STONEBRIDGE
Capital Advisors

Risk and What That Means to You

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The Bridge

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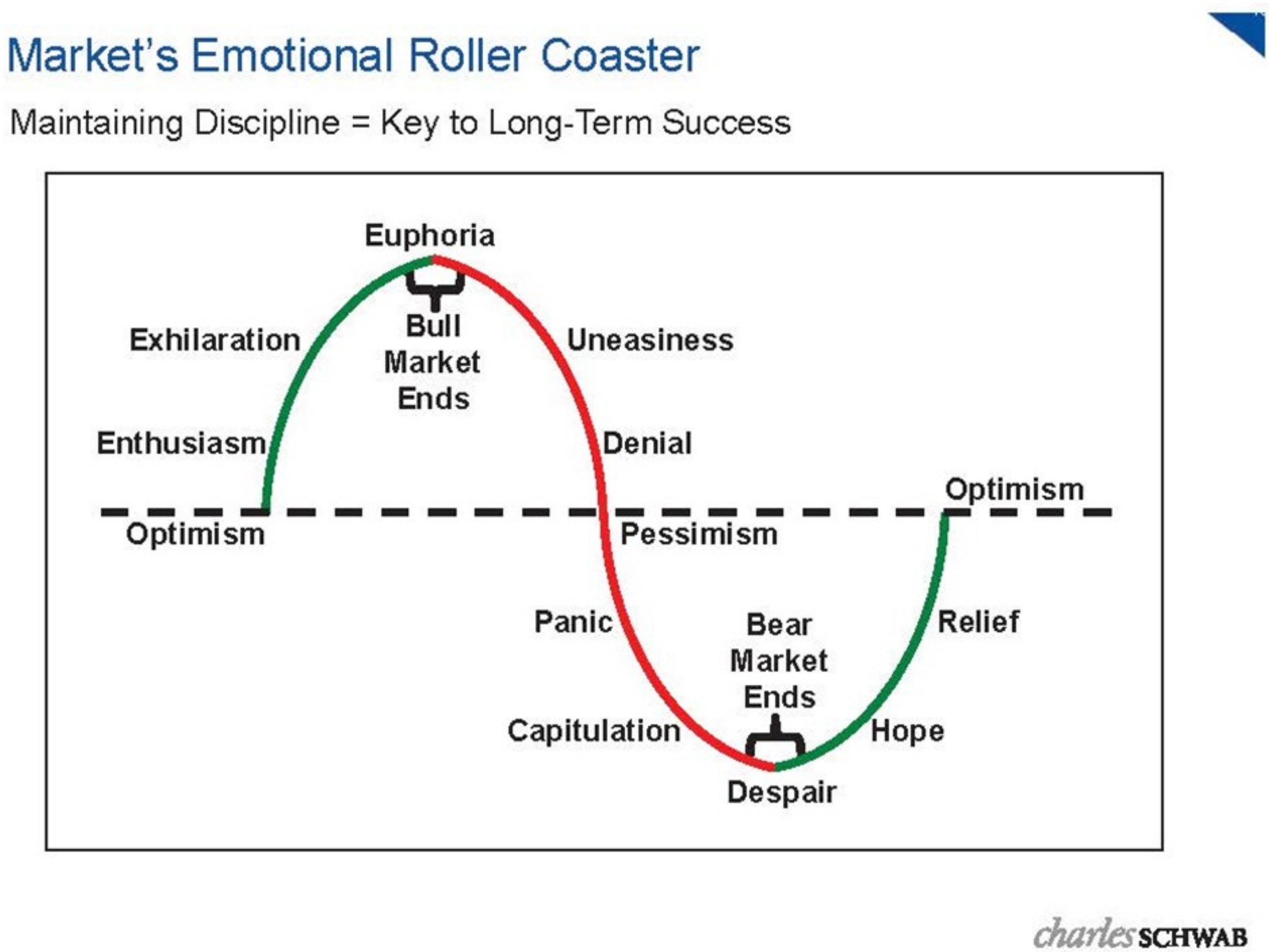
Generally speaking, if you have been invested in the stock market over the past 9 years, you have had a positive return. Since the Great Recession that ended in June of 2009 the S&P 500 has had an annualized return of 12.65% (14.93% with dividend reinvestment). This has been a great time to be in the equity market. It should also be a time to review and reflect the amount of risk that you are willing to take with regards to your investments.

Investing can tend to feel like a roller coaster sometimes, there are many ups and downs. Chart 1 illustrates the emotions that an investor might feel. On the upswing of a market, people feel positive and everything is good. On the downside the opposite is true. If you know what your risk tolerance is, you can both minimize the ebbs and flows of your emotions and also make better choices in regards to your portfolio and personal wealth.

