



## ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments



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### Are You Making These Retirement Savings Mistakes?

In our last update, we gave you some tips on how to help the teenagers in your lives begin saving for retirement. This week, we'd like to review some common pitfalls that all investors can fall into when making decisions about their retirement savings plans.

We've seen all of the mistakes listed below (and more) and have made it our goal to help clients develop the most effective strategy for their needs, relieving them of the ongoing burden of managing their own assets and freeing them up to fully enjoy retirement without worrying about outliving their nest egg.

While the market volatility we've seen over the last couple of years may have had a negative impact on not only your retirement savings accounts, but also your nerves, we would point out that with losses comes the opportunity for buying at lower prices, which will be capitalized upon by any good money manager. Pulling out of stocks in lieu of bonds or cash in an attempt to make your account "safe" is just one of the mistakes that investors make in times like these. Remember, it's time in the markets, not market timing that will lead to successful long-term savings.

With that said, let's take a look at our list of five retirement savings mistakes you don't want to make.

#### 1. Taking a "Hands Free" Approach

In an ideal world, your company offers you a wide range of well-managed, low-cost funds in your 401(k) or 403(b) retirement plan, giving you plenty of choices for putting together a diversified portfolio. But the reality is that many 401(k) and 403(b) plans do not offer much choice, let alone low-cost funds. By doing nothing and leaving your hard-earned investments in an account with limited and expensive investment options, you are unable to fully maximize your retirement savings and implement the most effective strategy for your needs.

One solution to being stuck with a company plan with a dearth of investment options is to move your assets into a rollover IRA when you retire. This will give you the same tax-free savings and investing power, but with lower costs and much greater choice.

#### 2. Cashing Out

You can cash out of your 401(k) or 403(b) when you retire, or take a lump sum when you switch jobs, if you so desire. However, taking a lump-sum distribution can be costly. When you make withdrawals from your retirement plan, you pay income tax on the entire value of the distribution, as all withdrawals from a 401(k) or 403(b) are taxable—since your contributions were made pre-tax, the government wants to reclaim its share of both your savings and any gains you've made over time.

And, if you're under 59½ years of age, it becomes even more costly to take withdrawals as not only will you be taxed on the distributions, you are also subject to a 10% penalty for making an early withdrawal.

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Finally, it's also possible that by taking a lump-sum distribution you'll find yourself in a higher tax bracket, making the transaction even more taxing.

So, when considering cashing out of a plan, you need to be well prepared: First, you ought to consider whether it makes more sense to pay taxes on your account now, in your current tax bracket, or if it would be better to roll your account over into an IRA and pay taxes later in retirement, when you may fall into a lower bracket (if you know that you'll be in the same or a higher tax bracket in retirement, a Roth IRA is also very worthy of consideration, especially with the new conversion rules, which we've discussed in past updates). Second, if you do opt to cash out or take that lump sum (or to rollover into a Roth IRA), you'll need cash on hand for the resultant tax bill, which could be quite large, depending on how much you've saved over the years.

### **3. Relying Too Much on Company Stock**

Think of the centuries-old proverb: "Don't put all of your eggs in one basket" when given the option of investing heavily in your company's stock in your retirement plan. If the unthinkable happens and your company hits hard times or goes out of business altogether, you could face losing both your job and all you've worked so hard to save for retirement in one fell swoop (think of Enron, where this exact scenario played out nearly a decade ago). If you want to make your company's stock part of your retirement portfolio that's fine, just keep that portion of your portfolio small enough so that if the worst happens, your future financial wellbeing will still be secure.

### **4. Failing to Contribute Enough**

While it can be hard to deprive yourself of your hard-earned cash in the short-term by contributing the maximum to your 401(k) or 403(b), how much harder do you think it would be to face having to look for another job to make ends meet after your so-called retirement?

Saving as much as you possibly can while still employed is your best defense against running out of funds after you've stopped working. And the more you have invested, the greater your potential earnings. We always recommend that our clients contribute as much as they can, if not the maximum, to their retirement savings plans for this very reason. (Many companies also have matching funds policies, where, up to a certain amount, they'll match your contribution to a 401(k) or 403(b)—if you're not investing, that's free money lining someone else's pocket.)

Remember, the power of compounding is a powerful investment tool—just look back to some of the scenarios we charted last week for an example of how powerful. The more money you have working for you in your retirement account, compounding gains upon gains, year in and year out, the fatter your retirement goose will grow.

### **5. Investing Too Conservatively**

This is perhaps one of the most common mistakes investors make when saving for retirement or managing their IRA rollover. The logic, wrong as it may be, is that because the money they're putting away is so crucial to their financial security in the future that it should be invested only in risk-free or ultra-safe funds. This can turn out to be a painful misconception as the adverse effects of inflation can erode the purchasing power of your retirement assets over time.

To succeed over the long term, it's essential to invest a sizeable portion of your assets in stocks—there's no need to take wild risks, but your goal should be to grow your retirement portfolio over time and maintain the "real" value of your assets after accounting for inflation.

We realize this advice could have had a short-term, negative impact on retirement savings in the market environment we've seen in recent years, but, as we mentioned above, a long-term focus should overshadow shorter-term volatility. Historically, stocks have significantly outperformed bonds and cash, and we expect this trend to hold true going forward. In fact, as we've written in previous *Adviser Fund Updates*, when the market experiences big losses, you get more value from new investments as prices have been pushed down, giving you the opportunity to follow the old adage of

buying low and selling higher down the road in retirement.

### **Fidelity Bullish on Interest Rates**

In a move that probably slipped under most Fidelity investors' radar, the firm reopened four money market funds it had shuttered to new investors 18 months ago as interest rates hit rock bottom during the financial crisis. U.S. Treasury Money Market (the only fund of the four with investor class shares) began accepting new accounts on July 1st.

In 2008, when the funds were originally closed, interest rates had gotten so low that many money market fund managers had to waive fees to prevent yields from entering negative territory. Vanguard closed two of its more vulnerable money market funds, Admiral Treasury Money Market and Federal Money Market around the same time, for the same reason—those two funds remain closed.

While the Federal Reserve is keeping key rates at historic lows, there has been some life in the shorter-term paper market, with yields creeping up over the last month. This movement has given Fidelity enough confidence to reopen the money funds that invest in these issues. We think that faith will eventually be rewarded, but as U.S. Treasury Money Market's seven-day yield remained at 0.01% as of July 21st, investors should be in no rush move their money market assets back into the fund just yet.

### **About Adviser Investments**

Adviser Investments is an independent, professional money management firm specializing in Fidelity and Vanguard mutual funds. With 1,500 clients and over \$1 billion dollars under management, Adviser is one of the nation's largest mutual fund research and money management firms. Our staff of 35 investment professionals focuses on helping individual investors, trusts, foundations, and institutions meet their investment goals. Our minimum account size is \$350,000.

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