



Investing | *Diversification*

WOULD AN EGG CARTON BE BETTER?

Everybody knows you're not supposed to put all your eggs in one basket. So should you put them in an egg carton instead? If you're concerned about protecting actual eggs, an egg carton is better than a basket. But this old saying isn't about eggs.

Spread the Risk

It's about diversifying* your investments. Diversification is the basic investment strategy of choosing a mix of different investments to help manage risk. Putting your eggs (money) in more than one basket (investment) reduces the chances that they'll all break (lose money) if the basket falls (market drops). When you diversify, if one of your investments doesn't do well, you have others that may perform better, boosting your overall return.

Automatic Diversification

The funds or portfolios in your retirement plan offer automatic diversification because each fund may hold hundreds of individual investments. However, unless you select a fund or portfolio that's specifically designed to be an all-in-one investment (and not all plans offer such options), holding just one fund isn't likely to offer enough diversification. So what other levels of diversification are there to consider?

Asset Classes

The various asset classes — stocks, bonds, and cash alternatives** — may react differently to changing economic conditions. So choosing a variety of funds or portfolios that invest in different asset classes can help you weather different conditions.

Stocks, bonds, and cash might be the asset classes you're most familiar with, but there are others — real estate, for example. Different asset classes offer different degrees of risk and reward and respond differently to what's happening with the economy. Your goal should be to choose an asset mix that will help keep your portfolio afloat no matter what the markets are doing.

Industries and Sectors

A market sector is an area of the economy that includes companies or industries offering the same or related products or services. Investing across various market sectors can help diversify your portfolio. Cyclical investments, such as housing, transportation, financial, and technology stocks, tend to be sensitive to how the economy behaves and have the potential for significant gains when the economy is thriving. Defensive investments come from industries, including utilities, food, and other staples, where consumer demand tends to remain stable, even in a slow economy. Including a mix of cyclical and defensive stocks from a variety of market sectors can help diversify your portfolio.

All Over the Map

Another way to diversify is to hold investments from different countries and regions of the world, including both established and developing economies. Gaining exposure to a variety of economic circumstances that may differ from those in the U.S. can add another layer of diversification to your portfolio.

Creating a well-diversified portfolio takes a comprehensive knowledge of investments and the expertise to choose those that fit your goals, time horizon, and risk tolerance. Your financial professional can help.

How Many?

Should you invest in every fund or portfolio your plan offers? Probably not. Some of your plan's investments may be very similar, so you essentially would be duplicating investments if you chose every one. The benefit of diversification can be diminished if your portfolio includes too many similar investments.

Suppose, for example, that you invest in several funds without carefully considering the funds' holdings. Because you're investing in funds rather than individual securities — and in more than one fund instead of just one — you may think you're managing risk while positioning yourself for potential growth. But, in reality, you may not be achieving your goal. A strong gain in one fund will have little impact if the fund comprises only a small portion of your overall portfolio.

A different problem could arise if the majority of your funds invest in the same type of securities — stocks of large U.S. companies, for example. In this case, your "diversified" portfolio will be subject to considerable risk of loss during periods when the market for large company stocks falls.

When planning your diversification strategy, it's important to avoid duplication and to be sure your portfolio includes not only different securities but also different types of securities. Take time to investigate your options and choose enough investments to have well-diversified mix.

**Diversification does not ensure a profit or protect against loss in a declining market.*

***Note that cash alternative investments may not be federally guaranteed or insured and that it is possible to lose money by investing in cash alternatives. Returns on cash alternative investments may not keep pace with inflation, so you could lose purchasing power.*

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