Too Much Risk or Too Little Risk – Neither is Good

Wise Investors Allocate Assets to Match Tolerance, Goals

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No matter what the value of an individual’s investment portfolio, whether it is $1,000 or $10 million, everybody has a “Baby Bear” level of risk tolerance that will set a path toward financial well-being.

Not too hot, not too cold; not too hard, not too soft – but just right.

Unfortunately, many investors establish their portfolios with an allocation of assets and degrees of risk that suit them at the time, and then go 10 or 15 years without reassessing. Lives change, circumstances change, attitudes change. And so, for example, that small-cap high-tech stock that gyrated between annual gains of 30 percent one year and losses of 40 percent the next, that looked like it might pay off in 10 years, now no longer looks so appealing as the investor begins thinking about retirement. The later in life an investor finds herself, the less time she has to absorb those huge losses that often accompany the big risks.

Likewise, investors need to keep in mind that a healthy balance between various investment vehicles – stocks, bonds, mutual funds, alternative investments and non-correlated investments – will improve an investor’s chances of reaching goals. What is that balance? It varies with every investor.

Asset allocation has become a more prominent focus among some investors recently in the wake of the upheaval in the stock market. They want to know how they can protect themselves from those huge fluctuations. A partial solution is a movement into bonds; but even bond values move in accordance with market conditions, both adverse and favorable. Thus, some investors have looked increasingly toward alternative investments such as energy, oil and gas equipment, real estate investment trusts (REITS) and even collectibles.

When we talk about non-correlated investments, we mean those investments that move up or down in value on their own accord, with little or no influence from the stock market. An easy example of a non-correlated investment is a fixed annuity, which is offered by life insurance companies.

While every investor should consider the proper asset allocation within a portfolio, not every investor has access to every investment vehicle. Some vehicles, such as most oil-and-gas drilling programs, are open only to qualified (accredited) investors, meaning those investors who can establish access to certain, reliable financial resources. For example, an investor might need to show that he or she has an annual income of $200,000, or net worth of $1 million. Other qualifications might apply.

Clearly, there is much to consider when examining a portfolio’s asset allocation, and sometimes it helps to have a trained professional examine the history of the portfolio, set it against the
current economic landscape, and compare it with the investor’s current goals and attitudes. A good wealth advisor will consult with the investor before making any moves within the portfolio, asking a set of detailed questions, to arrive at an accurate picture of an asset allocation that will work best for that investor.

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