



**BCWM**  
PROVIDING PEACE OF MIND



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## What is Your Tolerance for Investment Risk?

In the data gathering phase of the financial planning process, assuming the process is followed, it is not uncommon for the typical financial advisor to ask questions related to their prospective client's risk tolerance. A common financial profiling interrogation might sound like this:

Investing involves a tradeoff between risk and return. Historically, investors who have received high long-term average returns have experienced greater price fluctuations and higher potential for loss than investors who have received lower long-term average returns. Considering the above, which statement best describes your investment goals?

- Protect the value of my account. In order to minimize chance for loss, I am willing to accept the lower long-term returns provided by conservative investments.
- Keep risk to a minimum while trying to achieve slightly higher returns than provided by more conservative investments.
- Balance moderate levels of risk with moderate levels of returns. I am willing to accept occasional losses because I have the time horizon that allows time for recovery.

Maximize long-term investment returns. Therefore, I am willing to accept large and occasionally dramatic fluctuations in the value of my investments.

It is likely these advisors have good intentions. The problem is the advisors are leaving it up to their clients to tell them how much risk they are willing to take without any regard for how much risk they NEED to take.

At Boyer & Corporon Wealth Management we have enough combined industry experience to know investors' tolerance for risk vary widely based on market conditions. When stock markets are on an upward trend, investors' tolerance for risk tends to be higher. Conversely, when stock markets are on a downward trend, investors' tolerance for risk tends to be lower.

At BCWM we maintain that investment risk has three key elements: Need, Ability and Willingness.

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Instead of asking our clients to tell us their risk tolerance, our proprietary process tells them how much risk they need based on several key assumptions which are unique to them. The amount of risk an investor needs to take is determined by calculating the average, annual, after-tax rate of return which is required to make the investor's financial plan succeed. The lower the required rate of return, the lower the need for investment risk. Our long-time clients have learned we refer to this as their level of risk, and it is closely monitored during regular Wealth Management reviews.

Next, we assess our clients' ability to take financial risk. Interestingly enough need and ability are often inversely related. For example, Bill and Melinda Gates likely have the ability to survive a large loss on their investment portfolio, but probably do not need much return to meet their financial planning goals and objectives. By comparison, a 60 year-old couple who hasn't saved much for retirement does not have the means to survive a large loss on their investment portfolio, but probably needs a fairly high return to meet their goals and objectives.

The last element is willingness. It is not uncommon for us to work with a client whose need for risk is low, but their ability is high...and therefore, so is their willingness. The key here is we have defined how much risk they need. From there it is up to them to tell us if they are willing to take on more risk, as unnecessary as it might be. At least this decision is being made from an educated, mathematical perspective rather than an emotional one.

You may remember the ad campaign from several years ago where a prominent financial services company was highlighting individuals with their "number" following them around like a storm cloud. This was certainly a catchy ad campaign; however, if you ever used their too-simple retirement calculator it would quickly spit out a large, "pie in the sky" dollar amount that would leave you asking, "OK, now what, and how do I get there?" I suppose it was their goal to invoke some fear so you might contact one of their financial advisors to shed some light (translated...sell you some product).

When reviewing investment performance, we feel it is important to not only know your rate of return, but to also understand how much risk was involved to earn said return. In other words, what was your "risk adjusted rate of return"? The investment with the highest return is not always the best investment after accounting for risk. This type of risk management is where our Portfolio Management Team excels.

If you are a client of BCWM and someone asks you, "What is your number?" you can confidently respond, "I not only know the number...I know how much risk I need to take to get me to that number!"

