Here’s How Many Stocks You Need to Diversify Your Portfolio

Description

When it comes to investing, having adequate diversification in your portfolio is a major key to managing risk and ensuring long-term success.

There are a variety of potential risks that all companies face, regardless of their quality or competence of management, that are unforeseeable but could potentially have major impacts.

Because of this, it’s crucial that you not only own a variety of companies operating in different industries but also that you don’t overexpose yourself and invest a major portion of your portfolio in one company.

The thing is, though, it’s also possible to overdiversify, where you buy too many stocks.

Once you have reached the optimal number of companies in your portfolio, adding additional stocks is no longer lowering the risk of your investments. This wouldn’t necessarily matter if there wasn’t a negative effect of this; however, there is.

Once you no longer gain a benefit from adding a new stock, because you are no longer reducing risk, all you are really doing is investing money in new stocks that won’t earn as high of a return in theory; otherwise, you would have invested in that stock in the first place.

In other words, sticking to a core group of 12-20 stocks spread across numerous industries is what’s best for most investors. Any more or less, and your portfolio won’t be as optimal and as efficient as possible.

With hundreds of choices of investments to make, picking the top 20 or fewer stocks will mean selecting only the highest-quality companies, businesses that you can hold forever.

A good example of a quality long-term pick is a company like **Shaw Communications** (TSX:SJR.B)(NYSE:SJR).

Shaw is a growing telecom, offering investors major opportunity over the long run, as it grows out both its wireless and wireline businesses.

It’s always had a strong wireline business in Western Canada, but now, with its purchase of Wind Mobile and subsequent rebranding to Freedom, Shaw is looking to take on the Big Three telecoms and steal away a fair amount of market share for itself.

Currently, Freedom has a little over 5% of the Canadian market, with the Big Three combining for over 90% of the market share, so it’s clear that if Shaw is successful, there is a massive runway for growth.

The company has been aggressively trying to lure customers through high-value contract offerings or cheaper prices — anything to try and build its market share.

Plus, it’s pretty evident that the Canadian government is interested in seeing more competition in the telecommunications space, which bodes well for Shaw, as it tries to carve itself a nice slice of the growing market.

To take on major companies and be successful, the two things Shaw is going to need is time to make it work and a strong financial position, both of which it has.

All of this long-term potential makes Shaw attractive, and then when you consider that it’s trading at just an 18 times its price-to-earnings ratio and pays investors a monthly dividend that’s yielding more than 4.85%, it’s immediately clear how attractive a long-term investment it is. In addition, its beta is just 0.8, so it’s a lower-volatility stock that will help to preserve your wealth.

The stock is trading at bottom of its 52-week range, and with the stock selling off another 4% already this week, there’s no better time to gain some exposure and buy this top long-term company.

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