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Time to rethink your investment strategy?

Investment market turmoil may have prompted you to change your investment strategy in recent times. Is it time for a rethink?

Investment market losses over the past two years came as a shock to many investors who had been enjoying consistent gains over a prolonged period. Like others, you may have watched your invested capital lose value as the global financial crisis took hold. If you moved your money into the relative safety of cash or fixed investments, you may be thinking "should I change my strategy again?"

If you're a smart investor, you'll review your investment strategy on a regular basis because circumstances can, and do change.

Back to Basics

It's important to remember the basic rules of investing.

The strategy you adopt for your investments should always consider three things together: your goals, your timeframe and how you feel about risk.

1- Don't lose sight of your goals

When things are looking bad in the short-term, it can be easy to get caught up in the bad news and lose sight of your long-term goals.
Investment markets are less volatile now than they were in 2008 and the first half of 2009. If you changed your investment strategy during this period, now's the time to take another look at it. Is it going to help you achieve your investment goals?

2- Know your investment timeframe

Your timeframe for investing will depend on your goals. In the short-term, you could be saving to buy a new car or take an overseas holiday. Your longer-term goals could be to save for your home deposit, children's education or your retirement.

3- Understand your appetite for risk

Riskier investments such as shares can lose value in the shorter term so they generally aren't considered suitable for a short-term investment strategy, but over a longer period, they have the potential to generate significantly higher growth than a cash investment. Generally speaking, the longer your investment timeframe, the more likely volatile investments such as shares can recover from any downturn in the market.

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The Australian share market reached its lowest point in Mach 2009, and had last been at these levels around August 2003. Despite this, the All Ordinaries Price Index managed to rise 33 percent over 2009, illustrating how share markets can experience rises and falls over the short-term.

Risk and strategies to help reduce it

Your appetite for risk may have changed in recent times so it's something you need to carefully consider when deciding where to invest your money. But there are ways to help reduce risk.

1- Diversity

No one can predict which asset class will be the next top performer, so one way to reduce the risk of loss is to spread your investment across a range of asset classes. This could include Cash and Fixed Interest (eg. Term Deposits), Australian shares, International shares and Property.

2- A regular investment plan

If you're not ready to invest a lump sum, a regular investment plan could be the answer. Investing a regular amount into a shared portfolio, for example, can help smooth out any short-term volatility because instead of trying to pick an opportune time to invest a lump-sum, by investing the same monthly amount, you'll be buying fewer shares when prices are high and more shares when prices drop.

Let's say the share price is $1 per share and you invest $100 in the first month, you would buy 100 shares. If in month two the share price rose to $1.02 per share, you would only buy 98 shares for your $100. In month three when the share price say dropped to 95 cents, you would buy around 105 shares.

Over the longer term, as shares can increase more in value on average than a cash or fixed interest investment, this strategy can potentially result in you achieving a higher level of growth.

3- Cash and Term Deposits are not a risk free alternative

A cash investment may appear safe in isolation. However by staying in cash alone, you could be missing out on opportunities to get a significantly higher return on your investments.

You could potentially miss out on higher returns on your investment if you spend too much time out of the market. Pulling out before markets recover can make a substantial difference to your investment earnings. Short-term movements should not influence your investment decisions and the key is to focus on your long term strategy.