



## TFSA Investors: Do you Have an Edge Over the Smart Money?

### Description

No matter which industry you pick, economies of scale usually matter. More resources usually leads to better performance, whether you're trying to launch an online jewelry store or developing property.

However, finance is inherently unique. Size and resources may open up more opportunities for wealthy investors and large institutions, but it doesn't necessarily translate into better performance. At least not by much.

The typical high-net-worth investor or family office has plenty of access to startup investment opportunities, private equity funds, private credit instruments, real assets, fund of funds, secondaries funds, and other sexy investment vehicles. However, data published by Pitchbook showed that the difference in performance between private deals and public markets has been marginal since 2006.

Alternative investments have delivered an 8.44% internal rate of return (IRR) for the 10 years ended December 31, 2018. Meanwhile, venture capital funds have delivered an IRR of 7.48% over the same period. By comparison, the plain-vanilla **S&P 500 Index**, which you and I have access to, has delivered 9.06% for the same period.

Even the relatively less diversified **S&P/TSX Composite Index** has also delivered a 157% return or 9.89% annualized return over the past 10 years, so Canadian investors haven't missed out on exceptional performance.

So it seems the difference in performance isn't as extreme as most would imagine. In fact, the average retail investor saving up for retirement and investing in public stocks through her Tax-Free Savings Account (TFSA) has some advantages over the so-called "smart money."

### More wiggle room

The biggest advantage retail investors have over their institutional counterparts is the freedom to invest in anything. Asset managers are hamstrung by their clients and restricted to certain geographies or asset classes.

These professional money managers also have watertight rules on portfolio holdings, position duration, maximum leverage, cash reserves, and diversification. Retail investors, on the other hand, can take a high-conviction bet on relatively small companies with higher risk profiles like Bitcoin mining company **Hut 8 Mining Corp** or unmanned aerial vehicle startup **Drone Delivery Canada**.

Retail investors also have the luxury of longer time horizons. Professional money managers bear the risk of client withdrawals and may have to limit their time horizon or investment universe for greater liquidity.

## Domain expertise

Perhaps the biggest advantage for regular investors is their domain expertise. An investor with decades of experience in [auto parts engineering](#) or retail branding may have plenty of insights when it comes to picking specific investments like **Magna International** or **Canada Goose**.

By comparison, a portfolio manager who has spent decades in the financial industry may lack the intuition or granular knowledge necessary to pick winners and losers in certain industries.

## Index investing

Finally, retail investors have the opportunity to invest passively in index funds while professional managers must justify their fees with active management. The fact that passive strategies have outperformed active funds over the past decade makes this a clear advantage for retail TFSA investors.

## Bottom line

The freedom to invest with longer time horizons, make contrarian bets with conviction, and deploy domain expertise in decision-making gives the average retail investor an edge over the professional money manager when it comes to stock picking.

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