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Asset Allocation, Risk Tolerance and Shortfall Risk

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Asset allocation is the biggest driver of portfolio performance, particularly over the long-term. Moreover, it also is reflective of an investor's risk tolerance. The recent financial crisis has negatively impacted investment psychology, particularly among younger investors. As a result, the so-called "Generation-Y" has over half of their assets held in cash -- a "non-earning" asset. While this is safe, there is a risk of loss in value, as cash does not even hold up with inflation. In the long-term, such an allocation means a lower retirement balance--i.e., shortfall risk. Thus, these investors have essentially traded one type of risk for another. See article here, Investment News.

Related Chapters: Chapter 02