

## Diversification 101

Portfolio volatility is at an all-time high. Are there some basic elements to your portfolio that seem to be missing?

Diversification is important. It's tough to understand why diversification works when there are some funds that excel over time, and others that may lag.

On a large scale, investors should first avoid investing in the 'hot dot' of the present time. This means, that buying last years winning investment management strategy may not be the key to long-term success. The opposite is also true. The thought that purchasing a strategy or fund that didn't fare well recently seems counter intuitive to many people.

Stocks come in many formats: Large, Mid and Small. International stocks have their own category, and are also excellent diversifiers for portfolio management purposes. It's also important to understand the differences between value and growth. They are investment styles that have benefits in certain market environments, and carry their own risks. It's not that you need to make a choice between all equity asset classes, but rather, it's important to include most (if not all) within a properly diversified portfolio.

Bonds come in their own shapes and sizes also. They are long-term, intermediate term, and short-term. Generally, you break out bond classifications based on the lengths of their maturities. You can continue classifying bonds by their issuer: Government, Corporate and International. Each issuer will have their own risks affiliated with their bond, and it's important to understand why you would have one bond versus another.

Portfolio diversification isn't an assurance against portfolio losses. However, it is important to understand that diversification, in our book, provides 'insurance' against one asset class dominating the returns, both good and bad, within any portfolio.

The past 10 years have given us a glimpse into the inner workings of more than just one period of investment turmoil. In the late 1990's, investors categorically found themselves gravitating toward technology portfolios with a significant portion of their portfolios. Owning a few value stocks in your portfolio during that time in history would have helped keep your portfolio on an even keel despite the heavy losses in the technology market.

Adding bonds to any portfolio can provide a smoother investment return for investors. Bonds have the ability to reduce the volatility, and enhance the current income of a portfolio. Bonds and stocks carry their own unique risks, and each should be weighed in conjunction with your risk profile and time horizon. Diversification is an important part of any proper portfolio construction, and shouldn't be overlooked.

Human nature can cause us to chase past investment returns as if they are gospel. A rebalancing strategy, can help offset the desire to 'keep our winners, sell our losers' mentality that keeps us from taking profits and buying low. Diversification is a time-tested approach to prudent investment management.

Bonds have the ability to reduce volatility, and enhance the current income of a portfolio. Bonds and stocks carry their own unique risks, and each should be weighed in conjunction with your risk profile and time horizon.

