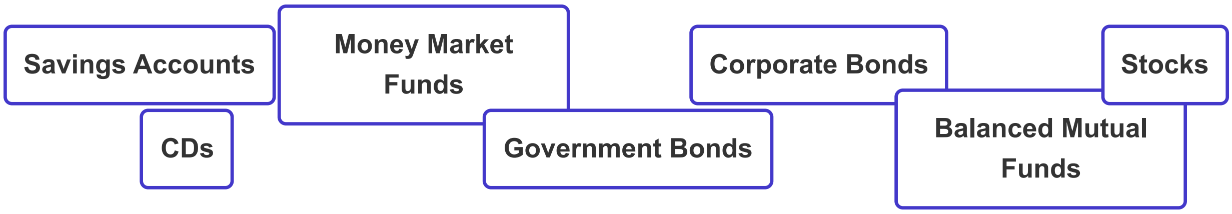
Risk-Return Spectrum

Understanding the Relationship Between Risk and Return in Investment Options

The Risk-Return Relationship

The risk-return spectrum illustrates a fundamental principle in investing: investments with higher potential returns generally come with higher levels of risk. This visual guide helps you understand where different investment options fall on this spectrum.



Lower Risk | Moderate Risk | Higher Risk

Lower Return Potential | Moderate Return Potential | Higher Return Potential

Investment Options Comparison

Investment Option	Risk Level	Potential Return	Liquidity	Time Horizon
Savings Account	Very Low	0.5% - 1%	Very High	Short-term
Certificate of Deposit (CD)	Low	1% - 3%	Low (penalty for early withdrawal)	Short to Medium-term
Money Market Fund	Low	1% - 2%	High	Short-term
Government Bonds	Low to Moderate	2% - 4%	Moderate	Medium-term
Corporate Bonds	Moderate	3% - 6%	Moderate	Medium-term
Balanced Mutual Funds	Moderate	4% - 7%	Moderate to High	Medium to Long-term
Index Funds	Moderate to High	7% - 10%	High	Long-term
Stocks (Individual)	High	Varies (potential for 10%+)	High	Long-term

Investment Option	Risk Level	Potential Return	Liquidity	Time Horizon
Growth Mutual Funds	High	8% - 12%	Moderate to High	Long-term

Note: Return percentages are approximations based on historical data. Actual returns may vary and are not guaranteed. Time horizons are general guidelines: Short-term (0-3 years), Medium-term (3-10 years), Long-term (10+ years).

Key Characteristics by Risk Level

Low Risk Investments

- Principal is generally protected
- Returns are predictable and stable
- Often backed by government guarantees (FDIC)
- May not keep pace with inflation over time
- Best for short-term goals and emergency funds
- Examples: Savings accounts, CDs, Treasury bills

Moderate Risk Investments

- Some potential for principal fluctuation
- Returns can vary but generally moderate
- Usually diversified to manage risk
- May provide some protection against inflation
- Best for medium-term goals
- Examples: Bonds, balanced mutual funds

High Risk Investments

- Significant potential for principal fluctuation
- Returns can be high but also highly variable
- May experience substantial short-term losses
- Historically outpace inflation over long periods
- Best for long-term goals where growth is primary
- Examples: Stocks, growth mutual funds

Matching Investment Options to Financial Goals

Different financial goals require different investment approaches based on time horizon, risk tolerance, and liquidity needs.

Goal Type	Time Horizon	Suggested Investment Vehicles	Rationale
Emergency Fund	Immediate access	Savings Account, Money Market Fund	Highest liquidity and principal protection for unexpected needs
Short-term Goal (e.g., vacation, electronics)	1-3 years	High-yield Savings, CDs, Money Market Funds	Low risk of principal loss with slightly better returns than regular savings
Medium-term Goal (e.g., home down payment, car)	3-10 years	CDs, Government Bonds, Corporate Bonds, Conservative Mutual Funds	Balance between growth potential and reasonable stability
Long-term Goal (e.g., retirement, child's college)	10+ years	Index Funds, Mutual Funds, ETFs, Stocks	Maximum growth potential with time to recover from market fluctuations

Diversification: Managing Risk in Your Investment Strategy

Diversification—spreading investments across different asset classes—is a key strategy for managing risk while seeking reasonable returns. Like not putting all your eggs in one basket, diversification helps protect against significant losses from any single investment.

Diversification Strategies

- **Asset Class Diversification:** Spreading investments across stocks, bonds, cash equivalents, etc.
- **Sector Diversification:** Investing across different industries (technology, healthcare, consumer goods)
- **Geographic Diversification:** Investing in both domestic and international markets
- **Time Horizon Diversification:** Having different investments matched to different time horizons