

Investing: A Risky Business?

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Dynamic Investment Club

Topics

- The balance between risk and reward
- Measures of market risk
- Diversification & portfolio asset allocation
- Closing thoughts
- Questions

Risks in Daily Life

- Risk is the probability of an event occurring times the consequence if it does

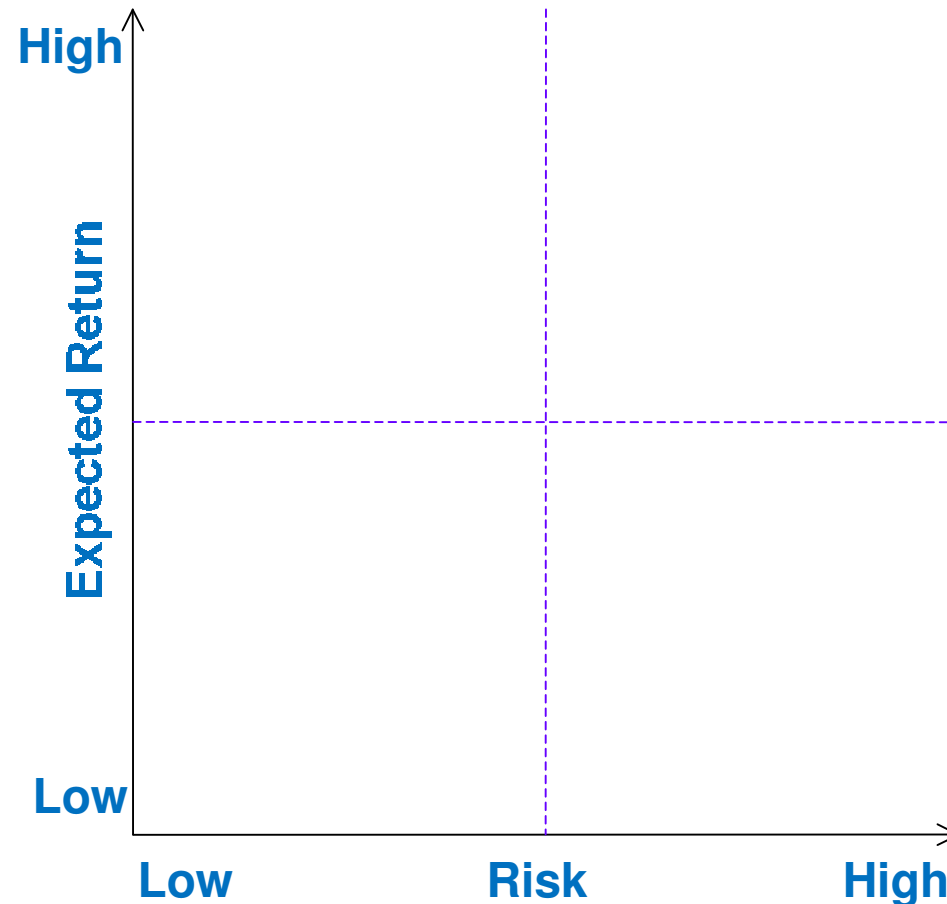
Activity	Average Annual Risk of Death
Maternal death in pregnancy	1 in 8,200 maternities
Rock climbing	1 in 320,000 climbs
Rail travel accidents	1 in 43,000,000 passenger journeys
Aircraft accident	1 in 125,000,000 passenger journeys

