KEMPER CAPITAL MANAGEMENT LLC

Advisor Views

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A feature from **Kemper Capital Management LLC**, *Advisor Views* offers timely investment news and market updates designed to keep you informed, while enhancing your overall investment experience.

Buy Risk, Not Return

You can't see it, hear it, or feel it. When markets are going up, you don't know it's there. It is known as risk, and when markets come crashing down, it usually rears its ugly head. So why would anyone want to buy something that we all have been reminded to avoid? After all, risk has a pretty bad reputation as of late. Over the past few years, a few financial products that were billed as having little to no risk instead had substantial downside implications. For years, investors have struggled with the theory that risk and return are related. In truth, risk is one of the only components of investing that investors can control. With that in mind, let's explore if it's not more reliable and sustainable to base your investment decisions on the idea that risk, not return, is a better measure to focus on.

The problem with buying or chasing returns is simple. Doing so forces investors to discount all of their emotional and behavioral characteristics. Double digit returns look and feel great. Double digit standard deviation for many investors, does not! Think of standard deviation as a measuring stick for risk, or better yet anxiety. The higher it goes, the higher your blood pressure rises during times of investment volatility. The decision to buy an investment solely based on return is akin to buying a 20-year-old used car from a skid row dealership without test driving it. Most rational individuals would never do this. Instead, executing a thorough examination of the car's vitals would be the best course of action to follow. If the individual is still comfortable with taking the risk of potentially owning a lemon, then so be it. At least they evaluated the consequences.

What is your risk tolerance? It's a tough question, so let's be direct and eliminate any confusion about what we're really asking. How much are you willing to lose? Candidly, when it comes to evaluating risk tolerance, this is the information that investors are really searching for. The decision is paramount because risk is a major component of the financial planning process is predicated on the amount of risk that you as an investor, can stomach. It is equally as important to evaluate your "risk temperature" throughout the different phases of life. A worriless, brash 25-year-old, may not have the same tolerance as a responsible, seasoned 60-year-old. It's not an adrenaline- driven, "lay it all on the line" mentality that should be used to make this decision. Rather, it requires a rational, balanced, level-headed approach to evaluate the emotional impact of risk.

THE POWER OF PASSIVE FOR YOU

In the world of finance there are few things that can be reasonably controlled. The idea is that you should control what you can. Cost awareness has forever been, and continues to be, one of the primary tenets that successful, passive investors adhere to. In certain instances, accommodations can be made for the various tax consequences that many of us have to contend with. Most importantly, risk– a key element to success –can and should be controlled. Investors never do themselves any favors by attempting to absorb more than they can handle.

Buying risk means taking on as much of it as you can sleep with at night. A prudent investor is likely best served by assuming a comfortable level of risk rather than pursing a rate of return that carries more risk than he or she can handle. Simply put: you should only bite off as much as you can chew. As your appetite for risk increases, so should the expectation for greater returns.