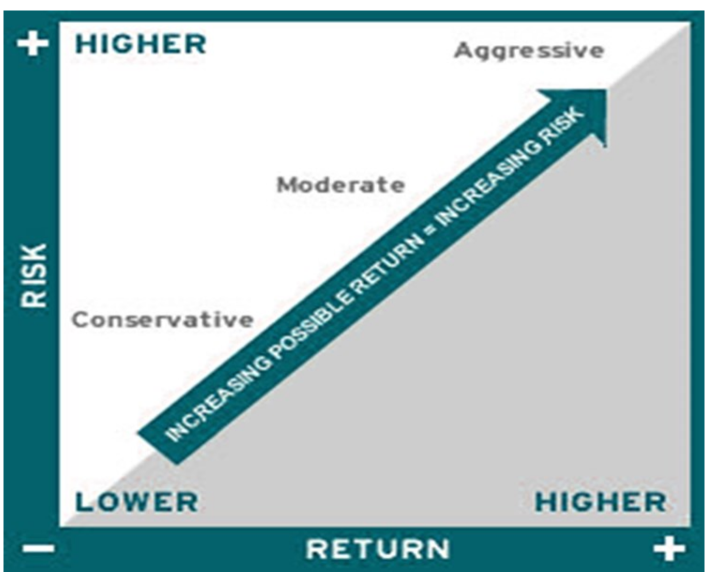
Chart 1



What Does High or Low Risk Tolerance Mean and Look Like

In order to have a true understanding of your current risk tolerance, it is important to think about the time frame that you are dealing with and the ultimate goal that you want. The ability to withstand higher losses is what determines your risk tolerance. People that have a longer time frame to work with, tend to have a higher risk tolerance. They are able to withstand a larger lose in their portfolio due to the amount of time they have to make that loss up. The closer a person gets to retirement, their risk tolerance might change. They might want to become slightly more conservative to preserve the assets that they have. As you can see, both your risk tolerance and your goal may change over time. It is not something that you need to be locked into for the entirety of your life. Life events happen, investment goals change and so does the risk that you are willing to take. Chart 2 provides a visual of risk verses return.

Chart 2



Higher Risk Tolerance:

What does a higher risk tolerance portfolio look like? That can vary a little bit, but in general it is a portfolio that has a higher concentration in stocks and might be willing to go down the rating scale for fixed income securities. The stocks in the portfolio will lean towards growth stocks that are expected to grow above the average rate compared to the market. They usually do not pay a dividend, as they are reinvesting their money into capital vs. giving the money back to shareholders. Investors should expect higher returns over time but should also expect more volatility. If the stock market has a pullback or goes into a recession, these securities will tend to get hit harder than lower growth stocks.

Age plays a role in whether or not an investor has a high-risk tolerance or not, but it is not the only factor. As we mentioned earlier people tend to be more risk averse the closer they get to retirement, but that isn't always the case. People who understand the risks they are taking and are fine with the potential downside effects of a market may still choose to have a riskier portfolio. It might be a portfolio that is intended for the next generation in their family. If that is the case, historical market returns could suggest that staying invested in riskier assets meet those goals and objectives.

Lower Risk Tolerance:

What does a lower risk tolerance portfolio look like? Again, this can vary from account to account, but generally speaking these accounts will have a higher allocation to fixed income. The allocation of equities to fixed income may vary, depending on the level of security that each investor is looking for. Some accounts may be closer to a 50/50 split, while others might be 100% fixed income.

The fixed income in these portfolios usually lean towards invest grade securities. The equity portion of the portfolio may have a tilt towards dividend paying stocks. Companies that pay dividends provide income during retirement and tend to be less volatile during market corrections.

This type of investment tends to be of more comfort for people that are close to retirement or are currently retired. It can also be used for people that just can't handle the emotional swings of a market. That can include people that are many years away from retirement but they lose sleep at night worrying over risk in the investment decisions that have been made. There is nothing wrong with that either. If you are losing sleep and have anxiety over the makeup of your portfolio, it might be a sign that you have too risky of a portfolio. If that is the case you should get in contact with your advisor and go over your portfolio to try and understand the risk level and potentially lower it.

Conclusion

As I stated earlier, your risk tolerance is something that should be looked at and reviewed over time. It changes with market cycles and life changes. Meeting with your advisor, accountant or any other investment professional that oversees your portfolio to review where you stand is highly recommended and allows all parties to better understand what step (if any) should be taken going forward.

Sources:
All data sourced through Bloomberg.
Chart 1 provided through charles Schwab
Chart 2 provided through Motif Investing