



Third Quarter 2024

Balancing Willingness to Take Risk and Ability to Take Risk

When it comes to the return we really want from our investments, the answer is generally the highest possible. But risk must also be a part of the investment decision.



Most people accept the fact that higher return requires taking greater risk, but all too many assume that higher risk assures higher returns. That's not the way it works. Risk is the possibility that you will lose money, sometimes all your money. If risky investments did not offer the potential for oversized gains, no one would invest in them. But accepting risk is never a guarantee of profit.

In building portfolios for clients, one of our questions is how much risk you are comfortable with, i.e. if your portfolio loses 10% will you be looking for another advisor? What about 20%, 30% or more?

While the long-term trend of the market is up, recent bear markets have resulted in losses of 25% and up. If you are determined your portfolio returns should equal the performance of the S&P 500 Index, investing in an Exchange Traded Fund that tracks the S&P 500 will achieve your goal, but can you accept the accompanying risk?

Recent Bear Market Periods	Duration	Total S&P 500 Decline
March 2000 to October 2002	31 months	-49%
October 2007 to March 2009	17 months	-56%
February 2020 to March 2020	1 month	-34%
January 2022 to October 2022	10 months	-25%

As a financial advisor, our role is that of a fiduciary. That requires that we look beyond your stated **willingness** to assume risk to your **ability** to take risk. How much loss can your portfolio reasonably assume without causing financial distress? This takes into consideration hard facts, including:

- **Age** – Do you have time to replace lost savings or recover from a down market?
- **Life status** – Are you retired, unemployed, under-employed? Do you have health issues, dependents, major life changes coming up? What are your savings goals?
- **Current assets** – Do you have sufficient assets that a loss will not negatively affect your present life and long-term financial requirements? How much can you risk in the pursuit of higher returns?
- **Job stability** – If a high-risk investment loses value, will you be able to rebuild your net worth through savings from your work?
- **Emergency savings** – Do you have sufficient available funds to wait out a market recovery period, a disaster, or a family emergency without having to liquidate investments?

Willingness to Take Risk and Ability to Take Risk change over time, which is why it is important to provide your advisor with updates as your life changes. Our goal is to assure your financial security over time while managing the risk of investing.



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