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EXCLUSIVE ADVICE ON FINANCIAL, INVESTMENT AND OTHER ASPECTS OF THE SUCCESSFUL PHYSICIAN'S PERSONAL LIFE

*Investing*

# ☞ How much should you diversify?

## *You can't avoid all risk*

As a physician, you know that almost any medication or procedure carries some risk. As an investor, the same holds true.

Even the broadest portfolio entails some peril, notes *The Washington Post*. But risk comes in two forms: market or systematic risk, and idiosyncratic or extra risk.

You can't avoid market risk. Over the past 75 years, the *Post* says, market risk, as measured in standard deviation, has hovered around 20%. Think of it this way: In two-thirds of the years, the S&P's annual return has ranged between a loss of 9% and a gain of 31%. That's the risk you have to live with if you invest in stocks.

But you want to avoid any more risk than that — the so-called idiosyncratic risk. A portfolio with just a few stocks usually exposes itself to that kind of risk.

Combining mutual funds and stocks might provide adequate diversification, the article suggests. One strategy: place 50% of your stock investments into a stock index fund like the Vanguard Index 500; 25% into sector funds; and the last 25% into 10 to 20 individual stocks.

There's no absolute best number of stocks to own, The Motley Fool points out. The idea is to invest your money in the best ideas. And, because you want to track company activities and financial performance, most people find 8 to 15 stocks manageable.

### Know more, diversify less

While you need to diversify, the more you understand the companies you invest in, the less diversification you need, maintains Steven Abernathy,[1] who runs a firm that specializes in medical and information technology investing.

He agrees that you want to spend as little time as possible on market risk, which you can't control, and devote the bulk of your efforts to reducing the risk you can control. And that, he maintains, involves understanding as much as possible about a relatively few well-chosen firms. "We would rather own a few companies that we know everything about than a lot of companies that we know very little about."

Many physicians, he says, understand the value of new products that they may use. But too often, they fail to grasp the financial underpinnings of the company producing the product. His firm makes a practice of understanding that kind of information for about 12 core holdings. He questions the ability of a nonprofessional investor to truly understand the financial workings of more than one or two companies.

Embrace volatility as part of investing, Abernathy says. But keep in mind that the key to intelligent investing involves knowing as much as you can about the companies in which you invest — or selecting a qualified money manager to do that for you. ■

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