Source: Health and Safety Executive



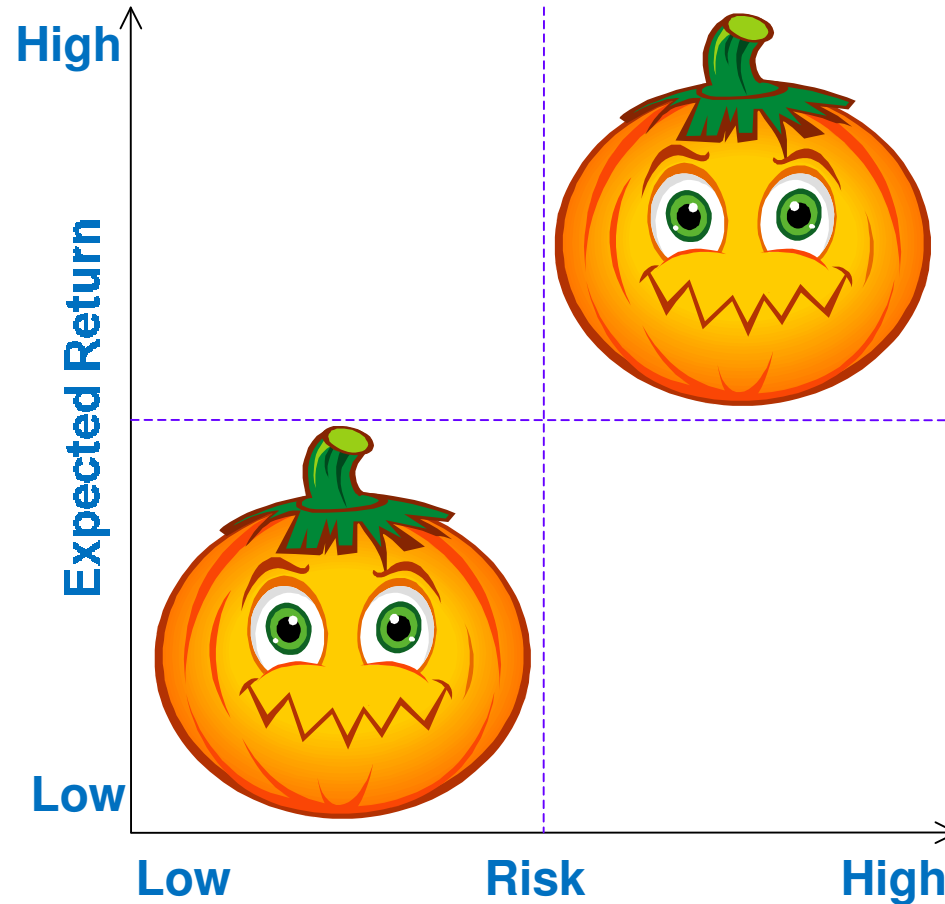
Risk & Reward for Investors

- What is your expected return?
- What level of risk will you accept to achieve it?



