The Stan Clark Financial Team's

PERSPECTIVES

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Asset allocation

Asset Allocation: Finding your comfort level when stocks fluctuate

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We've been discussing the topic of asset allocation – the mix between equities and fixed income – for some months. We've learned that the risks of each asset class change according to the length of time you invest. Last month, we examined the unique way that the Stan Clark Financial Team looks at the timing of your needs to figure out the best mix for you.

In this issue, we'll talk about how we consider your comfort level with stock market fluctuations in order to find the right mix for you.

We know that markets will always be volatile. Understanding your comfort level with fluctuations will help ensure you have a mix that allows you to weather the downtimes. We also take care to avoid setting a mix that will cause you to worry.

To assess your comfort level with fluctuations, we take you through a series of questions. Although your personal comfort level is subjective, we try to make it objective by using a clear process. All of your answers are scored. We use an average of those responses to determine your overall tolerance to volatility.

The questions are divided into six parts:

The first three parts are simple rules-of-thumb. Although everyone is different, we can categorize them into general groups. For example, people in their 30s would typically have a higher allocation to equities than people in their 70s. Another example: People more interested in high long-term returns would have a higher equity mix. People who prefer to avoid short-term price swings would typically want less in equities.

The next three parts look more in-depth at the three dimensions of volatility tolerance: 1) *risk behaviour*, 2) *your attitude towards volatility*, and 3) *your financial capacity to withstand fluctuation.*

1. The first of these sections, risk behaviour, consists of a series of questions about different areas of your life. For example, do you like to take chances? Have you ever borrowed to invest? People who like to take chances will usually be more comfortable with the fluctuations associated with equities.

2. The next section evaluates your attitude towards fluctuations in your portfolio – and the trade-off between risk and return. For instance, are you willing to accept higher than minimum risk for slightly higher returns? Or, do you prefer your portfolio to be very safe, not risking any principal in the short-term, even though this may result in low long-term returns? People with an accepting attitude toward volatility with equities can have more of their portfolio invested as such.

3. The last section examines your financial ability to withstand fluctuations in your investment portfolio. For example, would you have enough income to cover an unanticipated expense, or would you need to dip into your long-term investments? People who have a greater financial capacity to withstand fluctuations tend to have more in equities.

Each of these six sections provides us with a different estimate of the percentage of equities you could best tolerate. We then average all of these to come up with an overall volatility tolerance number.

The next step is to compare this to the best mix determined by your financial needs – as we discussed last month – to come up with an overall Equity Target. We'll talk about this in our next issue.

Sylvia Ellis is the Senior Estate Planning Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Sylvia provides support to the team in projecting and planning client financial affairs.

To learn more about CIBC Wood Gundy, the Stan Clark Financial Team and the many ways we can help manage your wealth, please contact us by phone or by email as listed below.

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