



PAGE ONE  
Investing in Volatile Times:  
What it Means to Diversify

PAGE TWO  
Financial Planning: Helping  
You Realize Your Goals

PAGE THREE  
Client Workshops in April

PAGE FOUR  
Staff News

# CURRENTS

CLIENT NEWSLETTER

OBRIENMANAGEMENT.COM | SPRING 2008



## INVESTING IN VOLATILE TIMES: WHAT IT MEANS TO DIVERSIFY

By Brandon Auger

With the return of volatility and explicit risk to the financial markets, diversification is becoming even more invaluable to investors. As many know, effective diversification is the most efficient means to reducing risk in a portfolio. While some may define risk as the potential for investment loss and others think of risk as the probability of not meeting financial goals, the investment community defines risk as the volatility of asset prices. The means to risk-reducing, volatility-damping diversification is widely misunderstood and often oversimplified. In this article, we set out to explain the technical intricacies of why diversification works and how it is accomplished.

What does it mean to diversify? When posed this question, many would respond by referring to an old saw: "Don't put all of your eggs in one basket". In a very simple way, this is true. While spreading your assets among more than one investment is a necessary condition of effective diversification, it is far from complete. After all, even when your money is spread across many investments, if each investment is exposed to the same risks, you have not effectively reduced the risk to your portfolio.

There are two principle risks that are of concern to investors: company-specific risk and systematic risk. As its name indicates, company-specific risks include factors that are specific to investing in single companies. An example of such a risk is the possibility that skyrocketing jet fuel prices will drive down the profitability of Southwest Airlines. Such an event would be challenging for the company and for all Southwest Airlines investors who are exposed to this company-specific risk. In addition to company-specific risk factors, investors must be aware of systematic risk factors. Systematic risk can be broadly defined as any risk factors that have an impact on all financial assets. Examples of systematic risk factors include the general level of interest rates, inflation, the stage of economic growth, and the legal/political environment.

So what can be done to diminish risk? Thankfully, there are methods of mitigating each type of risk. Company-specific risks can be completely eliminated by simply investing in many different companies that have different risk exposures. For instance, if you are an investor of Southwest, you may also want to be an investor in Exxon Mobil. The reason for this arrangement is intuitive: rising jet fuel prices will negatively affect an airline while positively affecting an energy company. With a portfolio of many

*Continued on page 2*

FOSTERING TRUST  
BUILDING WEALTH  
EDUCATING CLIENTS

## What it means to diversify, continued

diverse stocks, company-specific risks disappear altogether. The offsetting nature of company-specific risks justifies a very diverse portfolio.

The beauty of diversifying among many companies is that such diversification does not necessarily reduce expected return. After all, the return on Southwest's stock will be identical for a diversified investor and for a non-diversified investor, while the latter will be exposed to far more risk. It is because of this that company-specific risks are not regarded as compensated risks, meaning an investor can not expect that taking on greater degrees of company-specific risk will result in greater returns.

Systematic risks are far more difficult to allay. For instance, we can not reduce the impact that an economic recession would have on a portfolio simply by investing in many different stocks. Nearly every company, after all, relies on economic growth to retain profitability. To reduce systematic risks then, we must venture outside of equity investments to find securities that respond very differently to such dangers. This is where asset allocation comes into play. The most effective means to reduce systematic risk is to diversify an investor's money across asset classes. There are four primary asset classes: equity, fixed income, alternative assets, and cash. The difference between asset classes is that each responds differently to a change in a given systematic risk factor. For instance, while equity prospers during economic growth, bonds lag. When the economy's prospects begin to look dire, bonds begin to outperform equity. If inflation begins to climb rapidly, both stocks and bonds will likely suffer while alternative assets will appreciate. However, unlike company-specific risks that can be eliminated without reducing expected return, systematic risk avoidance results in reduced expected return. As a result, the degree to which an investor reduces the systematic risk exposure of his or her portfolio by diversifying across asset classes is largely determined by his or her ability and willingness to accept risk, as measured by volatility.



For diversification to work properly, investors must not only spread their eggs among many baskets, but also ensure that each basket isn't in the same room. While investment risk is an inevitability, we strive to minimize its impact as efficiently as possible by eliminating company-specific risk and appropriately managing systematic risk.

## Financial Planning: Helping You Realize Your Goals

**A diversified investment portfolio is the cornerstone to building a solid financial future, but a financial plan is the broader blueprint.**

At O'Brien Management, we believe that having a strong financial foundation involves more than a sound investment strategy. To attain financial security in any stage of life, it is important to have a comprehensive plan. Financial planning is an integral part of our services to O'Brien Management clients. We recognize that financial planning is not a one-time event; rather, it is an ongoing, fluid process that evolves as your life changes. During our meetings with clients we begin by talking about goals, risk tolerance, and time horizon. We then focus on specific topics to create a sound investment strategy that works for each client's individual situation. Among the areas we address are:

- Projecting income in retirement • Financing the purchase of a home • Renting vs. buying a home
- Insurance needs • Paying for a child's education • Social Security • Estate and tax planning
- Planning for long-term care expenses • Structuring a savings plan

Our role is to encourage you to consider all aspects of your financial wellbeing, and when needed we can help you find legal, tax and insurance experts in specialized areas to help you. When we meet we will talk with you about your planning needs, and we want you to call us when questions arise. There is no additional fee for our planning discussions; at present they are included as part of our services to you.

