

Understanding Your Risk Tolerance

A Guide to Smarter Investing



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Investing can feel overwhelming, especially when it comes to understanding how much risk you're comfortable taking. Some people enjoy the thrill of market swings, while others prefer a more steady and predictable approach. Knowing your risk tolerance helps you build a portfolio that feels right for you, so you can stay invested with confidence and peace of mind.

Here's how to figure out where you stand and what works best for you:

1 Define Your Investment Goals

What are you investing for? The answer shapes your approach to risk.

- **Short-term goals** (e.g., buying a house in 5 years):
You may need to prioritise capital preservation and opt for lower-risk investments, as there's less time to recover from market downturns.
- **Long-term goals** (e.g., retirement in 20+ years):
With a longer time horizon, you may have the flexibility to take on more risk, allowing you to benefit from market growth over time.

Being clear about your objectives helps you determine whether you can afford short-term volatility or need a steadier path.

2 Assess Your Time Horizon

Your investment timeline plays a crucial role in your risk strategy.

- **Longer time horizon:**
If you have decades before needing your funds, short-term fluctuations matter less. Equities and other growth assets, while volatile, can offer higher returns over time.
- **Shorter time horizon:**
If you need access to your funds within a few years, a more conservative portfolio may be prudent, reducing exposure to market downturns that could impact your plans.

3 Evaluate Your Financial Stability

Risk tolerance isn't just about how much risk you're willing to take—it's also about how much you can take. This would largely depend on your current financial position, earnings prospects as well as future obligations.

Consider these factors:

- **Income stability:**
A steady income allows for greater risk-taking since you can continue investing through market cycles.
 - **Savings and emergency fund:**
A strong financial cushion lets you weather downturns without selling investments at a loss.
 - **Debt levels:**
High debt obligations may limit your ability to take on investment risk, as you need liquidity to manage repayments.
- A young professional with a secure job, minimal debt, and a growing income may have higher risk capacity than someone nearing retirement with fixed expenses and limited future earnings.

4 Understand Your Emotional Response to Risk

Beyond your financial position, your psychological comfort with risk matters. Some investors can stay calm during market declines, while others may panic and sell at the worst time.

Ask yourself:

- **How do I react to market fluctuations?**
- **Would I be comfortable seeing my portfolio temporarily decline by 20%?**
- **Do I tend to make impulsive financial decisions under stress?**

If market volatility keeps you up at night, a more balanced or conservative portfolio might be a better fit. If you can tolerate short-term swings in pursuit of long-term gains, you might opt for a higher allocation to equities.

5 Diversify and Adjust as Needed

It is important to remember that one's risk tolerance isn't fixed. As we progress through each life stage—whether it's a career change, growing family responsibilities, or reaching retirement—your ability to take on risk may change. Major life events, such as an unexpected financial obligation or a shift in income, can also impact how much risk you can afford.

That's why regularly reviewing your portfolio is essential. By adjusting your asset allocation to reflect your current financial situation and long-term objectives, you ensure your investments remain aligned with both your goals and comfort level—keeping you on track toward financial security.

A well-diversified portfolio spreads risk across different asset classes such as stocks, bonds, REITs, and alternative investments. Each asset class plays a distinct role in balancing returns and managing downside risks.

Invest With Confidence

Investing isn't about taking the biggest risks—it's about making decisions that help you reach your goals while staying comfortable with the ups and downs. Take your time to understand what works for you, and don't be afraid to adjust as needed.

Take the first step toward achieving your financial goals. Whether it's saving, investing, or growing your wealth, AHAM Capital is here to support and guide you every step of the way.



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