



BEYOND WEALTH
FINANCIAL MANAGEMENT

What is a risk profile?



Introduction

If you are considering investing, you will certainly be asked about your “risk profile”, your “attitude to risk” and your “capacity for loss”. These terms can sound technical but the idea behind them is straightforward.

Your risk profile is an overall picture of how much investment risk is suitable for you. It usually takes into account three main factors:

- Your attitude to risk
- Your capacity for loss
- Your investment timescale

Together, these help shape the level of risk that may be appropriate. When you invest money, its value can go up and down. Risk is simply the possibility that the value of your investments could fall, especially in the short term. Your risk profile helps an adviser to understand how much of that uncertainty is appropriate for you.

It is not about whether you are brave or cautious as a person. It is about making sure that your investments match both your financial situation and your comfort level.

What does attitude to risk mean?

Your attitude to risk is how you feel emotionally about investment ups and downs. For example, imagine you invest £20,000 and, after a difficult year in the markets, it falls to £17,000. Some people would accept this as part of long-term investing and stay invested. Others would feel anxious and want to withdraw their money immediately.

Neither reaction is right or wrong. The key is that your investments should reflect your comfort level, so that you are less likely to make decisions driven by panic.

What is capacity for loss?

Capacity for loss is different from attitude to risk. It is about what you can actually afford financially, rather than taking into account your emotions.

For example, if you are investing money that you will not need for many years and you have a strong emergency fund, you may have a higher capacity for loss. A temporary fall in value would not affect your day-to-day life. However, if you are investing money that you need for a house purchase next year, your capacity for loss is low. Even if you say you are comfortable with risk, it may not be suitable to invest in assets that could fall sharply in the short term.

An adviser must consider both your attitude to risk and your capacity for loss before making a recommendation.

How is my risk profile assessed?

Most advisers will ask you to complete a risk questionnaire. This is usually a series of multiple-choice questions designed to understand how you view risk and uncertainty.

The questionnaire is not a test and there are no “correct” answers. It simply helps structure the discussion. However, the result of the questionnaire is not used in isolation. A good adviser will talk through the outcome with you.

For example, if the questionnaire suggests you that are comfortable with higher risk but your financial situation shows that you cannot afford significant losses, the adviser will discuss this with you and adjust recommendations accordingly.

At Beyond wealth, our assessment of clients’ attitude to risk and capacity for loss is underpinned by the Defaqto risk profiling methodology. This uses a scale of 1-10 to identify how comfortable a client feels with taking risk with 1-2 being very cautious/low risk and 10 being adventurous/high risk.

You will answer a range of statements based on how strongly you agree or disagree with them or whether you feel neutral and then your attitude to risk score will be produced. Some common style of statements may include:

- I feel comfortable investing in the stock market
- I generally look for the safer investments, even if that means lower returns
- I have little experience of investing in stocks, shares or investment funds
- I find investment matters easy to understand

Once you have answered all of the statements, a score between 1 and 10 will be produced. The adviser will use this score to then recommend products within your risk level.

What do different risk levels mean in practice?

Risk levels are often described using terms such as cautious, balanced or adventurous or low risk, medium risk or high risk.

Whilst the wording varies between firms, the principle is the same.

Your adviser will explain what these levels mean in practical terms, including possible ranges of gains and losses.

- A lower, cautious risk approach may involve more stable assets with lower potential returns over time.
- A medium, balanced risk approach may aim for steady growth, accepting moderate ups and downs.

A higher, adventurous risk approach may seek greater long-term growth but with the risk of larger short-term fluctuations.

For example, over a long period, higher-risk investments may provide stronger growth, but they may also experience sharper falls during difficult market conditions. Lower-risk investments may not grow as quickly but they are generally less volatile. It is important to note that no investment is completely risk free. Even those with very minimum risk still have a level of risk.

Why getting this right matters

If your investments carry more risk than you are comfortable with, you may feel anxious during market downturns and be tempted to sell at the wrong time. This can damage long-term returns. On the other hand, if you take far less risk than your situation allows, your money may not grow enough to meet your goals, particularly over the long term.

Your risk profile helps to strike a balance between growth and stability that fits your life, your goals and your comfort level.

Are you ready to understand your own risk profile?

If you are unsure what level of investment risk is right for you, the best next step is to have a conversation. A structured discussion with a financial adviser can help you to understand your comfort level, your financial capacity and how these fit with your long-term goals. You do not need to know the “right” answers in advance. The purpose of the process is to give you clarity and confidence.

If you would like to explore your risk profile and what it could mean for your financial future, arrange an initial consultation with the Beyond Wealth team today and take the first step towards an investment plan built around you.



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