

## Managing the Market's Risky Business

**E**ffective diversification means more than just holding a large number of accounts or securities. It also calls for efficient, low-cost exposure to a variety of capital markets from around the globe. Let's, expand on the benefits of diversification, beginning with its ability to help you better manage investment risks.

### There's Risk, and Then There's Risk

Before we even have words to describe it, most of us learn about life's general risks when we tumble into the coffee table or reach for that pretty cat's tail. Investment risks aren't as straightforward. It's important to know that there are two distinct kinds of risks: **avoidable concentrated risks** and **unavoidable market risks**.

### Avoidable Concentrated Risks

Concentrated risks are the ones that wreak targeted havoc on particular stocks, bonds or sectors. Even in a bull market, one company can experience an industrial accident, causing its stock to plummet. A municipality can default on a bond even when the wider economy is thriving. A natural disaster can strike an industry or region while the rest of the world thrives.

In the science of investing, concentrated risks are considered avoidable. Bad luck still happens, but you can dramatically minimize its impact on your investments by diversifying your holdings widely and globally, as we have described in the past. When you are well diversified and one of your holdings is affected by a concentrated risk, you are much better

positioned to offset the damage done with plenty of other unaffected holdings.

### Unavoidable Market Risks

If concentrated risks are like bolts of lightning, market risks are encompassing downpours in which everyone gets wet. They are the persistent risks that apply to large swaths of the market. At their highest level, market risks are those you face by investing in capital markets in any way, shape or form. If you stuff your cash in a safety deposit box, it will still be there the next time you visit it. (It may be worth less due to inflation, but that's a different risk, for discussion on a different day.) Invest in the market and, presto, you're exposed to market risk.

### Risks and Expected Rewards

Harkening back to our past conversations on group intelligence, the market as a whole knows the differences between avoidable and unavoidable investment risks. Heeding this wisdom guides us in how to manage our own investing with a sensible, evidence-based approach.

**Managing concentrated risks** – If you try to beat the market by chasing particular stocks or sectors, you are exposing yourself to higher

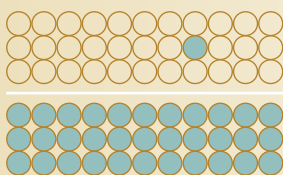
concentrated risks that could have been avoided with diversification. As such, you cannot expect to be consistently rewarded with premium returns for taking on concentrated risks.

**Managing market risks** – Every investor faces market risks that cannot be "diversified away." Those who stay invested when market risks are on the rise can expect to eventually be compensated for their steely resolve with higher returns. But they also face higher odds that results may deviate from expectations, especially in the near-term. That's why you want to take on as much, but no more market risk than is personally necessary. Diversification becomes a "dial" for reflecting the right volume of market-risk exposure for your individual goals.

### Your Take-Home

Whether we're talking about concentrated risks or market risks, diversification plays a key role. Diversification is vital for avoiding concentrated risks. In managing market risks, it helps you adjust your desired risk exposure to reflect your own purposes. It also helps minimize the total risk you must accept as you seek to maximize expected returns. We believe that it is important for you to manage your investment risks and that you will benefit by implementing your investment strategy with a broadly diversified investment portfolio.

*David Bromelkamp*  
President and CEO



Concentrating in one stock exposes you to unnecessary risks. While diversification does not eliminate the risk of market loss, it does reduce the impact of any one company's performance on your wealth.

## NEW EMPLOYEE SPOTLIGHT: Abbey Spoo



**Role at Allodium:** Senior Investment Consultant

**Joined firm on:** July 20, 2015

**University attended:** College of Saint Benedict

**Hometown:** Baldwin, WI

**Favorite movie:** *The Big Lebowski*

**Favorite book:** *Into Thin Air*

**Favorite TV show:** Anything on the Food Network

**Favorite musician:** Brandi Carlile

**Favorite food(s):** Vegetables

**Favorite news source:** *Wall Street Journal*

**Favorite Twin Cities neighborhood:** North Loop

**Favorite activity:** Running

**What I'm most thankful for:** My amazing friends and family

## Headlines

- Allodium hosted its annual client appreciation event in August with a boat cruise on the Mississippi River
- On October 27th, Allodium will host its fall education event – look for more details in the mail
- Eric Hutchens became a NAPFA Registered Financial Advisor
- Anne Ward was quoted in *US News* in an August article about improving finances during retirement
- Allodium was pleased to welcome two new clients in the second quarter of 2015
- Our office will be closed on Thursday, November 26th and Friday, November 27th for Thanksgiving

**Note:** To find out more about Allodium's breaking news, please visit the blog on our website [www.aicria.com](http://www.aicria.com).

# SPOTLIGHT

# NEWS

## WE APPRECIATE YOUR INTRODUCTIONS

To optimize our objectivity and avoid conflicts of interest, we are a fee-only registered investment advisor that is completely independent from banks, brokerage firms and other financial product providers.

If you know someone who may be looking for this type of objective investment advice, please contact Dave Bromelkamp at 612-230-3702 or [dbromelkamp@aicria.com](mailto:dbromelkamp@aicria.com) to arrange a friendly, no-obligation introduction.

*Steward* is published quarterly by Allodium Investment Consultants. Please contact Matt Hansen at 612-230-3704 or [mhansen@aicria.com](mailto:mhansen@aicria.com) if you have any comments about this publication or wish to be added to or removed from our mailing list.



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