

**A Short Treatise on Risk Compensation for Investors**

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### **A treatise on risk compensation for investors**

Calculated risks tend to be associated with compensation or award, where the higher the risk, the larger the return. Yet this is not always a fully balanced relationship, as investors sometimes do not receive full compensation for all the risks associated with the equity that corresponds to them. Risk is considered to be any uncertainty, and measurable potential about future financial or opportunity outcomes, where an “anticipated return on an investment is likely to differ from expectations” (Paiano, 2023).<sup>1</sup> There are two principal types of risk: systematic and non-systematic. Systematic risk involves any broad force such as market or inflation events that can’t be influenced by diversification of a portfolio. Non-systematic includes risks such that their loss potentials are mitigated by diversification since they are attached to only one security (in this case, a secondary market involving common stock). Without diversification, investors take both risks simultaneously, and if they were to minimize their non-systematic risk by investing in a mutual fund or ETF, investment vehicles like these “come with additional costs,” such that “mutual funds charge management fees” for example (Paiano, 2023)<sup>2-3</sup>. Therefore, if an investor were to pitch in money, the trade-off between risk and return isn’t always balanced, and even when minimizing risk by investing in a diversified portfolio through an investment company, additional costs are almost always involved.

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<sup>1</sup> Paiano, Frank. “Chapter I, Section B, Part 7, Risk and Return.” Introduction to Investments, Southwestern College, Chula Vista, California, 2023.

<sup>2</sup> Paiano, Frank. “Chapter I, Section B, Part 7, Risk and Return.” Introduction to Investments, Southwestern College, Chula Vista, California, 2023.

<sup>3</sup> Paiano, Frank. “Chapter II, Section B, Part 7, Mutual funds: Investment for the Masses.” Introduction to Investments, Southwestern College, Chula Vista, California, 2023.

## References

Paiano, Frank. *Introduction to Investments*. Southwestern College, 2023.