



Avoid the Biggest Mistake Many TFSA Investors Make

Description

The TFSA is the best thing to happen to Canadians since sliced bread. Most folks know that it's in their best interest to max out their TFSAs every single year and use the proceeds to invest in a diversified mix of assets like equities, fixed-income securities, REITs, and other alternative assets (definitely not cryptocurrencies!).

Despite being a disciplined TFSA investor who's following all the good practices recommended by financial professionals, most investors may not realize that they're sub-optimally setting themselves up to deal with choppy market moves over the long-haul by not monitoring their cash levels carefully.

As a Foolish investor, you know that timing the market is a loser's game. It's not a good idea to hoard tons of cash with the plan to put it to work after the next market crash happens.

There's a huge opportunity cost in hoarding cash as you wait for the market to meltdown. And until the markets implode and there's blood on the streets, you'll lose by default. You'll miss out on dividends, capital gains, etc. And all the while, your cash hoard loses its value from the insidious effects of inflation.

On the flip side, being all-in on stocks with no cash has the potential to have a disastrous outcome, especially if you haven't invested through the last Financial Crisis. Opportunistic investors like Warren Buffett know that market crashes are nothing more than a fire-sale on stocks. If you don't have the cash to spend at the biggest Boxing Day Blowout of the century, you're probably not going to be happy as you watch others scoop-up the door-crasher deals at huge discounts.

So, this brings up the question: How much cash are you supposed to hold? What's the optimal amount? How do you know when you've got too much?

There is no one-size-fits-all answer as to the exact amounts of cash you should hold at any given instance in time. It depends on the individual, their risk tolerance, their confidence in the markets, the amount of wealth they have, etc.

Warren Buffett likes to think of cash as OxyClean. We don't want spills (market crashes) to happen, but

they will eventually happen, and if you've got some OxyClean stored away in your closet, you'll be able to prevent your brand new carpet (your portfolio) from getting stained. And for those worried about damaging their carpet, hoarding a garage full of the stuff isn't the best course of action either.

The right amount of cash to hold is enough such that you'll be able to meaningfully accelerate your recovery time from a potential crash thanks to the outsized gains you'll receive as you continue averaging down on severely beaten-up stocks or one-stop-shop ETFs like the **BMO Low Volatility Canadian Equity ETF** ([TSX:ZLB](#)). If you keep averaging down (or up) when it's crash time, you'll be able to recoup the money you've lost well before the indices make a full recovery. The effects will be even more pronounced in the event of a V-shaped recovery.

Also, you'll want to consider overall valuations at a given point in time. If stocks are [expensive](#) and everybody's sanguine, consider adding to your cash hoard. And if stocks are cheap and everybody's worried as they were late last year, lessen your cash hoard to do some [buying](#).

In short, the amount of cash you should be holding in your investment accounts fluctuate with time. It should never be at or around zero, but it also should also never comprise a majority of your wealth unless you believe that there's a severe shortage of opportunities out there.

As an investor, you should continuously monitor your cash levels and make sure you never find yourself in a situation where you've got a mountain of cash when stocks are cheap and vice-versa.

If you're not quite sure what's on sale at a given instance, the ZLB and its robust lineup of hand-picked dividend-paying securities is a great go-to basket of investments that you can feel confident betting on if ever your cash hoard swells up more than you'd like.

Stay hungry. Stay Foolish.

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1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:ZLB (Bmo Low Volatility Canadian Equity ETF)

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1. Msn
2. Newscred
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Author

joefrenette

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