Fee-Only Financial and Investment Planning

(888) 320-9993

On Course

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Welcome. Asset allocation, which should be an important component of your investing, is the percentage of your portfolio invested in stocks, bonds, and cash. It determines how the markets and inflation affect your portfolio. This month we're talking about how you can consider allocation and diversification to manage risk within the framework of investment goals and time horizon.

You may have missed our recent series on retirement. For Retirement, Part 1 - Retirement Savings, click **here**. For Retirement, Part 2 - Social Security, click **here**. For Retirement, Part 3 - The Retirement Paycheck, click **here**.

If you want help understanding how asset allocation would work in your own investments, we are here to help you stay *On Course!*

Jennifer Lane, CFP

The Importance of Asset Allocation

Asset allocation

- Simply put, asset allocation is the percentage of your portfolio invested in stocks, bonds, and cash.
- Allocations are not good or bad; you should establish the allocation based on your situation.
- Asset allocations will change over time, given your personal goals, investment horizon, and risk tolerance.
- You can also diversify within asset classes to reduce risk even further.

How to begin

In This Issue

In addition to asset allocation, diversification is an important way to protect your investment. By owning investments that are affected by different economic factors, you reduce your risk. As one part of the economy is doing well, another might be struggling. The risk of loss is higher if all your investments are similar and are affected by the same economic factors.

- Determine your long-term and short-term goals.
    - Do you need the money to buy a new car next year or are you saving money for retirement?
    - The longer your investment horizon, the more stock market risk you can assume.
- Know your risk tolerance levels.
    - Determine how much money you are willing to lose against the possibility of higher returns.
- Match your goals with your allocation.
    - Ideally, you want to avoid having your goals adversely affected by fluctuations in the market. Stocks work best for long-term goals because they can help offset the effects of inflation. Too much stock in a short-term portfolio can hurt if the market is down when you need cash.

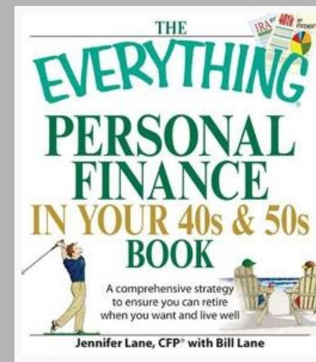
Diversity your portfolio

- Spread your money among the different asset groups to minimize your overall portfolio risks.
- Three major asset categories:
    - Stocks: more risky for the short term with potentially higher returns and better inflation protection over time.
    - Bonds: less volatility, good current income source, lower long-term returns.
    - Cash: low chance of loss.
- Ways of diversifying:
    - With tax efficiency in mind across your portfolio: allocate your stocks and bonds across the entire portfolio with the income producing bonds and fixed income in the tax sheltered retirement accounts and your stocks in your taxable and Roth accounts. Stocks are eligible for lower tax capital gains treatment when you sell them in a taxable account. Their larger expected growth is also helpful in a Roth account where that growth could be tax free.
    - Simple allocation in each account: when you're just starting to invest or your portfolio is new, it's easier to apply your asset allocation to each account individually. Target date funds are an easy way to include a mix of stocks, bonds, and cash in your accounts.
    - You can also diversify within asset classes to reduce (or increase) risk even further, e.g., emerging markets are international stocks that are riskier than developed international stocks. Small company stocks are US stocks that offer a more aggressive risk/reward balance than large US stocks.

Rebalance your portfolio

- Your portfolio shifts weight because over time some investments will do better than others. Rebalancing annually returns your portfolio to its original allocation. It's an important strategy because it forces you to sell what's done well and buy what has done less well. You will be selling high and buying low without trying to guess what is happening in the market.
- To rebalance your portfolio:
    - Sell investments that are overweight and use the money to buy investments that are underweight.
    - Buy new investments for the underweight asset categories.
- Remember:
    - Understand the transaction fees and tax consequences associated with each new investment you sell or buy.
    - Rebalancing works better when done annually rather than on a month-to-month schedule.

Get more tips in Jennifer's book



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Helpful Websites

Investor.gov

CalcXML asset allocation calculator

***Asset Allocation* by Roger C Gibson**

Morningstar

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Forward to a Friend

- While it may be difficult to sell your winners, it's better to sell high and buy low.

Q&A

Q. I was reviewing my investments and realized my bond funds have gone down. Does it still make sense to follow a 60 percent stock and 40 percent bond allocation?
-- Nia, Weston

A: Nia, it's important to live in what we call a pie chart world. Your asset allocation of 60 percent stocks and 40 percent bonds is a good, moderate one. You have a great habit in reviewing your investments annually. So now you should now rebalance to meet your 60/40 allocation. Sell the stocks that have done well and invest that money in bonds to move back to your 60/40 allocation. An important facet of re-balancing is that it takes your emotions and guesswork out of it and protects you against market fluctuations.

Jennifer in the Media

Below are links to Jennifer's frequent contributions to financial planning articles.

- The ***New York Times*** featured Jennifer in an article titled, **"Balanced Funds Don't Inspire Fear or Greed. That's Why They Are So Useful."** Click **here** to read the article.
- With a contrarian view, Jennifer contributed to an article, "***People are enraged by the idea that you should have twice your salary saved by the time you're 35!***" published recently by ***Business Insider***. Click **here** to read the article.
- Moving in together? Click **here** for the article from ***Business Insider***, **"Five questions you and your partner should answer before taking the biggest step in your relationship.**"
- ***Insider*** asked Jennifer to contribute to an article on old fashioned ways to manage your money, "**Six money-saving tips your grandma used that are way more effective than any budgeting app**." Click **here** for the article.
- Jennifer contributed to an article on ***Business Insider***. Click **here** to read "**This is the best way to do your taxes online - according to experts**."
- **CNN Money's** *Money Moves* featured Jennifer in an article on how to strike the right balance between retiring early and saving enough. Click **here** to read the article.
- Jennifer contributed to a ***CNN Money*** article "**When is the Right Time to See a Financial Advisor**?" Click **here** to read the article.
- Jennifer contributed to ***The Wall Street Journal*** article "**The Biggest Money Mistakes We Make -- Decade by Decade**." Click **here** to read the article.

Compass Planning News

- Jennifer and Sarah were both named **2019 Boston Five Star Wealth Managers**.
- AdvisoryHQ named **Compass Planning** as one of the ten best Boston financial advisors.
- Jennifer recently talked about **the top three things you should do with your money.** Click **here** to watch the segment on her blog.
- Jennifer appears on NECN every other Monday morning at 9:30 am.

Compass Planning Associates helps families, individuals, and small-business clients achieve financial security, knowledge, and control over their money. Our **fee-only, client-centered approach** provides education and guidance for achieving financial goals and dreams.