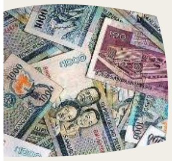

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Why Knowing the Risk Before Investing Matters

by Coach Rose D. Gases, RFP®

A cardinal rule in investing says high risk comes with potential returns while low risk is associated with low returns. But why do many still gamble on the possibility of the high returns without considering the amount of risk they are in effect taking?

During the pandemic, many are forced to work from home temporarily while some permanently. Either way, there is a good chance of diminution of income. And to recover that lost income over a short period of time, people are willing to gamble their life savings.

There is no shortcut as risks increase the higher the target return over a shorter period of time.

Financial planners train to evaluate the risk-reward tradeoffs to help their clients in their decision-making. This is why financial planners evaluate their clients' needs, time horizon, and risk appetite.

Investopedia defines financial risk as the possibility of losing money on an investment or business venture.

Risk assessment and matching allows the financial planner to narrow the options of his clients to what is truly fit for the latter. The exercise also leads to risk minimization through diversification strategies that the financial planner can formulate for his clients. For this reason, his clients need not enter into high-risk investments if there are available investments and strategies that can meet clients' goals at lower risk levels.

Even companies do risk assessments before they start on a new business venture to estimate their rate of return while mitigating the risks which will affect their growth and operations.

When it comes to investing in financial securities, one of the most common risk assessment tools used is standard deviation. Standard deviation measures the volatility of the historical or expected returns of an investment around its historical or expected average return, respectively. The higher the standard deviation, the riskier the asset is and vice versa. Investments with high standard deviations are not necessarily bad investments. What is important is to match the return-risk profile of the investment with that of the investor. Unless there is no other recourse, the return-risk profile of the investor should not be made to adapt to that of the investment.

Case in point, if a planner's client needs to earn a high return to achieve his financial goals (e.g. sending children to college or retirement) but the client himself is risk averse, risk minimization can take the form of adjusting the plan with higher periodic contributions, a higher starting investment, lower future cost of goals or even delaying the target date for goals (e.g. retiring later) so that the required return is aligned with the client's return-risk profile. And with investment diversification, the individual riskiness of investments may be lowered when combined in a portfolio while achieving the same target return.

It is difficult to gain a reasonable return without taking some risks. That is why it is only prudent to understand risk and manage it to minimize your losses.

Risk is manageable with due diligence and diversification. And a duly-trained financial planner will be in the best position to provide the guide on how to do just that.

Coach Rose is a Registered Financial Planner with an AB Mass Communication degree cum laude from Adamson University. She may be reached at rose@personalfinance.ph.

Gamification of Personal Finance

by Coach Theodore Marc B. Gutierrez, RFP®

Financial planning is often performed at the last minute. One of the reasons for the delay may be math anxiety or the feeling of being intimidated by numbers. And the stronger your aversion to math as a student, the higher the chance that you may be procrastinating on doing your financial plan.

Numbers are so complex that the brain finds difficulty wrapping itself around them. Simply thinking about math brings about various negative emotions, including fear, aversion, and even phantom headaches.

But financial planning is much more than just the fear of numbers. There is also the fear of discovering the harsh reality that you may be far off from where you need to be to achieve your financial goals in life.

Fear not! There are easier ways to do financial planning. One of them is to hire a seasoned financial planner who is both an expert number cruncher and therapist.

Another way is to apply gamification. Gamification is defined as putting game elements and mechanics into non-game scenarios.

Studies confirm that gamification helps ease the tension and anxiety associated with stressors like financial planning. Gamification is a great tool for providing motivation and soliciting higher levels of engagement.

The usual gamification stuff that you see are those that plug points, badges, and leaderboards into their products and services. The Nike Run Club app, for example, measures the distance of your runs and assigns equivalent scores for your friends to see, thereby motivating you to add more mileage for points.

Here is an example of how you can gamify financial planning.

Start by building good habits that progressively add to a better portfolio like saving Php100 per day. For each Php100 saved, give yourself a point. List down a few more positive personal finance activities to compile as many points as you can.

Seeing how your points increase is motivating enough. But that motivation may just be short-lived because, let's face it, merely assigning points can become dull after a while.

And since games need to be fun, the best way to overcome boredom is to further gamify the process. In this regard, a level up would be to create a to-do list that assigns your points to an energy bank which, in turn, fuels a spaceship! That's right, a spaceship. The goal is for your spaceship to reach a certain destination. When the destination is reached, without you realizing it, you would have formed habits out of your positive personal finance acts.

If you want detailed suggestions on how to gamify personal finance, you may send a message to my email below.

Coach Marc is a Registered Financial Planner with over a decade of experience of developing & presenting innovative programs that promote financial and social entrepreneurship. He may be reached at marc@personalfinance.ph.

Editor's Note

Efren Ll. Cruz, RFP®
Editor-in-Chief

Itching does not Provide Relief

The skin is the only part of your body that can feel both pain and itch. And though it feels good, scratching in fact triggers mild pain in the skin to distract you from the itchy feeling itself. Scratching may make you feel better but only for a moment.

Sometimes the pain from scratching releases the pain-fighting chemical serotonin that can make the itch feel even itchier. Thus, the more you scratch, the more you itch. And the more you itch, the more you scratch leading to a tough cycle to break.

We often find ourselves in situations where we also itch, but this time to spend our money on things that we probably never thought of buying in the first place. It is just that they were placed in our realm of consciousness as we surf online shopping sites. Once that itch is scratched, the itch is reinforced with the longing for the package to arrive. And when the package arrives, the itch is passed on to other purchases.

Just like with physical itches, scratching the financial itch only brings temporary relief. The best way to avoid the itch is to avoid the situations that lead to them, just like you would avoid places and even tempting foods you are allergic to that could lead to itching.

Both physical and financial itching cannot be totally avoided. But at least we can minimize them through conscious effort.