Singer Wealth

Asymmetrical Returns: More Reward with Less Risk

The best investors are always looking for opportunities with the greatest upside relative to the risk. Unlike traditional investments that often require balancing risk and reward, asymmetrical investing seeks opportunities where the potential gains significantly outweigh the potential losses. This does not mean that great investors never take big risks.

For instance, in venture capital, an investor might fund a startup with the potential for huge growth. Even if the startup fails, the loss is limited to the initial investment, but a successful venture could yield exponential returns. Understanding how to analyze the risk adjusted return is critical.

In 2022, when interest rates were near zero, it made little sense to own long-term treasury bonds since there was almost zero reward yet substantial interest rate risk. Historically referred to as risk-free return, US Treasuries were being called return free risk.

Investors must avoid investments with below average risk adjusted returns. In the stock market, asymmetry can also be seen in certain options strategies. An investor might use options to limit their downside exposure, while still maintaining significant upside potential. This could involve buying call options on a stock with high growth potential or employing strategies like straddles to take advantage of market volatility. Banks do this when they create structured notes that are linked to a security; they buy options against the stock or index to create leverage and or downside protection.

For instance, our clients have been investing in structured notes issued by major banks that track a major stock market index like the S&P 500, which provide twice the returns of the index while also being insulated from the first 20% of losses if the index falls. Imagine being able to double market returns on a guaranteed basis. When you can double the returns of the market while minimizing investment risk you are achieving asymmetrical returns. Investors do accept the credit risk of the issuing bank, so it is important to work with the biggest banks like JP Morgan or Bank of America to minimize that risk.

Have you heard about our Vision Quest Process? Watch the video below to learn more!

We are committed to helping you achieve your financial goals. Please feel free to contact us with any questions, comments, or a more in-depth discussion.

Sincerely,
Keith Singer

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