Understanding diversification

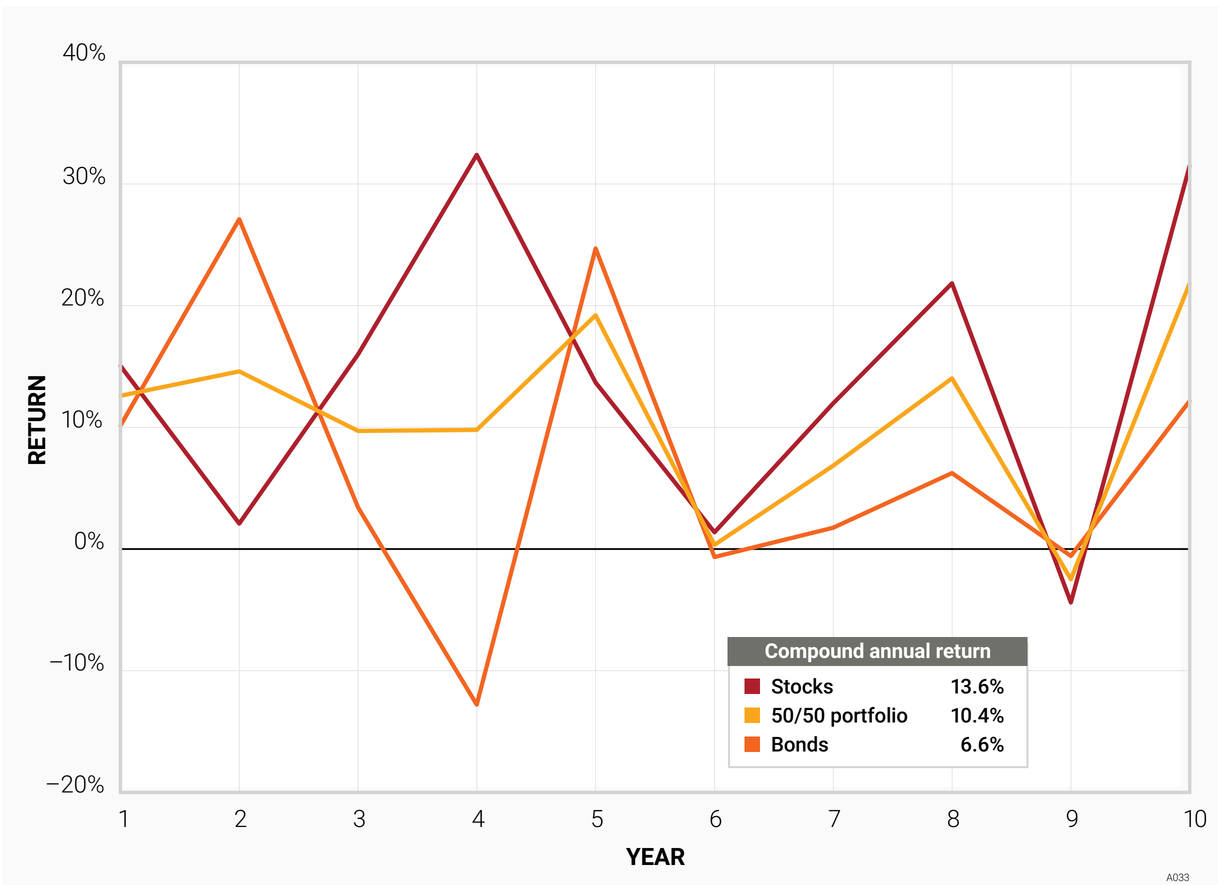
Balancing risk and reward can be a helpful investment strategy. For example, if investors invest only in stocks, they may suffer big losses when the stock market dips. But if they invest only in bonds, their returns may not outpace inflation and may not help them reach their retirement goals.

Experts recommend diversification—dividing a portfolio among different asset classes, such as U.S. and international stocks, bonds, and cash. While this strategy can encourage growth and reduce risk, it's important to remember that diversification does not guarantee profits or prevent losses.

Diversification can play a role in a portfolio's volatility. This chart shows how a diversified portfolio experienced less volatility than stock-only or bond-only portfolios over a period of 10 years.

