

Step 3: How much risk do I want to take?

The risk profile consists of the annual risk budget and the liquidity reserve.

My annual risk budget

The real risk is not volatility, but the loss of hard earned assets. The «My Private Banker» approach determines the personal risk appetite with a specific amount of money, the annual risk budget. This value determines the maximum loss the investor is prepared to bear in a given year.

This personal loss threshold should help to limit the destructive power of extreme financial market collapses. If the losses of the financial assets exceed the annual risk budget, measures should be taken immediately. This can mean the sale of all financial assets or the purchase of hedging instruments (e.g. derivatives). Investments in financial assets can only be made again when the risk budget for the following year is available.

The annual risk budget is set in proportion to the monthly salary in order to provide the investor with an emotional reference to this abstract value. It shows how big the tolerated maximum loss is and should help to simulate as realistically as possible reactions within the investor's fear alarm system. This can cause the investor to review and adjust the risk budget.

My annual risk budget (in CHF)

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My liquidity reserve

With the liquidity reserve, the investor determines the sum of liquid funds that must be available at all times in order to cover easily an unexpected liquidity requirement. The amount of liquidity required depends on the desired level of security.

The following question might help to determine the liquidity reserve: How long should the liquidity reserve cover the household expenditures when all income sources got lost? If the answer is «half a year», a liquidity reserve equivalent to half of the annual household expenditures would be required.

My liquidity reserve (in CHF)

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