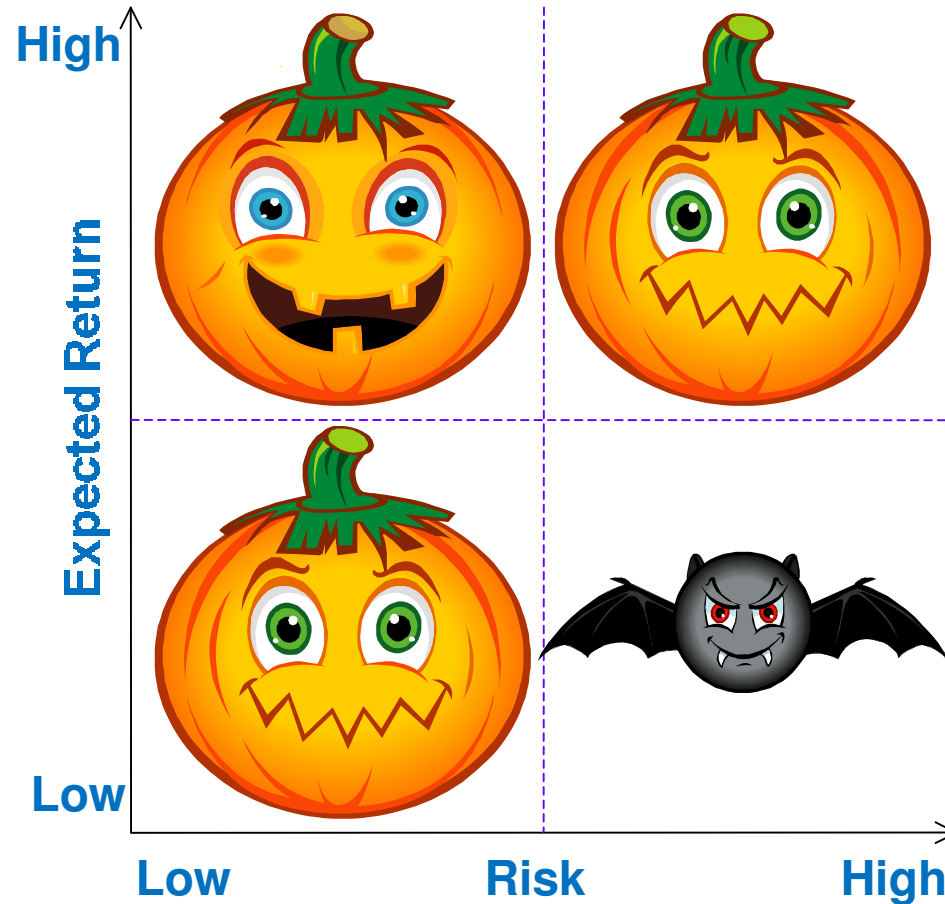
Balancing Risk & Reward

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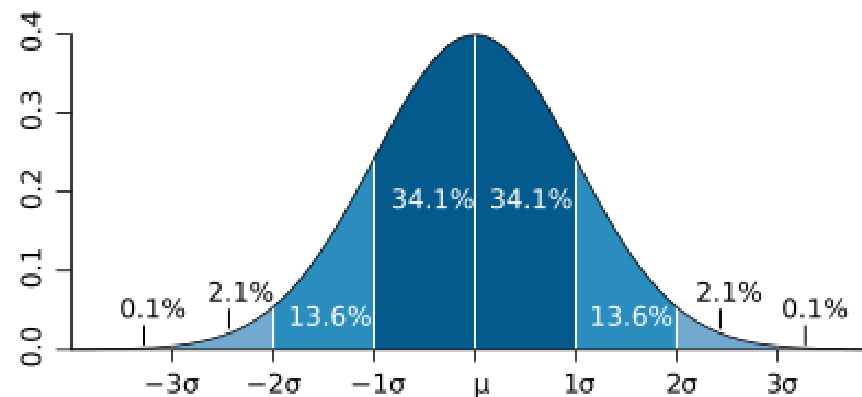
Balancing Risk & Reward

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Measures of Risk

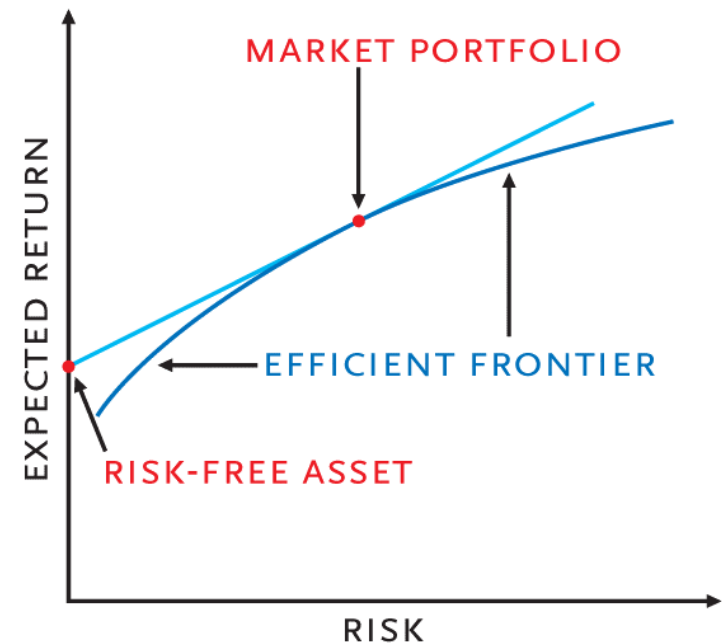
- Different measures based on volatility:
 - Beta. Greater than one when a stock is more volatile than the market
 - Standard Deviation for the spread of expected returns about the mean
 - But large movements are more common in practice



The three sigma
or 68-95-99.7 rule

Modern Portfolio Theory

- Modern Portfolio Theory seeks to maximise return and minimise risk
 - It can decrease risk without affecting return
 - Make risk and std deviation as small as possible
 - Needs uncorrelated assets
 - The efficient frontier



