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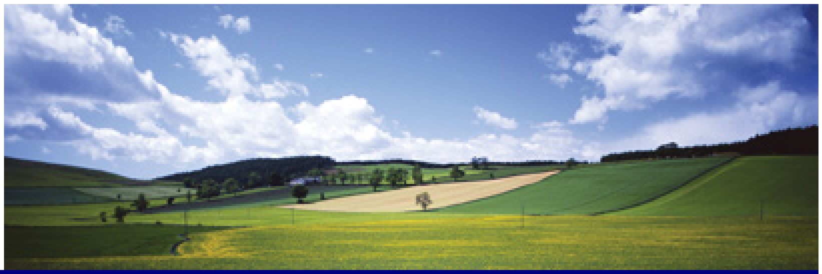

YOUR FINANCIAL FUTURE

Your Guide to Life Planning

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Balance Is Better Make It Happen!

Balance is a word we hear tossed around a lot these days. We want work/life balance, which can reduce our stress levels; we try to eat balanced meals, thereby keeping our bodies sound; and we try to balance our to-do list against our need for rest and relaxation.

Better balance can lead to better health-physically, emotionally, spiritually- and even financially. We can all agree that balance is important, so why do we often find it so difficult to apply balance to matters of finance?

According to behavioral scientists, it's because we're human. Rationality isn't always uppermost in our minds when we make money decisions. Instead, we may rely on emotion, like our need for security, the recommendation of someone we trust or the excitement of an investment's recent experience.

Unfortunately, this method of making investment decisions doesn't usually mean success-especially when compared to implementing and sticking to a balanced, rational approach. As we move through the fall season and head toward a new year, now is a great time to re-evaluate your investments, keeping the idea of balance firmly in mind.

You should remember that, while diversification neither assures a profit nor guarantees against losses, it is a widely accepted investment strategy that may help you meet financial goals.

So many investment choices…how can you decide?

Usually, people can choose from many different investment options in their retirement plans. There may be stock funds, bond funds, cash equivalents like money market funds, or others-a nice variety that could keep their portfolio healthy and strong.

Each of the three major categories of investments (stocks, bonds and cash equivalents) carries its own potential risks and rewards. You may be able to invest in some or all of them through your retirement plan. As you make investment decisions, you should be aware of some basic information about each of these categories.

Stocks. Historically, stocks have the greatest potential for growth-but they can and do experience losses. The value of stocks may rise as the economy grows strong. But, as we experienced during the recent recession, they may also suffer significant drops in value. This up-and-down tendency is known as "volatility." Investors who can accept a high degree of volatility, and who have a long time to recover if their stock investments drop, may be rewarded in the long run with higher investment returns.

Bonds. Bonds are often less volatile than stocks, but they also carry certain risks, because they are tied to credit ratings and interest rates. When these change, bonds may be impacted. Bonds may experience lower investment returns than stocks or cash, too. Some bonds (known as "junk" bonds or high-yield bonds) promise higher returns, but may actually carry a high level of risk.

Cash equivalents. This category includes money market funds, treasury bills and certificates of deposit. Although they may seem to be extremely safe, they too carry risk. By investing too much of your retirement savings in a cash equivalent, you may miss out on the potentially higher returns of the other investment categories.

While each of these investments carries some risk, the good news is that by investing a portion of your retirement account in several different categories, you can spread out that risk. Doing so may smooth the ups and downs of investing in a single category. Your finances may stay healthier, because the investments are balanced.

Investing always involves risk. That's why taking a balanced approach is so important: Returns on the three major categories of investments have not historically moved in unison, all going up or down at the same time.

How can you achieve balance?

First, remember that the right balance now may not be the right balance later. When you decide how to invest your retirement account, don't use a "one and done" strategy. Add a review of your retirement plan to your once-a-year to-do list.

Why? Because our needs and goals change as we age. An investment strategy that is appropriate for a 25-year-old may not be the best for someone who is 50. The mix of stocks, bonds and cash equivalents that works well to help younger persons grow their account in the early years may lean toward more risk-and therefore greater returns. But someone who is nearing retirement may want to consider a more conservative approach by exchanging some of the greater potential returns of stock funds for the greater potential security offered by other investment categories. Periodically reviewing the balance in your investments can help you stay on track.

Your personal balancing act: Consider risk tolerance and time

The exact mix of investments you choose depends on two basic things and how they work together. The first is your personal tolerance for risk, and the second is the amount of time you have available before you need the money.

Your ability to tolerate risk is something only you can decide. Risk tolerance, in a nutshell, is about your level of comfort with exchanging the possibility of losing some (or all) of your investment for the potential of higher investment returns.

Someone with a high risk tolerance is willing to take that chance, and someone with a low risk tolerance prefers investments that are safer but have lower potential earnings.

The time you have left to invest should be one factor in determining your risk tolerance; many people feel more comfortable with riskier investments (stocks versus cash, for example) when they are younger. That's because they have many years, or even decades, to recover if their investments don't perform well.

The danger of taking too little risk

It would be a mistake to assume that investing only in very low-risk categories is always safest. Remember, all investments involve risk. By choosing investments that have little or no investment risk, you actually increase the risk that you won't achieve your retirement goals. That's because your investments may not keep pace with inflation-much like burying money in the backyard. You won't experience much (or any) growth, and your buying power will likely erode over time. When you "dig up" your cash, it will be unlikely to meet your savings goal.

By diversifying your investments, you may benefit from positive returns on one type of investment, while being insulated from some of the negative returns of another. Your overall investment portfolio may experience less volatility than it would if you invested in only one category, contributing to your financial health.

So review your investments with an eye toward balance. Include a variety of investments in your overall portfolio, and don't be afraid to make needed adjustments. When you achieve balance in this important area of your life, you may find that the result is well worth your effort.

Here are a few questions to help you think through your risk tolerance:

1. When it comes to making investment decisions, how knowledgeable are you?

- Very
- Somewhat
- Not very

2. Which of the following best describes your investment philosophy?

- I'm a worrier, so I like to be conservative
- Taking on more risk is the only way to achieve potentially higher returns
- I like to take my time and investigate my options

3. Which of the following best describes your attitude toward investing for retirement?

- I want my retirement savings to grow but am only comfortable with a medium amount of risk
- I tend to worry that the value of my retirement savings will go down
- I want my retirement savings to grow as much as possible, and am willing to take on higher risk for potentially higher returns

Your answers to these questions may give you some insight into your own investing personality. Then you can use that information to help develop your personal investing strategy.

If your retirement plan includes a lifecycle fund, sometimes called a target date fund, it will automatically rebalance your investments as the years go by. You choose a lifecycle fund based on the year you expect to retire, and the fund managers invest for you considering the number of years remaining until that date is reached. In the early years, the investments may lean toward more risk, and move steadily toward more conservative instruments as the years go by. Of course, the principal balance of a target date fund is not guaranteed at any time, including at the target date.

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