IIROC-registered advisors and if they have been subject to disciplinary actions or are working under any disciplinary restrictions. If your advisor does not appear on IIROC's AdvisorReport, the individual or firm you are researching may be regulated by another regulatory authority in Canada. You can find helpful links on IIROC's website to other regulators.

Kelley Keehn is a Personal Finance Educator, best-selling author, keynote speaker and media personality with over 20 years in the Canadian finance industry. Her tenth book, Talk Money to Me, published by Simon and Schuster, is available in bookstores across Canada now and the COVID edition will be out in March 2021. She was the Consumer Advocate for FP Canada and serves on many other prominent financial committees and boards. Over the last four years alone, she has conducted over 1,000 television, radio and print interviews on a multitude of financial literacy topics. Her mission is to help Canadians feel good about their money.

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