How to Review Your Portfolio in a Falling Market: Part 1

Description

In the past week, the **S&P 500** has fallen 5.7%, the **Dow Jones Industrial Average** has fallen 5.2%, and the **S&P/TSX Composite Index** has fallen 5.2%. In particular, on Friday, in a single day, the first fell 3.2%, the second fell 3.1%, and the last fell 2%.

It surely looks like the sky is falling and more pain is coming. Investors should do at least this one thing as the market falls: review your portfolio.

Review your portfolio

Are you seeing stocks that you'd rather not have in your portfolio? Ones that are more volatile than others and have low-quality ratings? Do you like the allocation of each sector or company?

Divide your portfolio by quality

Ideally, I want to hold the companies I'm most comfortable with. You guessed it; stocks like **Royal Bank of Canada** (TSX:RY)(NYSE:RY) and **Canadian Utilities Limited** (TSX:CU). But at other times, I buy certain companies for trade, such as **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK). In a down market, Teck Resources can do considerably much worse than the former two.

So, it's very important to divide your portfolio between high-quality, long-term holdings, and low-quality or trading holdings. The division helps you prepare mentally for managing your portfolio.

If you're a long-term investor, you probably want most of your portfolio to be high-quality companies bought at proper prices.

Divide your portfolio by sector and by company

Another way to view your portfolio is to divide it into these sectors: basic materials, communication services, consumer discretionary, consumer staples, energy, financial services, healthcare, industrial, real estate, technology, and utilities.

Keep track of how much money you have allocated each sector. Since companies in the sectors of basic materials and energy generate more unpredictable earnings because their earnings depend on commodity prices, it may be wise to keep a lower portion of your portfolio in those sectors.

It can be alarming if one sector has over 25% allocation. That means 25% of your portfolio is in a single sector. If something bad happened to that sector, a quarter of your portfolio would be at risk. Likewise, you might consider allocating only up to 10% to any single company.

However, how much to allocate to each sector or company is up to each individual's comfort level and risk tolerance. Some investors concentrate their portfolios and only hold 10 to 15 stocks at a time. Others hold hundreds of stocks.

A sample portfolio

Here's an example of what a portfolio may look like.

- Consumer discretionary: **Starbucks Corporation** (NASDAQ:SBUX), **Amazon.com, Inc.** (NASDAQ:AMZN), and **TJX Companies Inc.** (NYSE:TJX)
- Consumer staples: **Alimentation Couche-Tard Inc.** (TSX:ATD.B) and **PepsiCo, Inc.** (NYSE:PEP)
- Healthcare: **Johnson & Johnson** (NYSE:JNJ)
- Industrial: **Emerson Electric Co.** (NYSE:EMR)
- Real estate: **Canadian REIT** (TSX:REF.UN), **Boardwalk REIT** (TSX:BEI.UN), and **Ventas, Inc.** (NYSE:VTR)
- Technology: **Apple Inc.** (NASDAQ:AAPL), and **Microsoft Corporation** (NASDAQ:MSFT)
- Utilities: **Fortis Inc.** (TSX:FTS) and Canadian Utilities Limited

To start, Starbucks, Amazon, and TJX might make up 15% of the portfolio, 5% each. Alimentation Couche-Tard, Pepsi, and Johnson & Johnson make up 8% each. Emerson makes up 3%. Canadian REIT, Boardwalk REIT, and Ventas make up 8%. Apple and Microsoft make up 7%. Finally, Fortis and Canadian Utilities make up 10%.

If I don't like the current allocations, I would add to the company or sector that I want more of when I have new money to add to the portfolio. If I think one company has overrun itself, I can sell some of its shares to reallocate to other companies.

Ideally though, I want to buy and hold quality stocks forever, and receive a growing income from them…as long as the companies retain their quality.

In conclusion

Actually, even before a market falls, Foolish investors should review their portfolios periodically, at least every three months. However, falling markets are a reminder that investing is not a set-and-forget thing. The market and the factors that affect it change all the time. They're dynamic. As a result, we need to be dynamic, too.

There's more to do in a falling market. Find out what they are in part two of this series.

CATEGORY

1. Dividend Stocks
2. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. NASDAQ:AMZN (Amazon.com Inc.)
2. NASDAQ:SBUX (Starbucks Corporation)
3. NYSE:RY (Royal Bank of Canada)
4. NYSE:TECK (Teck Resources Limited)
5. NYSE:TJX (The TJX Companies, Inc.)
6. TSX:CU (Canadian Utilities Limited)
7. TSX:RY (Royal Bank of Canada)
8. TSX:TECK.B (Teck Resources Limited)

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