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Work out how much of an investment risk you are willing to accept and then keep it under review, says Barry O'Neill, investment director with Carbon Financial Partners in Aberdeen

Step one for investors: Accept there's no way to avoid risk

RISK AND RETURN: Even hiding cash under the mattress involves an element of risk, says investment director Barry O'Neill

We all deal with different risks as part and parcel of our daily lives, and become accepting of and even comfortable with those we face most routinely.

The one exception for many people is the risk inherent in their investment portfolio or pension plan. This is usually because they don't properly understand the true nature of the risks involved.

Seismic events like the outcome of last month's EU referendum can lead people to re-appraise their attitude towards investment risk. What they may have believed was "theoretical" risk can feel very uncomfortable as it becomes a reality.

Understanding that risk and return are inextricably linked is the first step to a less stressful investment experience.

Even keeping all your money under your mattress or at the bank involves acceptance of risk.

Large piles of banknotes at home won't be covered by your home insurance and the compensation limit should your bank default is only £75,000 per person.

Anyone holding more than this in a single bank or building society should think about spreading the risk.

Over the long-term, whether held at home or in the bank, cash is wide open to the erosive impact of inflation.

Taking only as much risk as you need in order to achieve your financial objectives is the next most important principle.

If you don't need to earn 10% a year, you don't need to fill your portfolio with shares.

Although shares have the best record of delivering inflation-beating returns over the long-term, they can and regularly do have periods of several years where they under-perform government and corporate bonds or property.

Diversification reduces risk. A portfolio invested entirely in shares may deliver greater returns but it also comes with significantly more risk.

During the global financial crisis in 2008, many shareholders experienced falls of 30% or more.

Taking risky assets like shares and mixing them with less risky assets such as government bonds helps to smooth out the ups and downs, delivering a much less bumpy ride.

The next step is to make sure you regularly review the amount of "risk" in your portfolio. Whatever your optimum level of risk is to achieve the returns you need, stick to it.

The investment mix of your portfolio will vary due to the assets moving in different directions or at different speeds.

Leaving this unchecked over a prolonged period can result in you inadvertently taking on much more risk than you realise.

So, for a less stressful investment experience:

- Accept that there is no free lunch; if you want higher returns, you need to accept more risk.
- Diversify away as much of the risk as possible by spreading your investments widely.
- Regularly re-balance your investments back into line with your optimum mix of assets to deliver the returns you need, while controlling risk.

Barry O'Neill

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