Ready, Set Retire… next year or in 30 years

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Family, Consumer, & Human Development

Thanks to:
Barbara O’Neill, Ph.D., CFP, Rutgers Cooperative Extension
Overview

- Understanding risk tolerance
- Asset allocation & diversification
- Mutual fund expenses
- Am I saving (investing) enough?
USU Employees

- TIAA-CREF or Fidelity?
  » Defined contribution
- Utah Retirement System?
  » Defined benefit
What is your Risk Tolerance?
Risk tolerance questionnaires

- Beware of risk test results
  - Reflect what investors think they should do
- Investors over-estimate their risk tolerance during bull markets
- Results differ based on recent market conditions & media coverage
You don’t have a clue…

- Until you’ve lost LOTS of $
  - How much did you lose in 2002?
  - 2008-2009?
  - What did you do in 2009?
- Investors allow emotions to control them
  - Sell low & buy high
STOCKS

They can't keep falling FOREVER! They have to hit bottom SOMETIME, don't they?
What Is Asset Allocation?

- *Diversifying* portfolio among several investment categories to reduce risk
- Example: 50% stock, 30% bonds, 20% cash assets (e.g., Treasury bills)
- Objective: lower investment risk by reducing portfolio volatility
  - Loss in one investment offset by gains in another
How to divide the pie?

- Asset allocation decisions are driven by
  - Risk tolerance
  - Time horizon
  - Goals
Asset Allocation Example

- Cash: 0.26%
- US Stock: 62.03%
- Non US Stock: 27.40%
- Bond: 9.09%
- Other: 1.22%
The Callan Periodic Table of Investment Returns

- [Link](http://www.callan.com/research/download/?file=periodic%2ffree%2f757.pdf)
- Shows how various asset classes performed over 20 years
- Illustrates need for owning different asset categories
- Best performing asset class changes
- One year’s “winner” can be next year’s “loser,” so invest in multiple assets
The Importance of Asset Allocation

- Asset allocation is the MOST important decision an investor makes
  » (i.e., buying some stock, NOT Coke versus Pepsi)
- Asset allocation determines about 90% of investment returns
- Asset allocation & diversification go hand in hand
Why Use Asset Allocation? To Increase Long Term Investment Results

- Scenario #1: $100,000 invested at 8% over 25 years grows to $684,848

- Scenario #2: $100,000 divided equally among 5 investments (One loses principal and other 4 earn 0%, 5%, 10%, and 15% average annual returns)

- *Diversified* portfolio will grow to $962,800 over the long term
Questions?
Rebalancing

- Anyone remember when 2 choices were TIAA or CREF?
  - What if you picked 60/40 stocks/bonds 30 years ago?
- **Rebalance** yearly!
  - TIAA-CREF & Fidelity will do this for you on your birthday. Sign up!
Forget Market Timing

- http://www.ifacom/12steps/step4/missing_the_best_and_worst_days
- 20 years 1/1/94-12/31/13
- $10,000 invested in S&P 500 9.22%  $58,352
- Miss 5 days biggest gains: 7.00%  $38,710
- Miss 10 days: 5.49%  $29,121
- Miss 20 days: 3.02%  $18,146
- Miss 40 days: -1.02%  $8,149
Relationship Between Risk and Return

- **Cash Equivalents**
- **U.S. Bonds**
- **Int’l Bonds**
- **Real Estate**
- **U.S. Stocks**
- **Int’l Stocks**

For illustrative purposes only. Not indicative of any specific investment.
Historical Average Annual Rates of Return

- Small Co. U.S. stocks = 12.6%
- Large Co. U.S. stocks = 10.4%
- Government Bonds = 5.1%
- Treasury Bills = 3.8%
- Inflation = 3.1%
Stocks are Risky in Short Run

- Stocks can provide high returns but…
  - Very volatile in short run (1-5 years)
  - Annual returns -50% to +50%!!

- Are you approaching retirement?
  - What if you planned to retire in 2009?
  - If you had $1 million in Oct. 2007, by March 2009: $½ million
“Safe” Investments are Risky in the Long Run

- Inflation = 3.1%
- Government Bonds = 5.1% - 3.1% = 2%
- Treasury Bills = 3.8% - 3.1% = 0.7%
- Subtract the impact of taxes & ‘safe’ investments yield negative returns
- You will not reach your goal with low risk investments
Invest for Growth

- There is no such thing as a risk-free investment!
- Retirement $ must grow faster than inflation to provide financial security
- Risk is relative
  - Short term volatility=long term growth
  - Invest in stocks for growth
● Short, medium, & long time horizon
  » Conservative to moderately aggressive
● Asset allocation funds
  » Funds of funds (9-10 funds)
  » % do NOT change over time

Questions?
It’s all too confusing!

