Wealth Management

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Building an investment portfolio

What is a portfolio and how is it constructed?

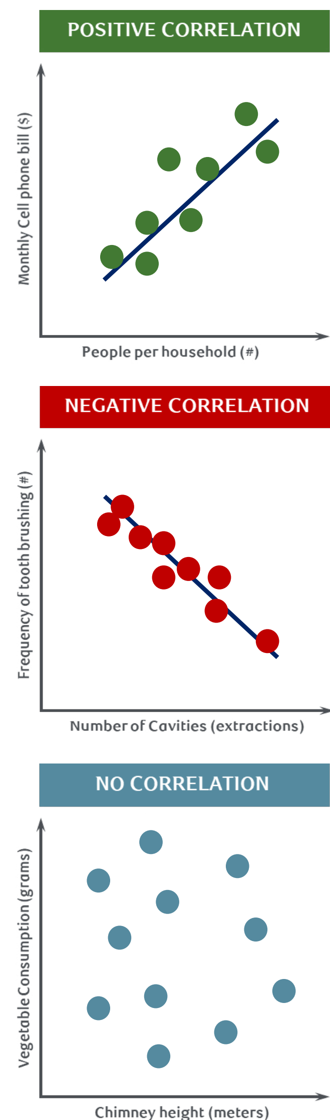
An **investment portfolio** is a collection of securities and/or financial assets. There is not a single "right" way to build the perfect investment portfolio. Building your portfolio will depend on your goals, objectives and time frame, your tolerance and capacity for risk, as well as your comfort level with different types of securities.

Why diversify your portfolio?

Investment securities perform differently throughout economic cycles. **Correlation** measures the degree to which security prices move in relation to one another. A **positive correlation** means that as one security increases in value, the other security can be expected to increase as well. A **negative** correlation means that as one security increases in value, the other is expected to decrease in value. **No correlation** means there's no expected connection between price movements.

A portfolio with highly correlated securities is generally more volatile than a portfolio with less-correlated securities. Choosing a mix of securities — **diversifying** — can help to reduce risk within your portfolio.

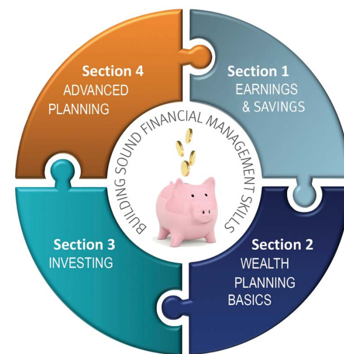
To the right, are some examples that illustrate positive, negative and no correlation:



Investor behaviour

As human beings, it's part of our nature to use mental shortcuts when evaluating information or predicting outcomes. **Cognitive bias** can lead to decisions based on thoughts or interpretations which may or may not be true. **Emotional bias** can lead to decisions that are affected by our feelings at a point in time. Biases can cause investors to make investment decisions that don't align with their long-term objectives.

Market cycles can influence perceptions about risk and potential returns. Investment markets move up and down over time. This up-and-down movement — **volatility** — can impact how you feel about your portfolio. When the markets are rising, people tend to feel good about their investments. Overconfidence, however, can lead to additional risk because investors are hopeful that growth will continue indefinitely. When markets decline, sometimes abruptly, investors can become fearful and cautious. Fear can lead to reluctance or inability to make investment decisions. Working with a qualified advisor can help keep you on track through the ups and downs of market cycles.



Evaluate your portfolio

It's important to monitor the performance of your portfolio, considering both risk and return. Return is typically expressed as a percentage — the amount that your portfolio increased or decreased over a period of time. Risk-adjusted return takes into account the amount of risk the investor accepted in order to achieve that return. To evaluate risk-adjusted return, investors can compare the performance of their portfolio to an alternative and comparable portfolio, also referred to as a **benchmark**.

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