

# Portfolio Risk Tolerance

When it comes to investing, many people associate risk with losing money. But investing entails different types of risk. Understanding each type -- and the potential return associated with your retirement portfolio -- can help you determine whether your investments are appropriate for your situation.

## Examining Risk and Return

Stocks historically have exhibited the highest level of market risk -- or the potential that an investment may lose money in the short term. Over long periods of time, however, stocks have outperformed both bonds and cash investments.<sup>1</sup> This risk/return tradeoff may influence how you allocate your investments. For instance, consider weighting assets that you intend to keep invested for 10 years or more toward stock investments.

Bonds carry their own risks -- credit risk, or the possibility that a bond issuer could default on interest and principal payments; and interest rate risk -- the chance that rising interest rates could cause a bond's price to fall. Ascending interest rates historically have influenced the prices of bonds more directly than the prices of stocks.<sup>1</sup> When short-term rates are on the rise, investors may sell older bonds that pay a lower rate of interest -- causing their prices to fall -- in favor of newly issued bonds that pay higher interest rates. On the plus side, bonds historically have exhibited less short-term volatility than stocks, although past performance is no guarantee of future results.

It's also important to look at cash investments, such as 3-month Treasury bills, from a vantage point of risk and return.<sup>1</sup> Although Treasury bills typically experience a low level of volatility, they may be subject to inflation risk -- or the possibility that their returns may not keep pace with the rising cost of goods and services. For this reason, you may want to use cash investments for short-term situations when you expect to access your money within 12 months or less.

## Putting Risk in Perspective

Because all investments entail risk, you may want to review your mix of stocks, bonds, and cash investments with an eye toward creating a risk/return profile that is appropriate for your situation. Owning different types of assets may increase your chances of experiencing the benefits associated with each, while mitigating the corresponding risk. Your retirement portfolio won't be risk free, but you will have the confidence of knowing that you've done what you can to manage a potential downside.

This article offers only an outline; it is not a definitive guide to all possible consequences and implications of any specific investment strategy. For this reason, be sure to seek advice from knowledgeable financial professionals.

## Source/Disclaimer:

<sup>1</sup>Source: Wealth Management Systems Inc. For the 30-year period ended December 31, 2013. Stocks are represented by the Standard & Poor's Composite Index of 500 Stocks, an unmanaged index that is generally considered representative of the U.S. stock market. Investing in stocks involves risks, including loss of principal. Bonds are represented by the Barclays U.S. Aggregate Bond index. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price. Cash is represented by the Barclays 3-Month Treasury Bills index. It is not possible to invest directly in an index. Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest, and, if held to maturity, offer a fixed rate of return and fixed principal value. Past performance is not a guarantee of future performance.

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