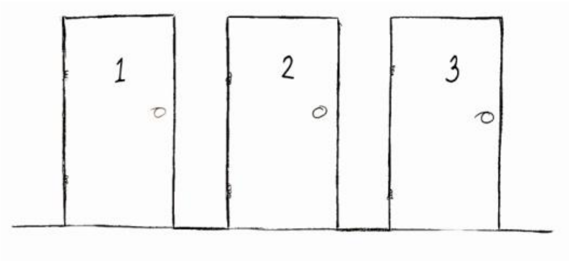
How not to pick a mutual fund

Time and again, do-it-yourself investors pile into the wrong stuff. They want to build their wealth yet end up in investments that separate them from their hard-earned savings. Following are some classic bad moves in choosing mutual funds that are virtually guaranteed to make you poorer.



C'mon, folks – you can do better than this!

1. **Chase performance**
   Buying a fund solely on how it has performed is a fool's game. The past is exactly that: a done deal, a sailed ship, a bird flown from the coop. You'll glean pretty much zero insight from a fund's performance history. It's especially critical to ignore strong short-term results that could very well be 100% the result of dumb luck.

   We get it. Fund companies love to tempt you to invest by advertising their numbers (only when they're favourable, of course). Just fugget about it! Focus instead on what you can control, like how a fund has been designed to behave from the point you invest rather than what it did in some bygone time.

2. **Dismiss the details**
   Too often investors buy a fund without looking under the hood. Investing 101 includes knowing who runs the fund, the approach they take and the amount of money they manage. Your decision should also be informed by the fund's age, the cost to own it and whether any changes have been made to the way it operates. All of these factors will influence your investment experience and there's always lots to consider before jumping in.

   It's either eyes wide open or your wallet wide open. Your call.

3. **Get starry-eyed**
   Investors will rely on research firm Morningstar Inc.'s one-to-five star fund rating system as a substitute for their own due diligence. Back to the #1 no no for picking a fund, star ratings are based exclusively on past performance. As dazzling as it may seem, no single data point will tell you enough about a fund to make an educated decision about whether to invest.

   Same applies to those lists of "top funds" regularly churned out by the media. They may help you to narrow the field but any practical guidance they offer ends there. You want more than a superficial analysis for something as important as your future financial security.

4. **Misunderstand diversification**
   Owning multiple funds from different companies is ideal, right? Or so investors are led to believe. They've been sold on the idea of diversification as an ultimate form of risk management. And it is, if done properly. However, it's easy to oversimplify the don't-put-all-your-eggs-in-one-basket rule. "More" doesn't automatically equal "safer."

There's such a thing as *diworsification*. In other words, investing overkill, where you hold a plethora of funds that are too closely correlated. This undermines your portfolio's balance of risk and reward. Understand that it's entirely possible to own only one fund and be sufficiently well-diversified. (This isn't a shameless plug to buy EdgePoint. We believe any fund properly diversified by business idea, even one offered by competitor, can be all that you need).

5. **Chase headlines**
   We refer to the diseased state of mind stemming from being barraged by negative headlines as "macromatosis." Macromatosis hits investors where it hurts them most, in their hearts and by extension their bank accounts. The bad news overwhelms them and drives their decisions. Acting on emotion causes investors to buy and sell funds at precisely the wrong times.

   The universal remedy to macromatosis is sticking to your investment plan, the one you created when things were calm and you were thinking rationally. Put your faith in that over your ability to time the market, which almost no one – professional investors included – gets right.

6. **Believe the hype**
   Sales- and marketing-led fund firms put their business needs first. Whatever the flavour of the day, they'll launch an investment product that attempts to capitalize on it. They then inundate you with related mass marketing. Because they know the latest hot trend is where the money will flock to. To line their pockets, these companies feed on investors' fear and greed at the expense of sound investing principles. Don't believe their hype.

   Indeed, some of the best fund managers often behave as if they don't want your money. You won't constantly see them on television or running ads boasting their returns.

If you're the type who spends more time planning your vacation than your investment portfolio, you could find yourself disappointed at best. It unfortunately goes downhill from there to the point that you could be in deep financial trouble. Before you give your money to someone to manage, invest adequate time researching what lies behind their claims and be your own best friend, not your own worst enemy.

Better still, hire a skilled and principled financial advisor. They're experts at helping you keep your emotions in check and can offer effective advice in helping you reach your financial goals, including navigating the often complex and tricky business of selecting the right fund(s) tailored to your individual situation.