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Diversify Your Asset Allocation To Reduce Your Risk

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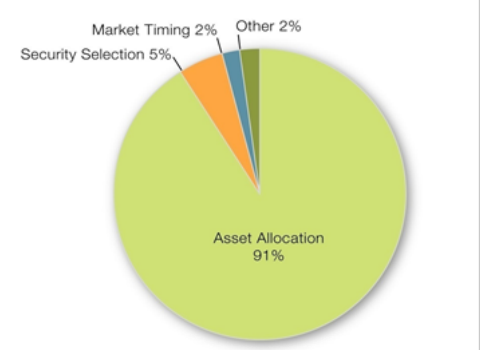
In a bull market like we are experiencing today, investing aggressively can produce high levels of returns. Conversely, in a bear market like the financial crisis in 2008, aggressive investments come with the potential for significant losses.

For this reason, investment experts say that your asset allocation is one of the most important decisions you can make related to your retirement savings. Asset allocation is a strategy to help deal with that risk. You basically divide your investments among different types of assets such as stocks, bonds, real estate, and cash. In essence, you reduce the volatility of your investment portfolio by not putting all your eggs in one basket.

The objective of asset allocation is to provide an investment mix that minimizes risk (for example, stock market volatility). The strategy is designed to help you reach specific financial retirement goals, based on your tolerance for risk. Asset classes tend to behave differently under different market conditions. Some go up while others go down. Stocks and bonds especially tend to move in opposite directions. By combining the two, you may experience more consistent performance over the long run than in either class individually.

Consider These Factors When Setting Your Asset Allocation

When setting your asset allocation strategy, take into account several factors. Look at your time horizon, how long until you will withdraw the money and your personal tolerance for volatility in the markets. Generally speaking, a longer time horizon offers the opportunity for a more aggressive investment mix, adjusted for risk tolerance. As the time horizon shortens, consider moving to a more conservative mix to minimize the risk of a short-term loss.



DETERMINANTS OF PORTFOLIO PERFORMANCE
Source: Brinson, Singer, Beebower (1991)

The pie chart to the right shows that asset allocation is the most important factor in determining how an investment portfolio performs. Individuals are much more likely to reach their long-term investment goals by following an asset allocation strategy. It’s more challenging to pick stocks or to time the peaks and valleys of the market. Changes may be appropriate from time to time but only because of a shortening time horizon, new goals, or a change in risk tolerance.

The Investor Profile Quiz at MillimanBenefits.com can help provide guidance on creating an asset allocation strategy for your retirement savings that is appropriate for your personal goals. With lower volatility, asset allocation may help you sleep better at night instead of worrying about the returns on your retirement nest egg!

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