

Staten Island Advance

Tool Helps Lower Risk in Stock Investments

Equity collar limits amount of loss you can sustain, while at the same time capping how much you can earn

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by Barton Horowitz

As consumers, we insure our homes, our autos, our health -- and our lives. Even money placed in a savings account at our favorite bank is insured -- but what about the money we use to invest in stocks? There's no insurance available in the traditional sense, but some market experts say there is a way, where certain stocks are concerned, to reduce the amount of risk.

For moderate or wealthy investors seeking to lower their risk in securities, the purchase of an "equity collar" can lessen the chances of being severely burned by some stocks, according to investment adviser Thomas J. Schwab, chief investment officer of Summit Portfolio Advisors.

Moderate investors, Schwab explained, are those who "have some investment capital, but not enough to live off without working, and wealthy investors are those who "have sufficient investment capital to support their standard of living without needing to work."

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An equity collar "is a tool that has broad application, not only for existing holdings but for new acquisitions as well," said the one-time Tompkinsville resident, whose company is based in Maui, Hawaii. "Before any stock is purchased, one should first see if equity collars are available for that stock, and if so, compare the benefits and risks of owning the stock outright versus under the collar."

In the simplest terms, an equity collar limits the amount of loss you can sustain from your investment, while at the same time placing a cap on how much you can earn.

The awareness of the need for this type of protection has become particularly apparent since the tragedy of 9/11, Schwab said.

"If a steep decline in the market would occur, perhaps caused by some catastrophic event, that portion of stocks protected with equity collars should retain the bulk of their values and represent a crucial source of liquidity for the investor," he said. "In my opinion, at least a partial allocation to this strategy is prudent."

Equity collars, however, may not be equally appealing to all investors, Schwab noted.

"If you are young enough to ride out the volatility of the market, collars may not be as attractive as they might be to the older investor, who doesn't have the time to recover before retirement," he said.

According to Summit Portfolio Advisors' Web site, www.ProtectYourStock.com, equity collars purchased for clients must meet the following conditions:

"The downside risk in each stock holding is within the client's risk tolerance."

"The upside potential for any collared stock is significantly greater than the downside risk."

"The net cost for the collar protection is minimal."

Wealthy investors who worry about losing their financial independence due to a sudden drop in the value of their assets might consider the equity collar strategy because it protects the core of their investment, Schwab said.

"Moderate investors who need higher returns, than bonds or CD's might offer, in order to achieve financial independence by the time they retire, might consider the equity collar approach because it allows them to be in the stock market without taking the full risk of the market," he said.

Barton Horowitz is the Advance consumer editor and writer of the Island Business Upclose column. He may be reached by e-mail at horowitz@siadvance.com.

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