

MANAGING RISK

You can **diversify** your risk if you buy a basket of shares, following a ‘risk-spreading’ strategy. A group of different companies’ shares that an investor might own is called a **portfolio**. Portfolio performance is a result of how well the stocks perform collectively (measured by the price you bought them at compared with the current market price). The benefit of buying a diversified portfolio is that losses on a certain stock can be diluted or compensated by gains in other stocks that comprise the portfolio. **Professional managers** make investment decisions about each portfolio and you can participate in such portfolios by investing in a **collective investment scheme**. There are several types of collective investment scheme to choose from, including:

- unit trusts;
- investment trusts;
- tracker funds (for example, exchange-traded funds).

Such schemes are also known as **pooled investments**, where many people put in different amounts of money and the total amount is invested in different assets or asset classes and managed by a professional asset manager.

Activity 7.1

The table below presents the value of four stocks on 2 January 2009 and 23rd October 2009.

Company	2/1/2009	23/10/2009
BP	533p	565p
Lloyds	97p	96.23p
Easyjet	283p	378p
Barclays	153p	361.45p

Source: www.reuters.com

Let’s say you bought 100 stocks of each company. What is the total value of your portfolio on 2nd January? What is the value of your portfolio on 23rd October?

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Activity 7.2

A stock market index is a representation of a portfolio of stocks in a certain market. FTSE 100 is the stock index of the UK market and it comprises the 100 largest UK blue-chip companies based on size and liquidity. Funds usually use stock indices as a benchmark, or reference, for their performance. Indices have their value not in price but using a points system. The points change corresponds to a change in price of the stocks composing the index portfolio. As you can see in the following graph, from mid April 2009 Barclays plc has performed better than the performance of the FTSE index.

FTSE 100 index and Barclays Plc



— FTSE 100 Index
 — Barclays Plc

Source: www.reuters.com

Which one do you think presents higher variability? Why?

Tip Look at the highest and lowest prices. Which line on the graph varies the most?

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Activity 7.3

Let's look at some other indices. Click on:

www.bloomberg.com

Go to 'Equity Indexes' and find out what the following indices are by clicking on the names: Dow Jones Industrial Average, S&P 500, Nasdaq Composite Index, CAC 40 Index, DAX Index and Nikkei 225.

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Activity 7.4

The table below presents the value of the main stock indices on 23 October 2009.

Index	Value	Last change	% change
S&P 500	1,079.60	-13.31	
NASDAQ	2,154.47	-10.82	
FTSE 100	5,242.57	35.21	
CAC 40	3,808.24	-12.61	
DAX	5,740.25	-22.68	

Calculate the daily percentage change of each index. Which index had the biggest change?

Activity 7.5

Click on this web link to find out more about pooled investments:

http://www.moneymadeclear.fsa.gov.uk/products/investments/types/pooled_investments.html

What are the main benefits of pooled investments?

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Activity 7.6

Click on this web link to find out more about the asset management industry:

www.investmentuk.org

Go to 'Investors', then 'Glossary'. Find out what the following are: unit trusts, investment trusts and index tracking funds.

Activity 7.7

Click on this web link to find out more about stock indices:

www.ftse.com

Go to 'About us'. What is the FTSE Group and what are their indices used for?

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