Avoid This 1 Big Investing Mistake

Description

Through discussions with investors and reading many investment articles, it is clear that many people care about buying stocks at fair value. While I think there are reasons to care about finding stocks that are not extremely overvalued, I think investors should avoid investing in companies simply because certain metrics say it is undervalued.

One of the most common companies I see suggested as a good investment is **Enbridge** (TSX:ENB)(NYSE:ENB).

Why should you not invest based on whether a stock is undervalued?

Enbridge is one of the largest oil companies in Canada. The company generates, distributes, and transports energy across North America. Looking at its utility and power segment, Enbridge services 3.8 million commercial, industrial, and residential customers in Ontario and Quebec alone. The company has also been focusing on increasing its renewable energies business in recent years.

The company is highly touted as a top investment among financial circles. The reason for its high conviction among retail investors is the company's reach across the continent. As mentioned earlier, Enbridge is responsible for distributing utilities to a wide network of customers. This has been translated into decent revenue growth over the past four years. Over that period, Enbridge has reported a 45% growth in revenue. The company is also known for its high dividend yield (6.93% at the time of this writing).

However, institutional investors and market movers have had a different opinion on the company. Over the past five years, dividends excluded, Enbridge stock has decreased 21.46%. When including dividends, your annual return from this company would still only be 0.42%. That is a severe underperformance that lags the broader market, interest from savings accounts, and inflation. Yet retail investors still seem to advise each other to add the company to their portfolio.

What should you do instead?

When looking for companies to invest in, I tend to do the opposite of what other investors do. I prefer to pay for high-quality stocks. Take **Docebo** for example. Ever since I first covered the company two months ago, its stock has more than doubled. Not to mention other companies that have been outstanding year to date: **Northland Power** (+36.44%) and **Shopify** (TSX:SHOP)(NYSE:SHOP) (+144.43%). Paying for high-quality, high-growth stocks is a good way to invest.

You should also be wary about "buying the dip," as investors like to preach. There is often a legitimate reason for stocks to go down. That could be deteriorating moats or lack of faith in management. Instead, you should keep adding to winners.

Going back to the Shopify example, say you wanted to add money to fund that position at the start of each quarter this year. On January 2, 2020, you would have paid $530 per share at that point. On April 2, you would have paid $493 per share. Finally, on July 2, you would have paid $1397.

As of this writing, the first tranche would have grown 144% and the second tranche would also be up 163%. Unfortunately, the third tranche would be down 7.3% at the time of this writing. However, Shopify's stock price also decreased for your purchase of the second tranche, and you would have still gone up an incredible amount since then. Stocks will go up and down, but as we believe here at The Motley Fool, "winners win."

Foolish takeaway

I would avoid companies that seem undervalued but have little else going for them. There are many other great companies out there that will give you market-beating returns. Instead, pay up for quality and keep adding to your winners.

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