

Guidance

Find opportunities. Avoid traps.

Forget Target-Date Funds

Submitted by Matthew Tuttle on Wed, 07/18/2012 - 9:00am

Target-date funds are on the march. These increasingly popular retirement vehicles adjust their portfolios over time, so they are stock-heavy for the young and move more into bonds as investors age. There are problems with them, though, that few understand.

These instruments focus on growing your assets early and shifting to a safer mix by your retirement – the target year when you quit working. Target-date funds are getting a lot of notice.

A July 9 [article](#) in the *Wall Street Journal* described how different target-date issuers, ranging from T. Rowe Price to Fidelity Investments, make the transition from equities to bonds at different rates. That move is called the “glide path” in mutual fund-speak. At your retirement year, some leave you with more stocks than others do.

Here are two of the key points, quoted from the WSJ piece:

[M]oney is flowing into target-date funds at a brisk pace. Their assets now total around \$400 billion, more than five times the amount at the end of 2005, according to Morningstar.

In 10 years, target-date funds could represent half of all the assets in U.S. 401(k) plans and other defined-contribution plans, says David Bauer, a partner at asset-management consultant Casey, Quirk & Associates, Darien, Conn.

The idea makes sense on the surface: Older investors closer to withdrawing 401(k) money can't afford to sustain large losses so target-date funds naturally get more "conservative" at their stage in life. However, in practice this doesn't work for a number of reasons:

1. Life expectancy is too long for you to trust a target-date fund as the panacea to your retirement financing. If I retire at 65 and have all my

SMART ADVICE



Why All Investors Need Good Advisors

By Larry Light, Editor-in-Chief

At AdviceIQ, we believe that everyone should have a financial advisor – a good one, vetted through our system to ensure that he or she has a clean background. Hiring an experienced, capable advisor gives you the services of someone who knows the landscape of investing and other necessary financial matters, such as the amount and type of insurance you should have, and how you should set up your estate.

money invested "conservatively," I could still live another 30 to 40 years. Add inflation into the mix and this is a recipe to run out of money.

2. What is conservative? Is investing a bunch of money into bonds at these yields conservative? I don't think so. Long-term interest rates can't go much lower but they can go a lot higher. And they inevitably will. When rates climb, bond prices go down much more. So that conservative, bond portion of your 401(k) will shrink in value.

3. Nobody should subject their portfolio to large losses, at age 65 or 20. That is why, for the average investor, nothing significant ever happens with their money. They get good returns in the up years, then give it all back and then some in the down years.

4. The market doesn't care how old you are. Moving money based on your age makes no sense. You should move it based on market dynamics. In a period like 1995 through 1999, when making money in the market was easy, a 65-year-old had just as much a right to earn 30% a year as a 30-year-old did. During the 2000-2002 and 2008 downturns, a 30-year-old had just as much right to be protective as a 65-year-old.

The better answer is to arrange your portfolio so it has good assets that are appreciating. If they are ascendant, buy them. When they flag, sell them and buy the new winners. This is called Tactical Asset Allocation, which I have [written about](#). You can do this yourself, or with the help of a good financial advisor. You don't need a target-date fund to do to for you.

Follow AdviceIQ on Twitter at [@adviceiq](#).

Matthew Tuttle, CFP, is chief executive of Tuttle Wealth Management in Stamford, Conn., and the author of How Harvard & Yale Beat the Market. He can be reached at 347-852-0548 or mtuttle@tuttlewealth.com. Nothing in this article should be interpreted to state or imply that past results are an indication of future performance. Please consult your tax or investment advisor before making any investment decisions.

AdviceIQ delivers quality personal finance articles by both financial advisors and AdviceIQ editors. It ranks advisors in your area by specialty. For instance, the rankings this week measure the number of clients whose income is between \$250,000 and \$500,000 with that advisor. AdviceIQ also vets ranked advisors so only those with pristine regulatory histories can participate. AdviceIQ was launched Jan. 9, 2012, by veteran Wall Street executives, editors and technologists. Right now, investors may see many advisor rankings, although in some areas only a few are ranked. Check back often as thousands of advisors are undergoing AdviceIQ screening. New advisors appear in rankings daily.

Topic:

[Bonds](#)

[Stocks](#)

[Mutual Funds](#)

[Home](#) - [About](#) - [DMCA Policy](#) - [Terms and Conditions](#) - [Privacy Policy](#) - [Journalistic Standards](#) - [Contact](#)

Copyright 2012 - AdviceIQ

Partners

Content Partner of the Motley Fool Network - Lodging Hospitality - National Real Estate Investor - Retail Traffic - The Online Investor