

## **Risk Tolerance Review and Questionnaire**

Investors face three primary risks:

1. Loss of principal
2. Loss of purchasing power
3. Insufficient growth

### **1. Loss of Principal.**

Loss of principal is the most obvious and perhaps scarier of the three risks. Loss of principal happens any time the market price of an investment falls in value. Most investors understand that asset prices fluctuate in value over time and many (but not all) can often tolerate relatively small and short-lived declines in value. However, an investor's comfort level can be severely strained whenever there are significant declines in value and/or the declines last for long periods of time. For example, the bursting of the dot.com bubble in 2001 to 2003 saw the S&P500 decline 50% and the credit/housing implosion in 2007/2008 saw a 55% decline in the S&P500. During the Great Depression of the 1930s the S&P500 lost 89% of its value. These historically large, out-of-trend "train wrecks" are unpredictable and should serve as a limiting factor on the portion of a portfolio invested in assets that are vulnerable to "loss of principal" risks.

Assets most vulnerable to loss of principal are "equity" ownership in corporations and natural resources (i.e. stocks and stock mutual funds). Bonds are generally viewed as good protection from loss of principal. However, bonds can also lose value if not held to maturity or via default, particularly in the event of rising interest rates. Historically, bond losses have been small relative to equities.

The safest assets (FDIC insured CDs, money markets and savings accounts) are very unlikely to lose principal but may not provide sufficient growth to meet the investors long term needs or offset the effects of inflation.

### **2. Loss of Purchasing Power**

Loss of purchasing power occurs when the portfolio grows at a rate below the rate of inflation. Inflation has two main sources: an imbalance between supply and demand in the economy (demand exceeding supply) and/or the central government growing the money supply at a rate greater than the growth rate of GNP (i.e. devaluation of the dollar). This is a particular threat to very conservative investors because their portfolio may contain too many low growth assets whose returns may not keep up with inflation.

### **3. Insufficient Growth**

Most long term investors need their investments to grow in order to meet their financial goals. The rate of growth needed will vary with each investor. In a relatively free market economy like the U.S. there is a direct relationship between the potential for growth of a particular asset and the risk of losing principal. In other words, in order to achieve higher returns, higher risk must be assumed. Historically, equities have provided higher growth than either bonds or cash equivalents (CD, money market). However, as discussed above, equities expose the investor to a higher risk of losing principal. Inflation is also a factor since an investor must earn a minimum of the inflation rate in order to maintain constant purchasing power.

**Therefore, the investor must reach a strategic trade-off between these three risks that recognizes their individual risk tolerance as well as their view of current and future economic conditions.**

**The following questions may assist you in deciding how you would like your portfolio to be designed and managed.**

## Risk Tolerance Review and Questionnaire

1. What is your Age?

- ☐ a. Over 65
- ☐ b. 55-64
- ☐ c. 35-54
- ☐ d. under 35

2. When do you plan to begin taking withdrawals from your portfolio?

- ☐ a. 1 to 3 years
- ☐ b. 4 to 7 years
- ☐ c. 8 to 10 years
- ☐ d. after more than 10 years

3. How stable are your current and future income sources (salary, SS, pensions)

- ☐ a. very unstable
- ☐ b. somewhat stable
- ☐ c. stable
- ☐ d. very stable

4. When it comes to investing in stocks, bonds or mutual funds you would describe yourself as:

- ☐ a. very inexperienced investor
- ☐ b. somewhat inexperienced investor
- ☐ c. experienced investor
- ☐ d. very experienced investor

5. How would rapidly falling market prices affect you emotionally?

- ☐ a. dramatically affect me
- ☐ b. moderately affect me
- ☐ c. marginally affect me
- ☐ d. almost no effect

6. How optimistic are you about long term economic prospects?

- ☐ a. pessimistic
- ☐ b. unsure
- ☐ c. somewhat optimistic
- ☐ d. very optimistic

7. Which of the following statements best describe how you would like your portfolio to be managed?

☐ **a. Conservative**

I want all, or almost all, of my portfolio to be in assets with little to no fluctuation in value and I am willing to accept the potential for lower returns and loss of purchasing power.

☐ **b. Aggressive**

I want all, or almost all, of my portfolio to be in assets with high potential for growth in value. I am willing to accept that my portfolio may lose substantial value for short and even long periods of time.

☐ **c. Moderate**

I want my portfolio to provide an approximately equal level of protection from the three primary risks described above.

### Risk Tolerance Review and Questionnaire

☐ **d. Moderately aggressive**

About half way between Moderate and Aggressive.

☐ **e. Moderately Conservative**

About half way between Moderate and Conservative.

8. Based upon the above information how would you like your portfolio to be allocated among the three major risk categories?

___ %	1. High risk (U.S. Stocks, Foreign Stocks and Natural Resources)
___ %	2. Moderate risk (bonds)
___ %	3. Low risk (cash and cash equivalents: CD, Stable Value Fund, Money Market, etc.)
100%	Total

Client name: \_\_\_\_\_

Date: \_\_\_\_\_