The case for diversifying

Example of market performance, 2010–2019

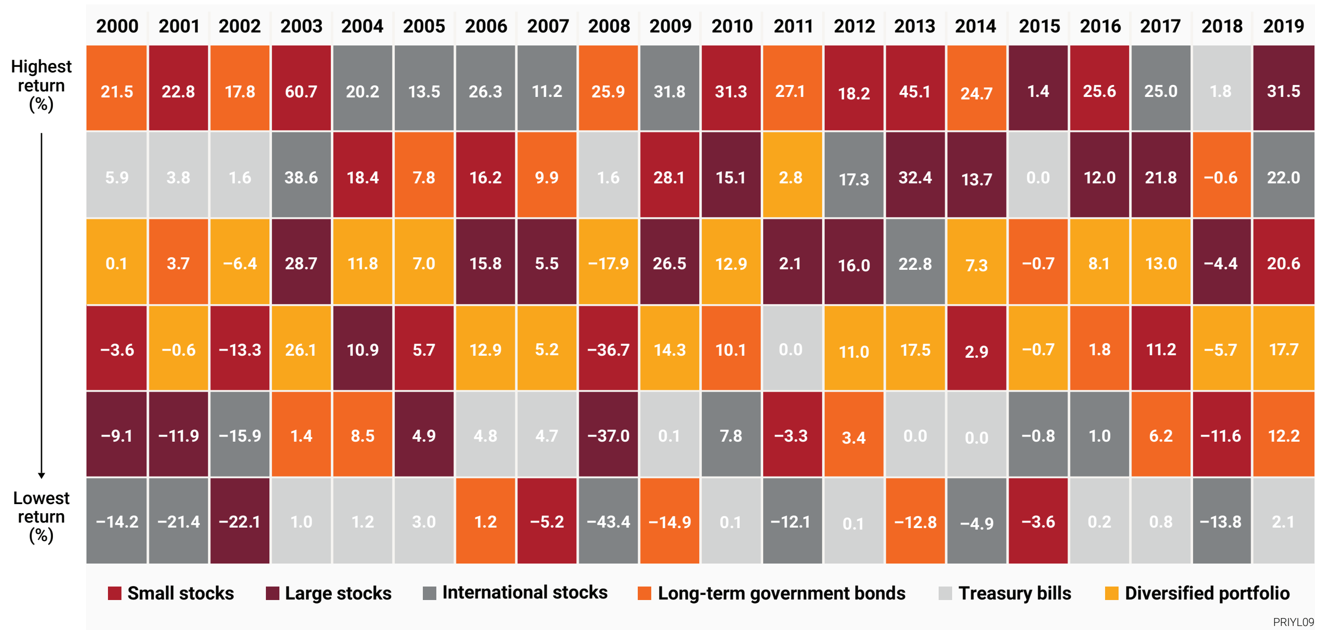


Past performance is no guarantee of future results. Stocks are represented by the Ibbotson® Large Company Stock Index and bonds by the 20-year U.S. government bond. Annual rebalancing is assumed in the 50% stocks/50% bonds portfolio. An investment cannot be made directly in an index. The data assumes reinvestment of all income and does not account for taxes or transaction costs.

No asset class stays on top

This chart shows how different asset classes perform in a given year over a ten-year period. In some years, stocks lead the way and bonds lag, and in other years, the situation is reversed. Diversification may help investors smooth these ups and downs in their portfolios.

Asset class winners and losers



Past performance is no guarantee of future results. This is for illustrative purposes only and is not indicative of any investment. Small stocks are represented by the Ibbotson® Small Company Stock Index. Large stocks are represented by the Ibbotson® Large Company Stock Index, government bonds by the 20-year U.S. government bond, Treasury bills by the 30-day U.S. Treasury bill, and international stocks by the Morgan Stanley Capital International Europe, Australasia, and Far East (EAFE®) Index. An investment cannot be made directly in an index. The data assumes reinvestment of all income and does not account for taxes or transaction costs. The diversified portfolio is equally weighted between small stocks, large stocks, long-term government bonds, Treasury bills, and international stocks (20% each). ©Morningstar. All rights reserved.

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Not guaranteed by any bank or savings association
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