



Managing Risk Through Diversification

Diversification—spreading your money among many different investments—is a widely accepted method of minimizing investment risks. Diversifying your DAP/401(k) account is as much common sense as it is investment science. This article discusses diversification and why it is so important to successful portfolio design.

What Goes Up, Usually Comes Down

We know securities behave differently from one another, going up and down in separate cycles and to varying degrees. Each individual stock is affected by a combination of different elements, including the overall stock market, the health of the industry the company does business in, and the company's own performance. For example, technology stocks have gained value in 1995. Although no one can predict with any accuracy the market's future direction, the Aggressive Growth Stock Fund, currently holding more than 35% in technology stocks, will likely decline if technology fortunes reverse. Stocks generally vary more than fixed income investments, but fixed income prices can be affected by changes in interest rates and the overall fixed income market.

Combining investments takes a middle road through the highs and lows of market performance, allowing your

DAP/401(k) money to grow regularly with fewer ups and downs along the way. A portfolio of 20 or more investments will usually fluctuate less than a single stock investment, reducing the risk of significant loss from a sudden downturn.

Diversification isn't a free ride however. When some of your investments are gaining, others are holding or losing value. Consequently, you are not likely to make a killing with a highly diversified portfolio. But you are helping to protect your savings from short-term losses and allowing them to grow over time.

Diversification Within and Across Asset Classes

Diversification can be achieved in two ways: within an asset class (for example, the Equity Index Fund) or across asset classes (for example, combining the Equity Index Fund and the Stable Value Fund).

Risk, or variability, of different markets can depend on national and international developments. Economic factors, such as production, employment, monetary policy, and levels of investment, influence markets for equities and fixed income securities in different ways. By diversifying across asset classes, therefore, you reduce that risk, or variability, of returns.

Investors who diversify but limit themselves to a single market, such as large cap stocks, assume more risk than those who invest in multiple markets. For example, a DAP/401(k) portfolio containing the Equity Index Fund, International Stock Fund and the Aggressive Growth Stock Fund should exhibit lower volatility over time than any one of the individual options alone.

Practicing Diversification in the DAP/401(k) Plan

The six DAP/401(k) stand-alone options are already highly diversified within asset classes, containing hundreds of securities within their respective markets. Each

New Investment Guide Available

Together with Neuberger & Berman Management, the TWA Pilots' DAP/401(k) Plan is pleased to offer you a copy of a new booklet titled "*Building Your Nest Egg With Your 401(k).*"

This helpful guide will provide insights into how you can best use the TWA Pilots' DAP/401(k) Plan. It will help answer many of your questions about saving and investing for and during your retirement. Topics include:

- Understanding the basics of investing and investment risk
- What you need to know to find an appropriate investment mix
- How to use your DAP/401(k) most effectively at different stages in your life
- How a 401(k) plan works and what are your obligations
- How mutual funds work and what are their advantages and disadvantages
- And much, much more

Please call or write the DAP/401(k) office for your free copy.

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investment option is designed to outperform a particular market index. For example, the Aggressive Growth Stock Fund is compared to the Russell 2000® Index (stocks of small to medium companies) and the International Stock Fund is compared to the MSCI EAFE Index (non-U.S. stock market).

The three DAP/401(k) model portfolios, discussed in the July 1995 issue of

Different Types of Risk

Principal Risk: The chance the money you have invested will decline in value.

Credit Risk: The chance a borrower will default on an obligation.

Market Risk: The likelihood a broad investment market, such as the bond or stock market, will decline in value.

Liquidity Risk: The possibility you won't be able to sell or convert a security into cash when you need the money.

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Performance



See printed newsletter for performance

How To Read Performance: The graphic display above shows fund performance as arrows and market performance, represented by the benchmarks, as bars. Fund and market performance YTD runs through September 29, 1995. Performance since inception runs from July 1, 1993, when all six funds and three model portfolios became available to participants, through September 29, 1995.

FUND COMPONENT WEIGHTING

These tables represent component weighting for individual investment funds as of September 29, 1995.

Stable Value Fund

	Weighting
Wellington Bonds	Liq 10%/Core 40%
PRIMCO GIC	45%
Cash	5%

Conservative Equity Fund

Federated Stock Trust	21%
Morgan Core	21%
Neuberger/Berman Guardian	21%
USAA Income Stock	16%
Wells Fargo TAA	21%

Equity Index Fund

Wells Fargo US Equity	100%
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Growth Stock Fund

Fidelity Contrafund	20%
Fidelity OTC	20%
Janus Fund	20%
20th Century Growth	20%
Vanguard US Growth	20%

International Stock Fund

EuroPacific Growth	38%
Templeton Foreign	38%
20th Century Intl Equity	10%
Morgan Stanley Instl Asian	7%
Morgan Stanley Instl Emerg Mkts	7%

Aggressive Growth Stock Fund

AIM Constellation	17%
DFA 9-10 US Small Co.	16%
Fidelity Select	17%
Heartland Value	16%
PIMCO Adv. Oppty "A"	17%
20th Century Vista	17%

Net Value of Funds (Millions)	401(k)	DAP
(September 29, 1995)		
Stable Value Fund	\$23.5	\$103.1
Conservative Equity Fund	25.8	46.3
Equity Index Fund	4.5	24.3
Growth Stock Fund	6.6	33.6
International Stock Fund	11.7	42.8
Aggressive Growth Stock Fund	32.9	76.6
Conservative Portfolio	1.2	16.6
Moderate Portfolio	10.3	465.4
Aggressive Portfolio	3.8	19.2
Fidelity Funds Window	—	96.3
Total	120.3	924.2

Managing Risk... cont. from front

Heads Up, are good examples of well-diversified investments, both across and within asset classes. If you prefer to choose your own mix of investments rather than invest exclusively in one of the model portfolios, the stand-alone options provide the tools you'll need to create a well-diversified portfolio. If you take this route, it's important to choose your options wisely and don't concentrate all your assets in one investment option (see rule two below).

Rules for the Road

Here are two simple rules to remember when diversifying investments, both within and outside the DAP/401(k).

Rule One: Eliminate "security-specific risk." Purchase a broad range of investments across various markets rather than a limited selection of individual securities. This way, no single investment will dominate the performance of your retirement account.

Rule Two: Spread your money across the different asset classes, stocks and fixed income. As you've seen, each asset class has its own unique risk and return attributes. And since the risks of one asset may complement the risks of another, it may be possible to achieve higher investment earnings and reduce your portfolio's volatility. **HU**

Mark Your Calendars!

DAP/401(k) investment seminars are planned for December 11 and 12 in St. Louis, and December 13 in New York.

New retirement planning software will be introduced, a guest speaker from a prominent mutual fund family will discuss investment basics as they apply to the plan, and plan features and fund performance will be reviewed. More details will be announced in November.

DAP/401(k) Important Telephone Numbers

Performance:

Benefits Express Daily NAV 1-800-892-2017
Fidelity Funds 1-800-881-4015

Account Information:

Benefits Express 1-800-828-8100

For account balance information or to make transfers, 8 am to 5 pm CST Monday through Friday.

From rotary telephones or from outside the US, call 1-708-883-0471.

Use company ID# 6662 followed by the # sign.

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The intent of this communication is to provide useful information, not investment advice. Each participant in the TWA Pilots' DAP/401(k) Plan is ultimately responsible to make his or her own investment decisions.