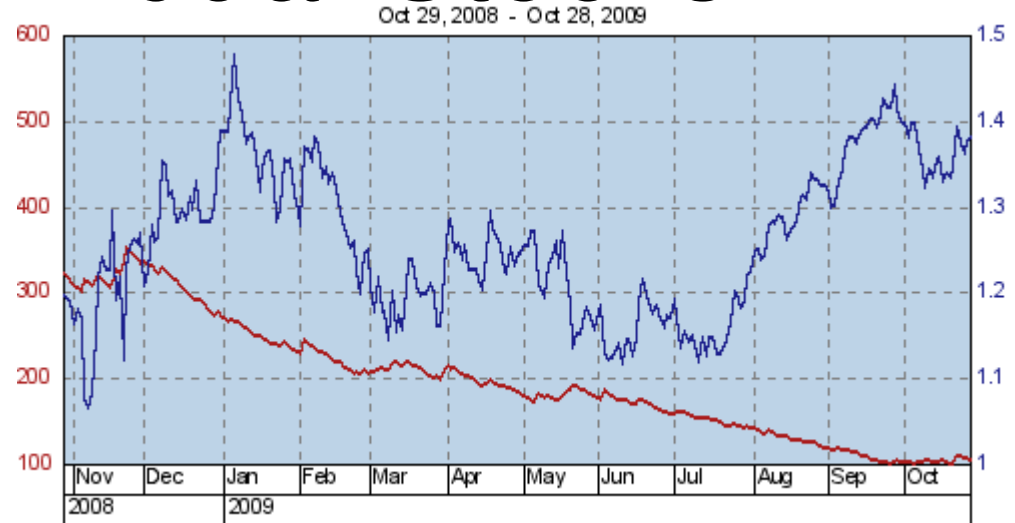
RiskGrade Measures

- RiskGrades are another way to compare investment risk across asset classes, regions & currencies
 - A measure of price volatility to help investors better understand their market risk
 - They can range from 0 to well over 1000
 - See: <http://www.riskgrades.com/>



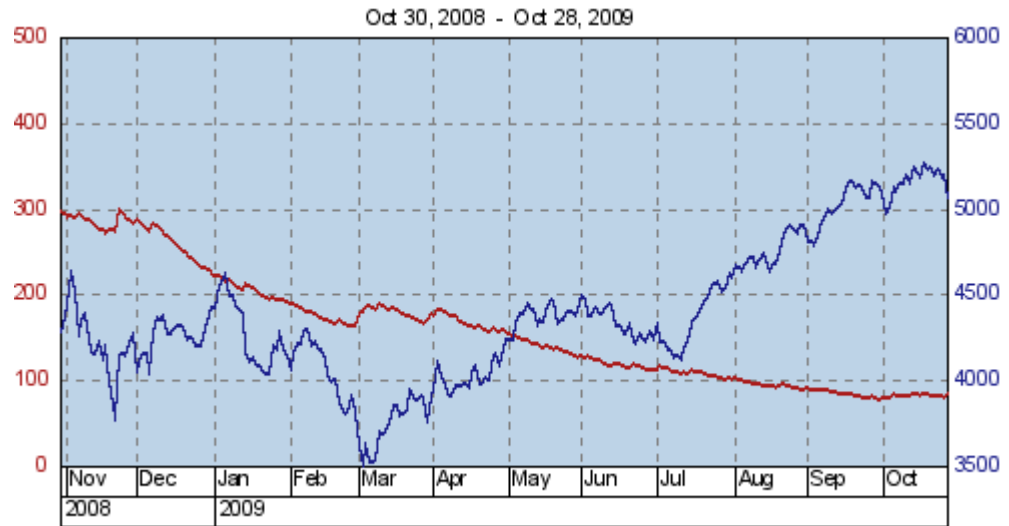
Comparing Individual Stocks

- Vodafone (1 yr)
 - RiskGrade: 108
 - Close: 138p
 - Range: 107-148p
- ReneSola (1 yr)
 - RiskGrade: 340
 - Close: 111p
 - Range: 77-279p