- Let the ‘experts’ make your asset allocation decisions for you
  - Diversified portfolio starts aggressive
  - Becomes more conservative as you age & near retirement…
Target Date Retirement Fund
Target Date Retirement Funds

- Diversified portfolio of stocks, bonds & cash
- “Fund of funds”
  - Composed of multiple funds from same ‘family’ (company)
- Target date: year investor plans to retire
  - 5 year increments: 2025, 2030, 2035, etc.
- Assets are automatically re-allocated
  - Allocation gradually changes from aggressive to conservative over time
A Fund of Funds

- Income Fund
- Bond Fund
- Growth Fund
- Mid-Cap Fund
- Large Cap Fund
- 500 Index Fund

But NOT in even %
Asset allocation becomes more conservative over life of fund.
Target Date Retirement Funds

- TIAA-CREF Lifecycle funds
  - 50 yrs. 2030 (TCLNX) 0.88%

- Fidelity: Freedom funds
  - 2030 (FFFEX) 0.77%

- Vanguard Target Retirement 2030
  - (VTHRX) 0.17%
Questions?
Retirement Portfolio Tips

- Diversify across asset classes
- Avoid market timing
- Choose investments with good historical performance
  » Past returns are NO guarantee for the future!!
- Choose funds with low fees
TIAA-CREF Today: Too Many Fund Choices!

- Too much choice >> fetal position
- Few funds are “pure”
- CREF Stock
  - 80% Large-, 15% Mid-, 5% Small-Cap
  - Some foreign stocks
- Mid-Cap Growth
  - 59% Large-, 39% Mid-, 2% Small-Cap
- Read Prospectus (or at least the summary)
Most real estate mutual funds invest in the **stocks** of real estate companies

**T-C Real Estate** owns 75 properties!

- Rental income
- Appreciation @ sale
Adjusting Your Allocation

- Use TIAA-CREF.org (Fidelity) website
- You can change future allocations
- You can transfer current balances among funds
- Sign up for automatic rebalancing
- Meet with reps on campus
  » Sign up for appointment with HR
Key Considerations For Successful Investing

- Establish policies and objectives
- Stick to your plan and stay focused
- Educate yourself to make informed decisions
- Monitor investment performance (yearly)
- If you need help, seek a professional advisor
Expenses Really Do Count!

- All MFs charge expense ratios (%)
- Even small % (1-2%) make a difference
- Fund analyzer: [http://apps.finra.org/fundanalyzer/1/fa.aspx](http://apps.finra.org/fundanalyzer/1/fa.aspx)
- BEWARE! T-C expense ratios for similar funds vary a LOT!
  » Look for “institutional” in fund name for lowest expenses
Target Retirement Funds 2030
$10k for 20 yr. @5%

- TIAA-CREF Lifecycle (TCLNX) 0.70%
- Fidelity Freedom (FFFEX) 0.77%
- Vanguard Target (VTHRHX) 0.17%
- $23,066
- $22,746
- $25,646

Finra find analyzer
http://apps.finra.org/fundanalyzer/1/fa.aspx
Am I Investing Enough?

- What’s your number?
  » 10% is so 20th century
  » Research: new number is 15%
- You’re in luck! How much does USU contribute to your retirement?
  » 14.2% is top of the charts!
- Late start? Fund an IRA to supplement
Your “Action” List

- Review your current asset allocation
- Use the TIAA-CREF (Fidelity) website
  - Risk tolerance quiz
  - Asset allocation calculators
- Sign up for automatic rebalancing
- Meet with a representative
Summary

- It’s time to revisit your portfolio
- KISS: Stick to one provider
  - Consolidate your statements
- Diversify but watch for fund overlap
- Include real estate
7Twelve: A diversified investment portfolio with a plan

» Author Craig Israelsen will speak at ESCL 130 @ 1 pm Wed. Nov. 5

» Check out his website: http://7twelveportfolio.com/
It’s not magic
Financial Planning for Women

www.usu.edu/fpw

- PPT will be posted on FPW website
- Searchable blog: http://fpwusu.blogspot.com/
- Monthly (except Aug. & Dec.)
  » 11:30-12:30 in TSC 336
  » 7:00-8:30 at FLC, 493 N 700 E
- Oct. 8: 7 pm only: IRAs, 401(k), 403(b)
- Oct. 8: 12-2 TIAA-CREF workshop employees
- Nov. 12: Figure out a retirement plan
The end

● Questions?

enlightenment