Conejo Valley Estate Planning Council

How to Take Risk

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Roadmap

- Traditional definition of risk
- A different way to look at risk
- Lessons from history
- How to take risk

The traditional framework for risk….

The allure of financial models

- Capital Asset Pricing Model
- Sharpe Ratio
- Information Ratio

Reminder from an all-time great

"Investing is foregoing consumption now in order to… consume more at a later date."

- Warren E. Buffett

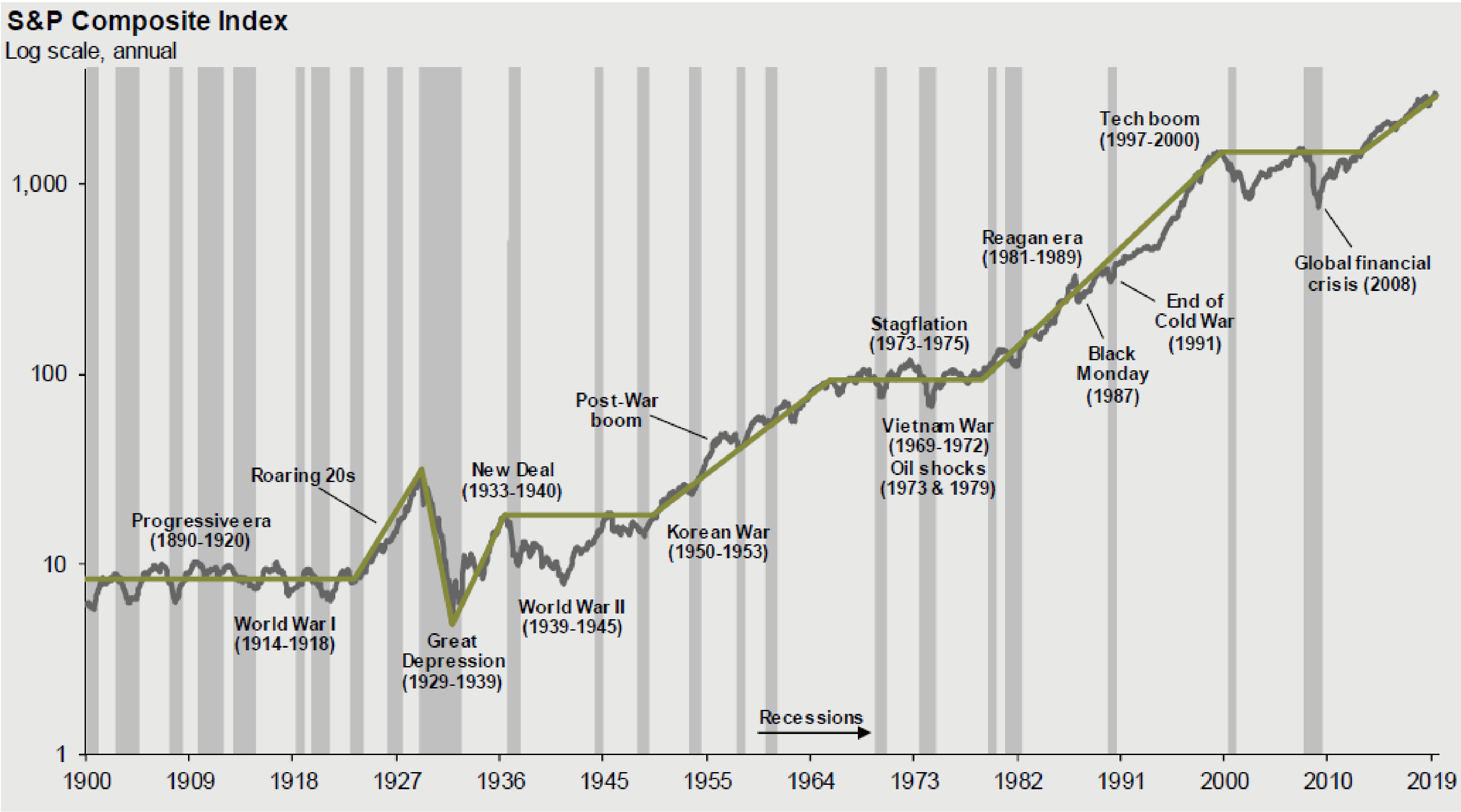
Risk re-defined

Risk = Size of Loss x Length of Time

Risk re-defined

Shallow Risk	Short-lived loss Deprives you of sleep
Deep Risk	Permanent loss of wealth Deprives you of sustenance

