

BUILDING BLOCKS FOR RETIREMENT

Investment Strategy

An Investor's All-Season Strategy

Quality does count. Stocks of companies with strong earnings, bonds from issuers with excellent credit ratings, and mutual funds with consistent management have often been strong performers. But even high performers sometimes stumble unexpectedly, resulting in losses to investors. Investment risk never completely goes away, regardless of a portfolio's quality.

Market Uncertainty

Market history includes many years when the returns of stocks as a class have been higher than bond returns. It also includes other years, such as 2000, 2001, 2002, 2008, and 2011 when bonds outperformed stocks. And it even includes some years, most recently 1994, when cash equivalents beat both stocks and bonds. Going forward, avoiding a poor performing asset class (or picking a winner) is always far from certain.



Countering Market Risk

Fortunately, a diversification strategy can help investors counter market risk under varying economic conditions. A diversified portfolio includes a variety of different investments that are unlikely to gain or lose market value at the same time — or to the same extent. If you own a carefully chosen mix of investments in asset classes that tend to move in different directions — or, at least, are not too closely correlated — you gain a measure of protection against performance variations and are not dependent on the unpredictable performance of any single asset class. The overall result of diversifying may be the achievement of more consistent, long-term performance than would be accomplished with a single-class portfolio — and with less risk.

Diversification does not guarantee profits or necessarily prevent losses. And, if one asset class within a diversified portfolio advances more strongly than the others, some return is sacrificed because the portfolio is not 100% invested in the advancing class. At the same time, the potential for loss is lower than it would be if the entire portfolio were invested in an asset class that significantly underperforms.

Your Asset Allocation

Diversifying within a broad asset class is also an effective strategy for controlling portfolio risk. In a portfolio of 100 stocks, for example, a sharp drop in the value of one or two



stocks would have much less effect overall than the same decline in a portfolio of just 10 stocks. A portfolio of U.S. and foreign stocks may be less affected by losses in the U.S. market than an all-U.S. stock portfolio. And a portfolio that contains stocks of large, mid-size, and small companies is more diversified than one concentrated in a single capitalization range.

A well-planned, diversified portfolio doesn't necessarily contain assets evenly divided among investment classes. An equal allocation might not suit your needs because of differences among the potential returns and the overall risks of the asset classes. A very small allocation to stocks, for example, might unacceptably reduce your portfolio's potential returns, while a very large stock allocation might unacceptably raise overall volatility. A better choice: Create a well diversified portfolio with an asset allocation in keeping with your individual risk tolerance and goals that balances market risk against the potential for long-term growth.

Please call us if you want to know more about building a portfolio that reflects your objectives and individual risk preferences.

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