



# Understanding & managing risks

A little risk can improve the overall returns on your savings and investments

BY LILIAN NG

**R**isk means different things to different people. Some investors take risk to mean volatility or the swings in asset prices. In this way, stocks are widely perceived to be more risky than bonds or bank deposits because their prices tend to fluctuate more.

In statistics, risk is defined as the chance that the actual outcome of an investment would be different from the expected outcome. In this respect, all investments with the exception of bank deposits and fixed income instruments are risky since the actual outcomes would in most





• **Diversification over time**

Time enables you to tap into the power of compounding. It also enables you to ride out the worst business cycles that affect some asset classes like stocks.

• **Diversification over asset classes**

By spreading your investments over different asset classes such as bonds, stocks, commodities and real estate, through an asset allocation strategy, the overall portfolio risk is reduced because each asset class has different boom and bust cycles.

• **Diversification over geographical boundaries**

Different countries go through different phases of the economic cycles at different times. While some countries may be going through depression and tough times now, other countries may be having a booming good time. By investing in different countries, you balance out the risks.

Risk is not all bad. In fact, a little risk can do a lot to improve the overall performance of your investments. So understand risk, manage it and learn to profit from it. **1**

• **Commitments and responsibilities**

– A sole breadwinner with young school-going children may not be able to take on the same kind of risk as one who is single and without family responsibilities.

• **Personal chemistry**

– If you tend to overreact to bad news and to play down good news, then stay away from stocks and just stick to safe and secure investments like time deposits.

• **Earning power**

– If you are a high-income earner with a relatively secure income source,

you might be able to deal with a higher-risk portfolio. On the other hand, if your income varies significantly yearly, then you will need to take a more conservative investment approach.

Most investment advisers would have standard procedures to help you discover your risk tolerance level. If you answer the questions truthfully, you will indeed be able to find out how risk averse you are. Put yourself in a worst-case scenario and then ask yourself how you would react. You may be risk averse but do understand that there are ways to reduce risks:

