Risk Management Strategies to Address Uncertainty

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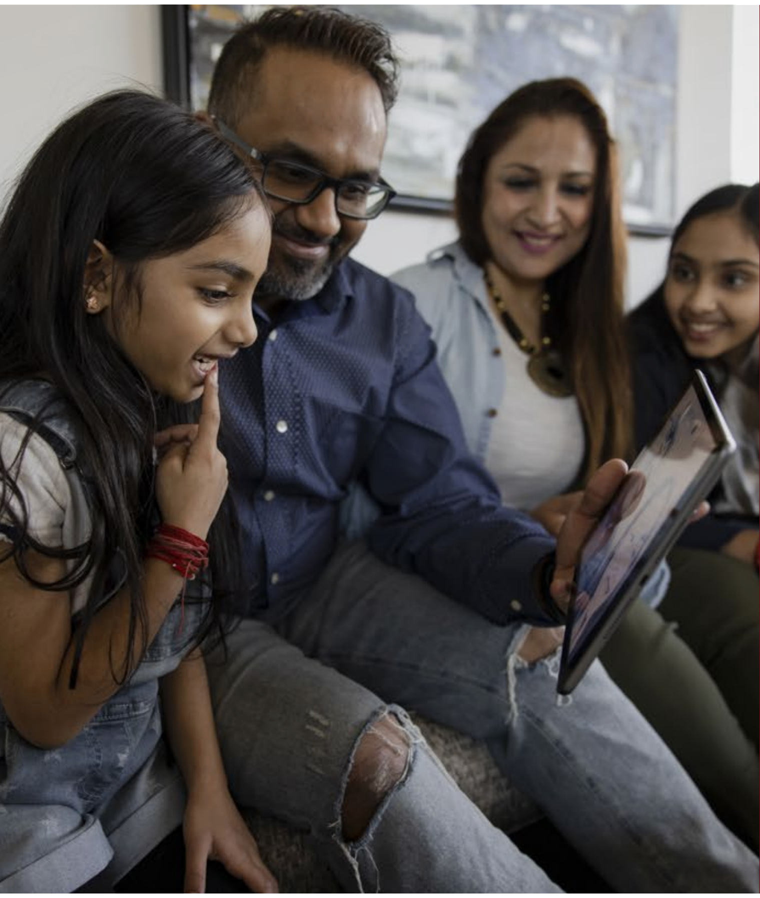
Addressing Uncertainty

Have you ever had a dreaded 'what if' scenario plague your thoughts? What if something bad happened – something small like your bus not showing up and being late for work, or something larger like a family health scare?

Focusing on the negative is not good for your mental wellness, and no one wants to tempt fate by ruminating on negative scenarios. However, being prepared for those negative 'what ifs' can set your mind at ease so you can focus on your Quality of Life.

To attain that peace of mind, there are 4 strategies to increase your financial resilience. This is a newer term in the financial fitness world that means when life events happen, you're able to withstand the impact to your finances and preserve your Quality of Life. This includes risks such as unexpected obstacles, delays, illness or even death that could have a negative financial impact on you or your family.



Decreasing financial risk increases financial resilience

These four strategies to gain resilience are called 'risk management'. They include: avoidance, reduction, transfer and retention. You're managing the financial downside – this means that bad things still could inevitably happen in your life, but you're potentially reducing the frequency and financial impact – all very good things to maintain you and your loved one's Quality of Life over time.