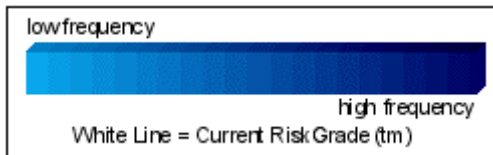
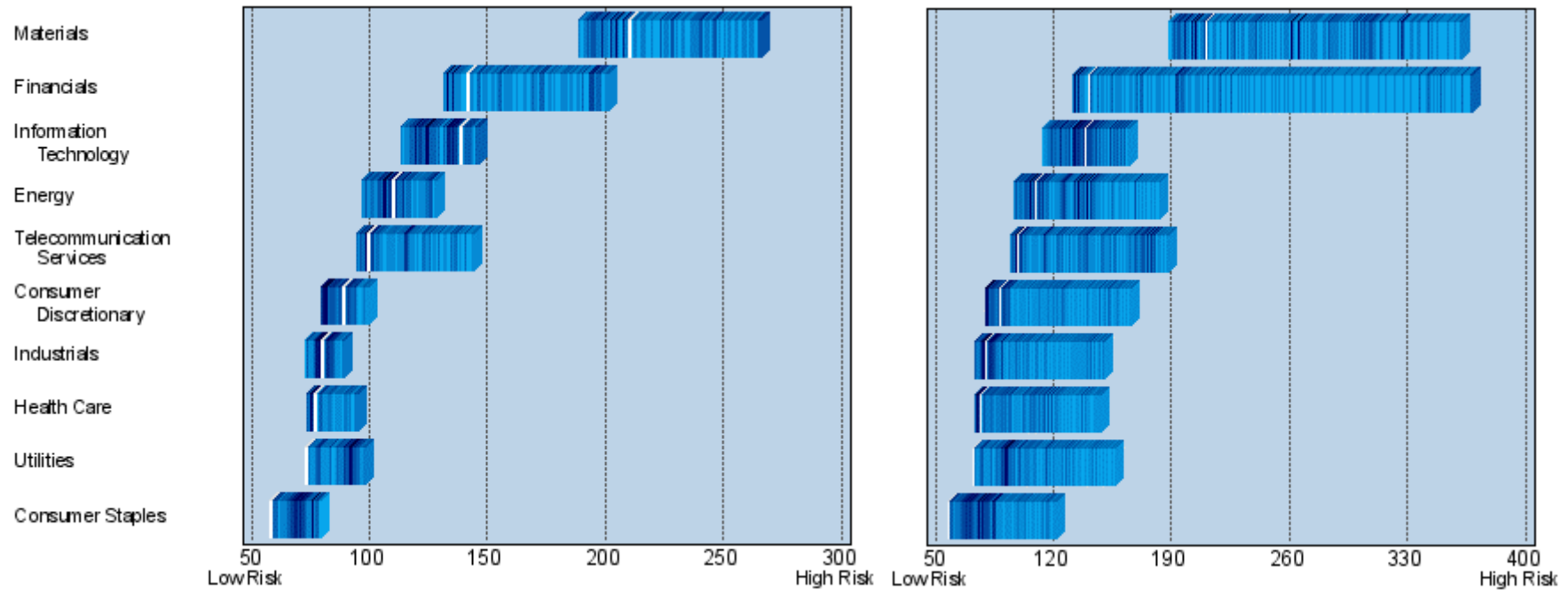
Monitoring Market Indices

- FTSE-100 (1 yr)
 - RiskGrade: 87
 - Close: 5080.42
 - Range: 3512.09 to 5281.54



UK Sector Spotlight

- Distribution of sector RiskGrades over time

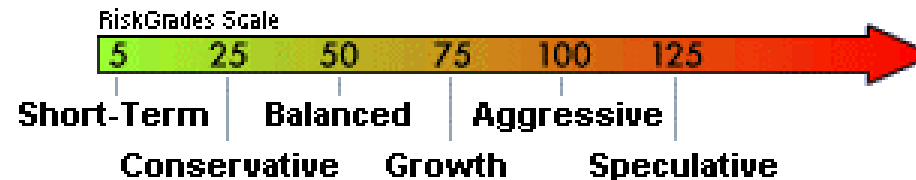


3 months to
29 Oct 09

6 months to
29 Oct 09

Establishing Your Attitude to Risk

- The Risk Profile Quiz uses five questions to build a portfolio with an allocation mix that meets expectations of risk and return
 - Balance between stocks, bonds and cash
 - Stocks allocated to large cap, growth and international equity
 - You screen the market for suitable assets



The Merits of Diversification

“There never were, in the world, two opinions alike, no more than two hairs, or two grains; the most universal quality is diversity.”

