

Strategies To Mitigate Risk

Key Terms

- **Hedging:** Hedging is a strategy in which you mitigate risk by investing in instruments that are inversely related to each other to reduce risk. For example you may be long a stock in a certain industry and also take a short position to reduce potential losses.
- **FETCH:** This acronym refers to 5 following industries: Financial Services, Energy, Technology, Communications, and Healthcare. Companies within these industries are commonly recognized as core components to the economy and society regardless of the current economic climate.

Avoiding Risk

Risk is impossible to fully eliminate, it can be modeled for and mitigated. The following three strategies, employed separately or all together, can help protect your portfolio from many types of risk.

A sure fire way to completely eliminate risk is to avoid products, companies and industries that engage in blatantly risky operations. Any startup, for example, is a risky investment. Additionally, companies that are in competitive sectors or are reliant on any one product/service can be risky investments. For a portfolio with minimal risk, large cap blue chip stocks may be the way to go. Keep in mind that investing with the goal of avoiding risk may cut you off from opportunities with high returns.

Accepting Risk

Another strategy to mitigate risk in investing is to “Accept” that risk is inevitable, and develop policies to monitor risk. This strategy allows you to partake in more volatile investments, as long as you have a defined method for keeping track of company financials, new product releases, and concerning or promising media reports from or about the company.

Of course, this will not eliminate risk, but it is a more flexible strategy that can reduce risk if properly followed.

Reducing Risk

A tried and true method to reduce risk is to diversify your portfolio. Investing across industries, sectors and different types of assets ensures that you have exposure to all parts of the market. As such, your portfolio will consistently rally in some sectors even if it falls in others.

The Bottom Line

There are a few strategies that can help reduce risk when investing. They can be used individually, but are most effective when mixed together into a larger investing ideology. In the market, high risk stocks often have high returns. It is up to you as an investor to determine your risk appetite, and use these strategies accordingly.