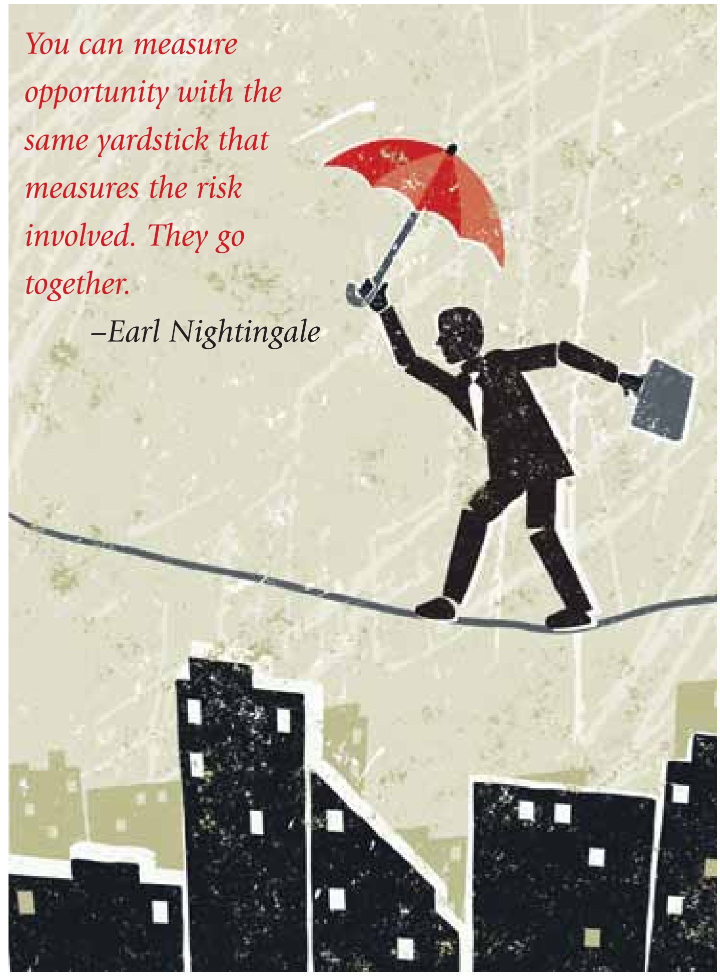
In the Age of Risk

By Jessica A. Maldonado

Your appetite for taking on risk can change throughout your years as an investor, depending on how and when you plan to utilize the results of your investment strategy. While you can never eliminate investment risk, managing the risk to meet your needs and align with your current sentiment is a strategy we encourage every investor to employ. Has your portfolio management fallen behind the times, leaving you exposed to more risk than you're prepared to handle?

Investors must understand their personal risk tolerance level because a certain amount of risk must be taken to garner returns. The level of risk, and therefore the portfolio allocation, is how the varied amount of risk will be allotted for each investor. An investment portfolio will not be allocated the same for an investor whose primary concern is minimizing risk as one whose primary concern is maximizing returns. These investors will have differing viewpoints on uncertainty, comfort levels and change. Basically, there is a difference in how much volatility each investor is willing to assume, but this also means there will be a difference in how their portfolios will perform.



Risk Throughout Life

Presumably, the amount of risk you are comfortable taking will change with your current life situation. Your age, investment goals and timelines, financial obligations and other financial considerations may factor into your choice for an appropriate level of risk. As a young investor with few or no dependents, one might choose to have more exposure to equity securities because statistically, equities garner higher average returns over the long run. Younger investors have a longer time frame in which to continue saving and buying equities at a lower price if the positive returns don't initially present themselves.

An investor nearing retirement may have more exposure to fixed income securities and cash equivalents to limit the volatility in the portfolio and produce income. However, even for an older investor, it might be necessary to have some exposure to equities to keep up with taxes and inflation.

The amount of risk taken does not only correlate with age, but also with your overall goals. An adult couple that still has more than 30 years to save for their retirement goals might also have the goal to fund their child's education and only have four years left to save for that expense. Their portfolio, or at least a portion of their portfolio, might look like an older investor's because their goals and timelines align with someone nearing retirement (i.e. both are working toward a major goal within a short time frame). These goals and special situations must be considered by yourself or your advisor when determining your risk tolerance level.

Proactively Managing Risk

Regardless of your risk tolerance level, managing risk is impacted by the investment principles that guide your portfolio. Perhaps one of the most risky moves you can make is not abiding by sound investment principles that should be guiding the exposure taken in your portfolio. Do you leave your portfolio exposed to the same investments regardless of the economic climate? Do you manage your fixed income holdings that same way regardless of the economy being in an inflationary period or recessionary period? Do you consider expansion and contraction of the economy and utilize investments that will fare better during those periods? Do you modify your investment weighting depending upon changing global economic conditions? By proactively managing your portfolio, you can better manage the risk associated with your investments. While common portfolio allocations (conservative, moderate, moderately aggressive, aggressive) may seem like safe "buckets" to help guide your percentages of exposure to various investments, how flexible are you with these allocations during changing economic climates? An investor should have a process to carefully select their investments, diversify their portfolio, monitor performance, and be flexible to make changes when conditions change.

Our investment portfolios can help us reach the goals we've set for our lives, but only if we're taking care of our portfolio. We cannot build a portfolio and then cross our fingers that it will work how we've designed it to through the highs and lows of the economy. Unless you're prepared to take on enormous amounts of intolerable risk, it's time to step up your portfolio management process to keep the risk working in your favor.

Jessica A. Maldonado is Chief Compliance Officer for Allos Investment Advisors, a registered investment advisory firm located in Overland Park, offering fee-only investment management services with no account minimums. For additional information, visit AllosAdvisors.com.