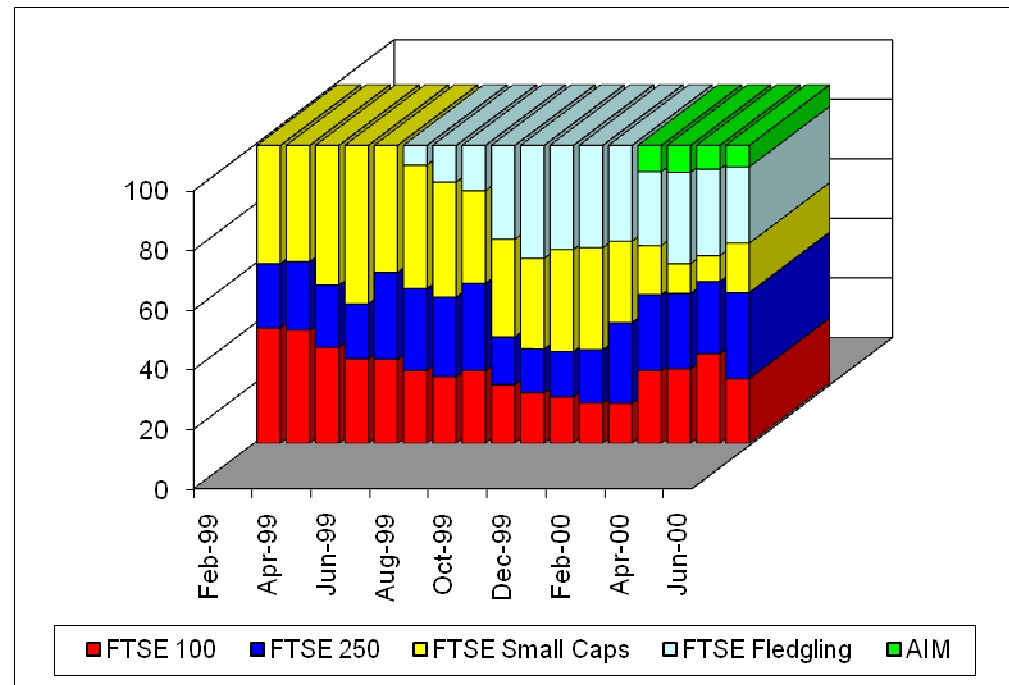
MONTAIGNE, *Essays*

Different Ways to Diversify

- Asset class (stocks, bonds, cash, commodities)
 - Made accessible through trusts, ETFs and ETCs
- Number of holdings
 - David Berger & Jim Slater suggest 8-15 shares
- Company size by market capitalisation
- Sector (business vs. characteristics)
- Market (UK, Europe, US, Emerging...)

Striking a Dynamic Balance

- Core of large caps and mid caps
- The weighting of the very smallest companies increased and matched the 1999 Q4 rally in this market

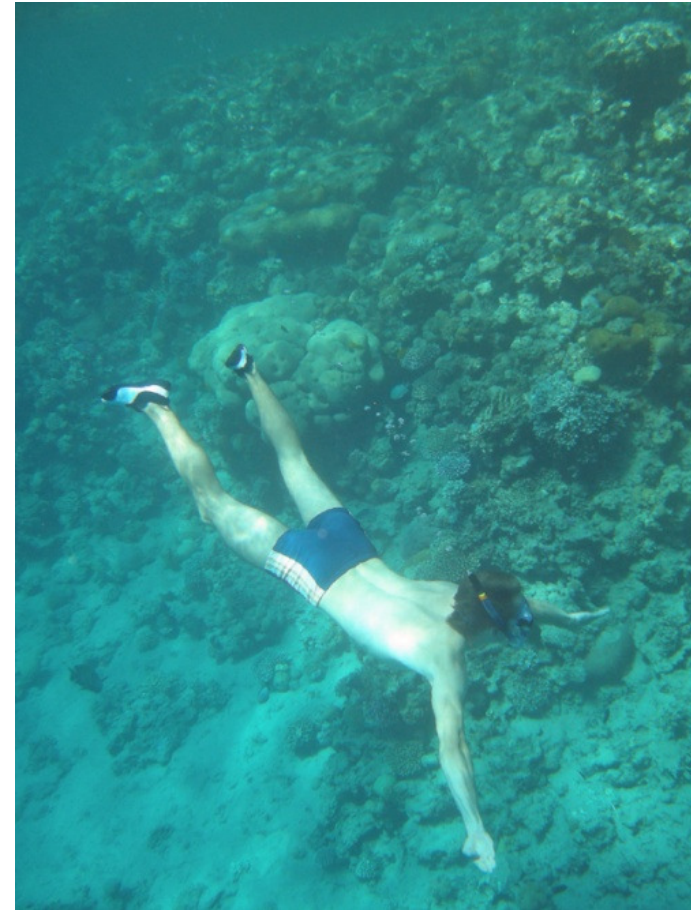


Monthly Percentage Weighting
by Company Size

Summary

- Aim to build a portfolio that strikes a dynamic balance between risk and reward that is right for you
- Combine top-down asset allocation with bottom-up stock picking
 - Blend fundamental & technical analysis
- Diversification can help you to spread risk

Questions...



Investing is about being prepared so that you will find pearls

National Investment Club Conference 2009

Why Elephants Don't Gallop...



National Investment Club Conference 2009