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How to Build Your Investment Portfolio

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How you invest your money can shape how you build your future. This is true whether you are in your 20s and just starting to save up for a new home or you are in retirement and managing your money through your golden years. Creating a solid investment portfolio may be one of the most important determinants of your financial success. With tens of thousands of stocks, bonds, mutual funds, ETFs and other investment options to choose from, where should you start?

Constructing the right portfolio to meet your goals can be daunting. For many, it's similar to renovating a house and not knowing where to begin. Do you meet first with the contractor or the architect? Do you include a decorator now or later? Do you move out while the work is underway or do you stay put? How do you orchestrate all the pieces necessary to make it run smoothly and efficiently? As with any formidable project, the best thing to do is to break it down into smaller, more manageable tasks. Here are some fundamental and easy-to-implement steps to follow when building your investment portfolio. Hopefully, they will help you simplify what can often feel like an overwhelming job.

Separate saving and investing. Think about your big-picture financial goals. For example, saving to purchase a new house is very different than putting money aside for retirement. So, separate your goals into short-term and long-term objectives. Any money you'll need in the next five years should go into savings, not the stock market. Stocks are too risky and volatile in the short term. If you plan to buy a house in the next couple of years, consider keeping the down payment in a savings account. Amounts set aside for retirement (or maybe a vacation home a long way into the future) can be invested. Only put money in the market if you're able to leave it there for five years or more.

Gauge your risk tolerance. Investing is a balancing act. The more risk you're willing to accept, the higher the long-term returns you can hope to receive. But can you stomach big ups and downs in the market? Can you leave money invested for many years? If so, your portfolio can be on the more aggressive side. On the other hand, are you close to, or in, retirement and require that money to be there for ongoing living needs? If so, your portfolio may need to be on the more conservative side (less risky). Accurately and honestly evaluating your risk tolerance is important because there are few better ways to tank your returns than panic-selling in response to market volatility.

Get the mix right. Risk and return are related. Historically, equities have offered higher returns with greater risk. Bonds are generally less risky, but their returns are typically lower. High-quality bonds benefit the overall portfolio by managing the volatility you see in the equity markets. The right mix for you is the one that provides enough return to meet your goals without being so risky that you can't sleep at night.

Diversify. Don't put all your eggs in one basket. This well-worn nugget of wisdom never goes out of style. Using low-cost, evidence-based mutual funds, spread your equity exposure across multiple asset classes. Balance out your exposure to large company stocks by allocating a portion of your portfolio to small companies. International companies create another level of diversification, balancing out your domestic stocks. Add in real estate through a well-diversified real estate investment trust. Build your bond component using high-quality, short-to-intermediate term bonds. Don't let any single holding dominate your portfolio.

Stay in balance. The most reliable predictor of your investment results is your overall allocation and ability to stay disciplined. Once you've built a diversified and risk-appropriate portfolio, the key is to keep it that way. As different elements of your portfolio advance at different rates, your 70/30 allocation of stocks to bonds, for example, may drift to 60/40 or 80/20. Get back into balance by selling some of your best performers and spreading the gain across securities that have lagged. That's selling high and buying low.

Step away. Avoid the news you hear daily in the financial media. Often the biggest mistake investors make is letting their emotions override discipline. It's extremely important to not tweak and tinker with your holdings after every scary headline or market swing. Remember, investing is for the long term. Buy, hold, rebalance, and let the market work for you.

In a house renovation, if you take the time to lay out the steps, you can come away with a successful project. The same is true for building your portfolio. The preceding suggestions should help you get your arms around the important task of investing. If you lay out your goals, review your risk tolerance, diversify your portfolio and tune out the noise, you will have a great start to building the portfolio that can help you achieve your dreams.

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Stuart Vick Smith collaborates with women to help them achieve financial freedom. Along with her deep understanding of wealth management and tax, she helps her clients as a holistic planner instead of just an investment advisor. In her 10 years as partner with ML&R Wealth Management, she believes it is important to build and maintain long-term relationships. She connects with her clients on a personal level allowing them to develop a plan to support their long-term dreams for themselves and their families. She has been recognized in her industry and has been asked to speak at national events on the topic of women and wealth. Stuart lives in Austin, Texas and enjoys time with her husband, two kids and two rescue dogs.