Rebalancing

Investing for your retirement

A tune-up for your portfolio

From your body to your car, regular maintenance can help you avoid future problems. You visit your doctor annually to keep yourself in peak physical condition, just as you take your car in for a tune-up to keep it running smoothly. So too, can periodic reviews of your investment portfolio help keep your retirement strategy on track.

Regular maintenance

Let's say that your investment portfolio is in order. You've determined your risk tolerance, your long-term goals and developed an asset allocation strategy that's right for you. You're making regular contributions to your employer-sponsored retirement plan and other personal investments. You can check off retirement planning from your to-do list. Right? Not quite.

Just as your weight fluctuates, so too, can your portfolio. As the markets change, the value of each security in your portfolio will increase or decrease at a different rate of return – changing the overall weightings of your investments. The result: Your asset allocations may no longer match your risk tolerance.

Watching your weight

To stay true to your asset allocation strategy, periodic reviews of the value of your investments can help you determine whether you wish to rebalance them to ensure they stay in line with your risk tolerance and timeline. Rebalancing is a tool for returning the components of your portfolio to the weights you desire.

Tuning up your portfolio

To rebalance back to your original asset allocation strategy, you'll need to sell off some of your stock and invest the profits in bonds and cash until your original percentage weightings are achieved. Or you can invest new money into your portfolio to bring the percentages back to the levels you have set.

Using this example, many investors might see the sharp rise in their investment and choose to leave their portfolio alone. But deviating from your asset allocation strategy can be risky. If stocks should fall rapidly – as happened during the stock market decline of 2008 – you could have lost a greater percentage of your investment than if you had rebalanced and stayed with your asset allocation strategy.

Sticking to your strategy

Rebalancing is a tool that can help you stick to a strategy when markets shift or your goals change. Your financial professional can help you learn about rebalancing and developing an asset allocation strategy that's right for you.

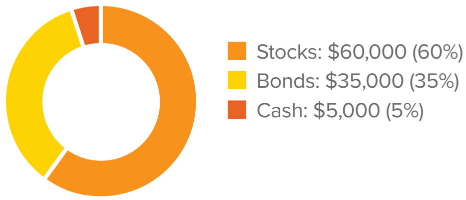
When to rebalance

Many financial experts recommend rebalancing at regular time intervals, others recommend rebalancing when your asset mix drifts 5% or more away from your allocation strategy. If your personal goals have changed, you may also wish to consider rebalancing. As you near retirement, for example, your risk tolerance may become more conservative, so you may want to rebalance to alter your investment strategy. Please note, rebalancing does not ensure a profit or protect against a loss in a declining market, but it will help you stick to a strategy that you believe is appropriate for you when markets shift or your goals change.

Note that some retirement plans offer an option for automatic rebalancing, which helps many investors know that their asset allocation strategy is being maintained.

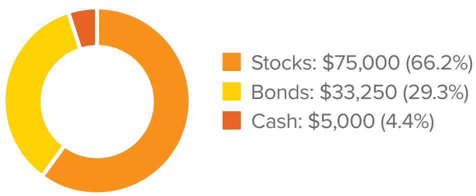
A simple example on the need for rebalancing:

PORTFOLIO – ORIGINAL: $100,000
ASSET ALLOCATION:



One year later, a boom in the equity markets causes your stocks to rise 25%, while your bonds have fallen 5%. Your portfolio's asset allocation now looks like this:

PORTFOLIO – ONE YEAR LATER: $113,250
ASSET ALLOCATION:



In just one year, you're up 13.25%. That's good. So what's the issue? The issue is that as your investment grew, it moved away from your asset allocation strategy. Your portfolio is now weighted even higher in stocks, which may expose you to more risk than you intended.

Talk to your financial professional for more information about the importance of rebalancing your investments.

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