Our commitment to financial planning has grown in recent years. Lis Zimmerman heads our financial planning practice; Lis, Lauren Gibbons, and Cindy Kuppens are all enrolled in Boston University's Program for Financial Planners. In today's volatile markets, we remain focused on helping our clients build wealth through disciplined, diversified conservative investing, yet our interest in your financial wellbeing extends beyond your investment portfolio. Call us to talk about building a solid financial plan, or reviewing the plans you already have in place.



## Upcoming O'Brien Management Client Workshops

### YOUR 2007 TAXES AND YOUR PORTFOLIO

Are you considering the most effective way to pay taxes on realized capital gains and income produced by your O'Brien Management investment accounts? One option you may want to consider is using assets from your OBM account to cover your investment tax liability. Please call us if you would like to discuss whether this option is right for you.



### SIGN UP FOR EDELIVERY FROM SCHWAB

Would you like to access your account statements, trade confirmations and tax reports online via schwaballiance.com? Benefits of online delivery include speed and access to a 10-year archive of your account statements.

OBM can help get you started. If you are interested, please call Allison Gates or Lauren Gibbons at (617) 547-6717.

CURRENTS EDITOR: CINDY KUPPENS  
ckuppens@obrienmanagement.com

### Investing Basics for Women Wednesday, April 16 10 am to 11:30 am

By popular demand, Lis Zimmerman and Cindy Kuppens will hold another Investment Basics workshop for OBM clients. During this interactive workshop you will gain an understanding of O'Brien Management's approach to investing, key investment concepts and terminology, and how to read an O'Brien Management quarterly statement. This workshop is very helpful for any woman who wants to gain an understanding of basic investment concepts and OBM's approach to investment management.

### Investing in Volatile Times Thursday, April 17 9 am to 10:30 am

Hear Ted Martin and Brandon Auger discuss recent financial market trends and O'Brien Management's views on our strategy for long-term investing. As space is limited, please register early for this session.

### Planning for Long-Term Care Expenses Wednesday, May 14 4 pm to 5:30 pm

A recent study reports that more than 68% of people over age 65 will have a need for assistance with daily activities at some point in their lives. Long-term care, including help with daily living activities, either in your home or in an assisted living or nursing facility, can be very costly. We believe that it is important to think ahead about how you will pay for long-term care services if you need them. For some people, it makes sense to self-fund long term care. For others, it may be wise to purchase a long-term care insurance policy.

Lis Zimmerman and Lisa McAree (president of the McAree Company, an insurance brokerage) will discuss the basics of long-term care. Lis will focus on when it makes sense to self-insure long-term care expenses, and Lisa will present an overview of Long-term care insurance—how it works, what it costs, and situations in which it may be appropriate. Lisa has worked with several O'Brien Management clients to help them evaluate the need for long-term care insurance. We value her expertise and her commitment to helping clients evaluate what is best for their situations.

**To Register:** Please call us at 617-547-6717 or e mail Cindy Kuppens at ckuppens@obrienmanagement.com if you would like to attend one of our spring client workshops. All workshops will be held in our office at 124 Mt. Auburn Street. If you are interested in attending any of the workshops (at a separate time) via Web cast, please let us know.

*Our goal is to continually improve our service to you. We want to hear from you whenever you have a suggestion about how we can better meet your needs. As always, our best suggestions come from you, our clients.*

## Staff News

Congratulations to **Brandon Auger**, who has passed his Chartered Financial Analyst Level 2 exam! Brandon is on the home stretch now, and will take the last exam (Level 3) later this year.

**Ted Martin** spoke at the Massachusetts Council of Human Services Providers convention early this winter. His topic was "Investment Best Practices for Nonprofits". Please let us know if you would like us to meet with your nonprofit or church board. We have an excellent presentation on guidelines to follow as financial stewards for your organization.

**Cindy Kuppens** and **Lis Zimmerman** are founding members of the **Boston Area Women's Life Planning Network**, a group of professional women committed to providing exceptional education on legal, financial and eldercare issues facing women at every stage of life. The group held its first roundtable workshop in November. Attendees resoundingly agreed that the workshop was very helpful and said that they would welcome additional sessions. In May, workshops on investing and financial planning, tax and estate planning, family law, long-term care and elder care, and mortgage basics will be held in Weston and Lexington. Please contact Cindy at 617-547-6717 if you would like to receive an invitation to these workshops.