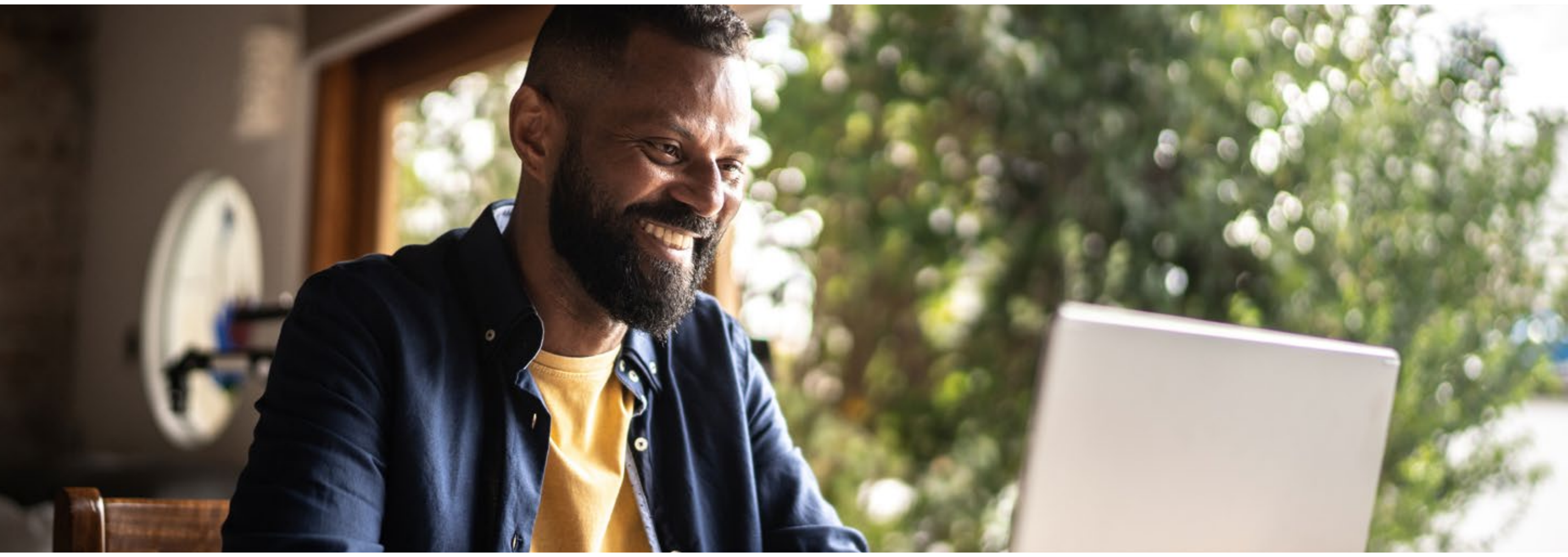
4 Strategies to manage risk

Strategy 1 - Risk Avoidance

Risk avoidance is pretty simple, as it's the elimination of the activity that leads to a financial risk. Generally, it decreases risk the best, but it's often the least practical strategy. Sure, you can avoid getting killed in a plane crash by avoiding flying, but using this as a dominant strategy will have you never leaving your home. There are also many aspects of life where you cannot eliminate absolute risk, including illness and death. So this strategy is limited in the practical application.

Strategy 2 - Risk Reduction

Risk Reduction is a more pragmatic approach that helps you dampen the financial effects of any potential activities or uncertainties in your life. A great example of this strategy is to invest in your health – do what you can to build and maintain your health, as we've seen in the HSBC Quality of Life Report, it's the top factor for Quality of Life scores. Ensuring you focus on good functional aging by keeping your body healthy will impact your Quality of Life and will save you in expenses over the longer term.

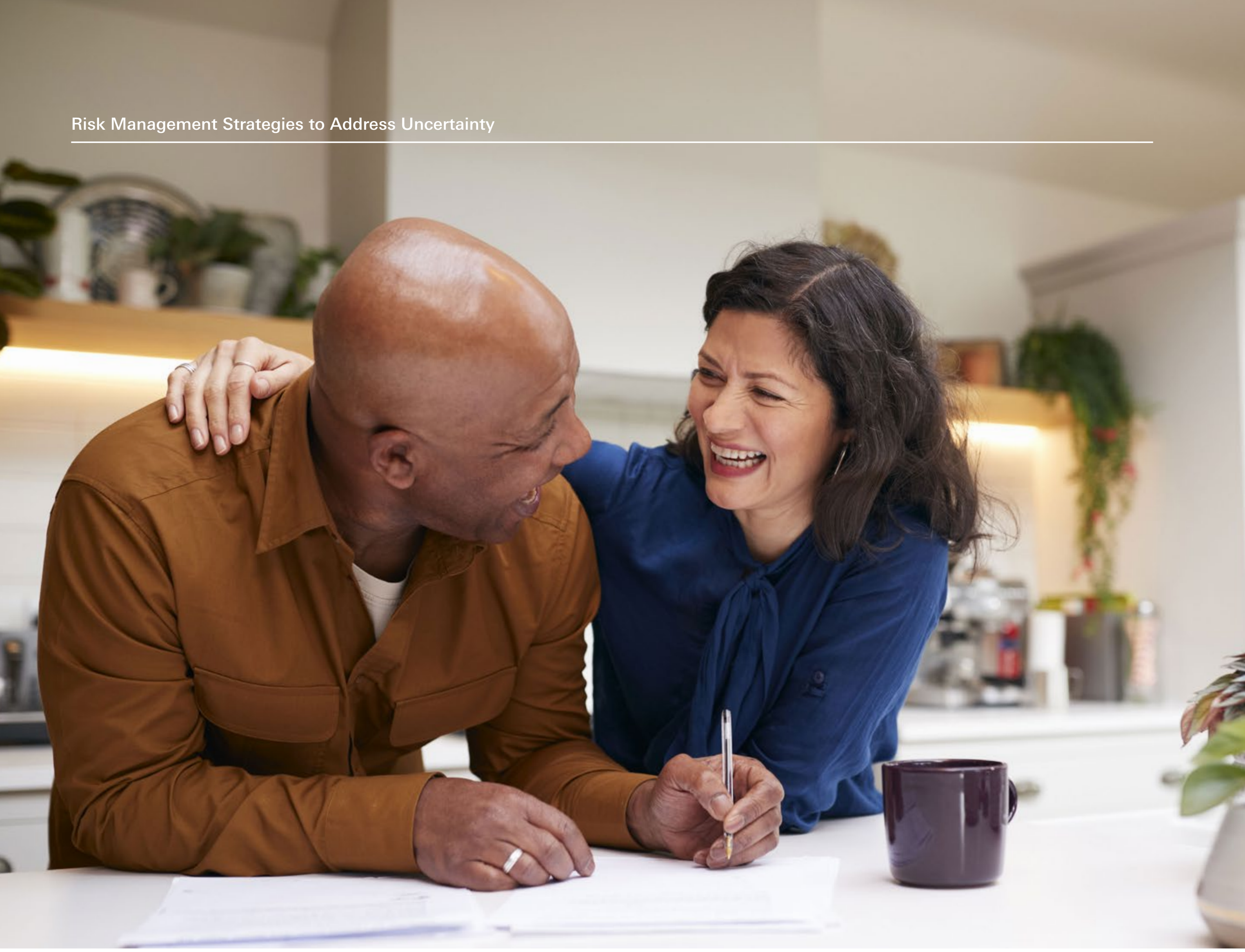


Strategy 3 - Risk Transfer

Risk transfer is transferring the financial risk of the activity or uncertainty to a third party, like an insurance company. If you take out a life insurance policy for your full need for your family, you're transferring your financial risk of dying to the insurer. You have done nothing to change your actual risk of dying. This is a great strategy for financial risks that are infrequent and would be material in impact (meaning you could lose a lot of family wealth, not attain goals, or even face bankruptcy).

Strategy 4 - Risk Retention

The fourth and final strategy can be seen as a 'do nothing' strategy, but it's generally accepting the responsibility of the financial risk. This is a good strategy when the risk probability is low, or is financially immaterial. A great risk retention strategy everyone can do is to have an emergency fund – or opportunity fund – of cash that you can access to cover six months' expenses. This will help dampen the impact of any life events with a financial impact, like car repair, minor illness or job loss. Another reason why you may retain a risk is that it's uninsurable. If this is the case, you may want to combine serval of these strategies or speak to your advisor for your options.



Review your strategy

Risk avoidance, reduction, transfer and retention are the four main strategies of handling uncertainties in life that could reduce your Quality of Life. You can choose one or a combination of these strategies to optimize your financial resilience and reduce current or potential costs. On an annual basis, it’s good to review your risk strategy, ensure you’re still comfortable with it, especially if you’ve had a major change in your life such as a move, job change, addition of a family member or change in health status or death in the family.

This will not eliminate the uncertainty in your life, but it will ensure you’re best equipped to address things as they come up with the most resilience so that you can maintain a good Quality of Life for you and your family.

Meet the expert

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