History of the U.S. Stock Market

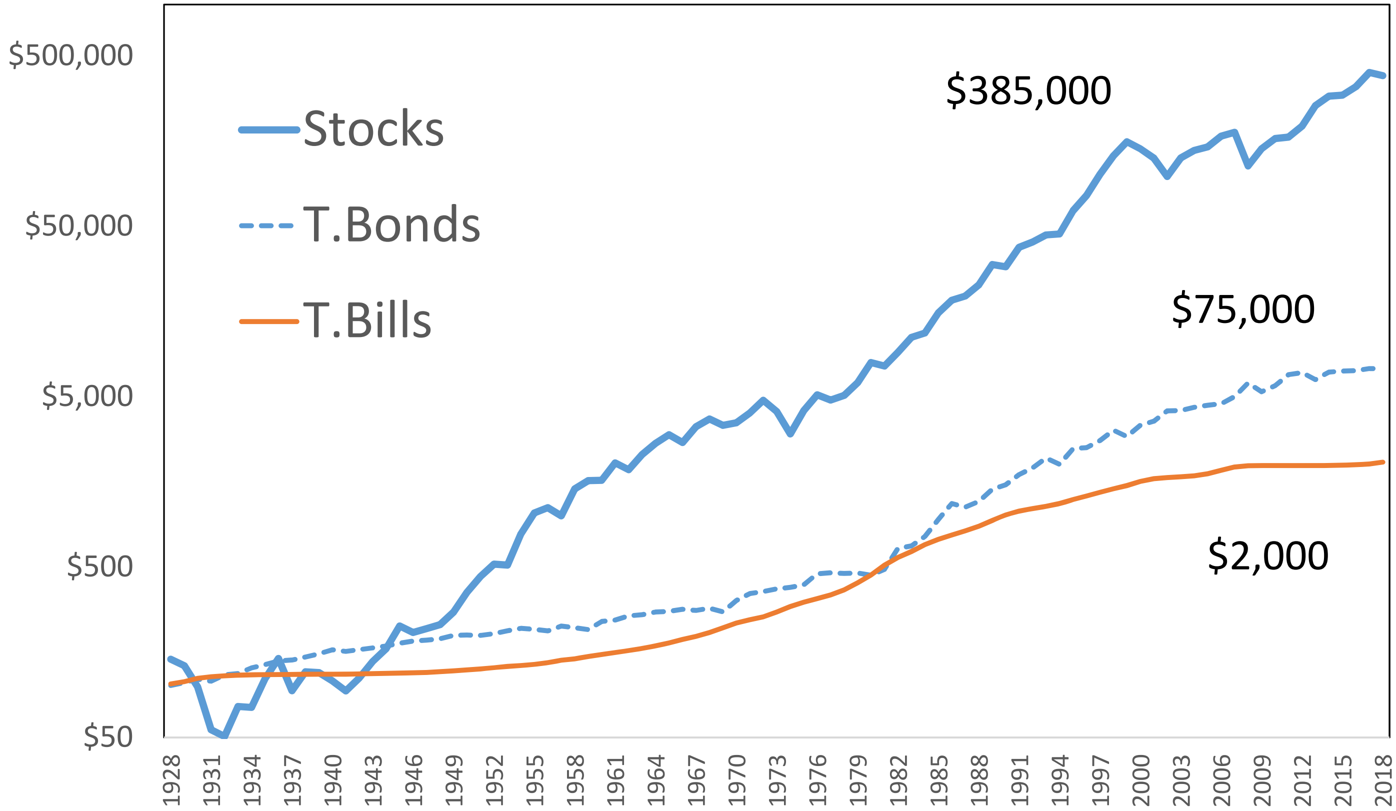


Shallow risk

1. We’ve recovered from most drawdowns quickly

2. Unlikely to suffer another Great Depression, decades long natural resource shocks.

What if you invested $100 in 1927?

