What is diversification?

SUPER:

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Part of Manulife's investment basics video series.

The Manufacturers Life Insurance Company

ACTION:
The video starts with CHIP, a Financial professional with a neat haircut wearing a business suit, standing in front of a white-screen background. Chip is talking to the

DIRECTOR off-camera.

VOICE OVER: Okay, ready? On my mark. 3-2...

ACTION:
JIM enters interrupting Chip and sticks his head into the shot. Chip has no idea who this is. Jim is an everyday guy wearing jeans and a casual button-down shirt.

JIM: Hi.

CHIP: Can I help you?

JIM: Uh, yeah, they actually sent me in to help you...

CHIP: Help me?

JIM: Yeah, to try and... simplify things?

JIM: Just do what you were doing and I'll jump in if I think something's too complicated.

I'll just stand right here.

ACTION:
Jim stands right next to Chip in the shot. Chip composes himself and then looks at the camera.

CHIP: Well, today... we're here to try and explain some simple investment concepts to you.

ACTION: Jim gives Chip a look.

JIM: Well, they're important, but not necessarily simple.

CHIP: Fair enough. Let's get started. Do you even know what we're here to talk about today?

JIM: Yes, I've read your notes.

ACTION:
Chip looks a little surprised.

JIM (Cont'd): When talking about investments, many bring up the word "diversification."

CHIP: As they should.

JIM: Diversification is a pretty fancy word, but what does it actually mean?

CHIP: I'll jump in here. Diversification is really the easiest way to even out the ups and downs of the market. It's the act of dividing up your money among a variety of asset classes – which consist of various stocks, bonds and cash vehicles.

JIM: You've already lost me. Look. I'd simplify that a bit and say when it comes to investing in the stock market, you shouldn't put all your eggs in one basket. You should try to invest your money in many different things. And to do it right, you need to understand how different investments work.

CHIP: That's right. And that's where a chart like this can help....

ACTION:
He points to this "Callan Chart" that appears and builds on-screen.
CHIP (Cont'd): As you can see, this Callan chart shows the average return of the indices of each asset class over the last ten years. The investment with the highest average returns one year did not have the highest returns the next, so it's difficult to predict which will perform best each year.

JIM: Yeah, and nobody can read that chart without their eyes glazing over. Look, how about this, here's an example...

JIM (Cont'd): Let's say you invest all your money in an Umbrella company, but the next year it hardly ever rains. Chances are, that company will not sell many new Umbrellas and you will lose money. Now, what if you put only half of your money in the Umbrella company, but took the other half and you invest it in a company that makes Sunscreen?

JIM (Cont'd): If it didn't rain much and the Umbrella company lost money, odds are that the Sunscreen company would make money with all those extra sunny days! This is a simple example of how diversification works. You spread your money around and avoid investing in only one thing, or putting all of your eggs in one basket.

ACTION:
Chip shakes his head, a smirk on his face.

CHIP: I should add that just spreading your money around doesn't mean you'll make a profit or avoid losses. But aside from that it was a pretty good explanation of diversification.

JIM: Glad you liked it.

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