Why Picking Stocks May Be More Important Now Than Ever

Description

To actively manage or not actively manage? That is the $1 million question.

It is true that in today's complex and confusing world filled with overvalued stocks and sectors that are seemingly ready to pop, investing one's money in an exchange-traded fund (ETF) that tracks any of the major indices may be a very dangerous exercise.

Cautious long-term investors looking for control over convenience have often gone the stock-picking route; however, I'm going to discuss why even passive investors should consider some level of active investing, even if the actively managed portion of a passive portfolio is small.

Stock markets around the world, fueled by cheap money and bullish investor sentiment following the global recession of 2007/2008, have climbed to record highs (in most cases).

In Canada, the **S&P/TSX Composite Index** (TSX:^OSTPX) has risen to levels that now exceed its 10-year average by 12%, with an average dividend yield 20 basis points (bps) below its 10-year average. In other words, investors focused on either growth or income will be provided with significantly fewer value opportunities than any other time in the past five years.

While many analysts still believe that a number of catalysts could take global stock markets to even higher highs, cautious investors will note that the once-reliable rising tide, which has lifted global stocks higher over the past 10 years, may be waning, and picking stocks remains one way defensive investors can hedge out some of the cyclical market risk by weighting a portfolio heavier towards defensive names.

Those who prefer offence as the best form of defence will also benefit from stock picking in that such an investor will be able to choose above-average growth companies that can withstand a potential periodic decline — something ETFs do not do.

Bottom line

In today's uncertain economic environment, I prefer to look at companies that have stable dividends and have track records of increasing said dividends over long periods of time.

Companies such as **Fortis Inc.** (TSX:FTS)(NYSE:FTS) which have increased their dividend each year for decades (in the case of Fortis, 43 years in a row) are best suited to manage a stock market downturn or recession moving forward, given the stability of the company's cash flows and dividend yield, as well as Fortis's counter-cyclical nature, which significantly outperforms in times of economic weakness (check out Fortis's stock chart around the time of the Great Recession).

Stay Foolish, my friends.

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