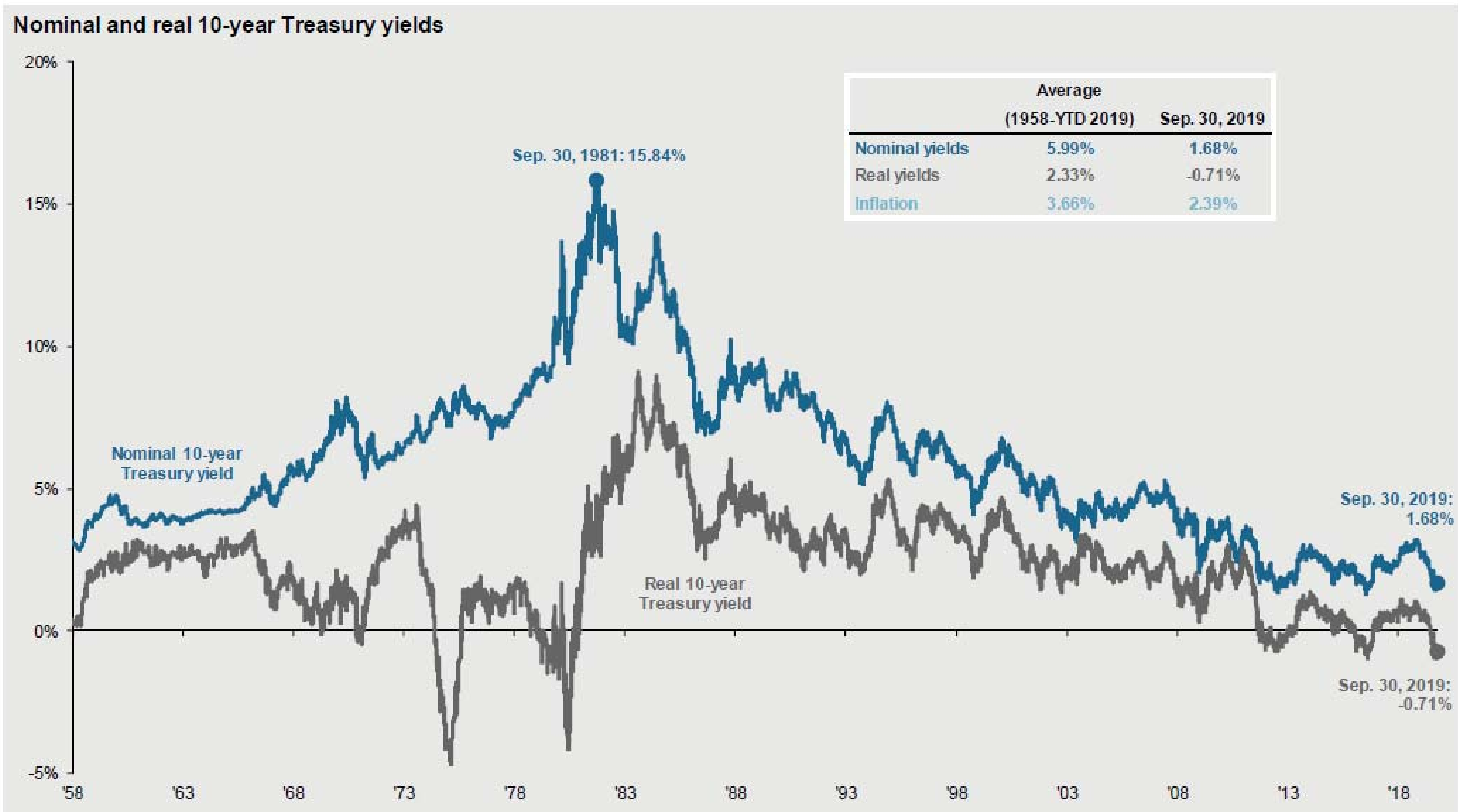


Deep risk

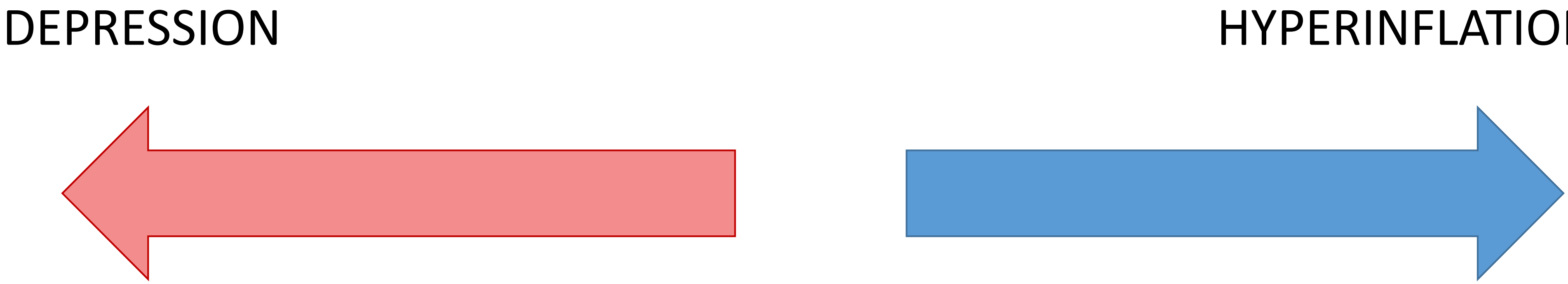
1. On purchasing power, bonds are riskier than stocks.

2. Permanent loss of wealth – hence “deep” loss.

Real yields on bonds



The Economic Cycle



Deflationary cycle

DEPRESSION

<u>What works?</u>

Own bonds
Accumulate hard assets, collectibles
Deleverage

Inflationary cycle

HYPERINFLATION

<u>What works?</u>

Own stocks
Own income-producing assets
Borrow to buy assets

How to Take Risk


What Investors Listen to Since 2008
ANSWERS
Macro doom BS
Rational
Optimism
GOCOMICS.COM/NONSEQUITUR