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ADVISER INVESTMENTS

ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments

In Th

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Is Riding the Lifecycle Financially Healthy?

Fidelity's answer to this question apparently was "no, not enough," as the firm recently announced it would be "enhancing" the investor, Advisor and VIP classes of its line of Freedom lifecycle funds by increasing or adding allocations to international stocks, commodities and inflation-protected securities (TIPS). But even with the enhancements, we do not think the Freedom funds, or Vanguard's Target Retirement funds, are a good fit for most investors' portfolios.

If you're not familiar with it, the term "lifecycle fund" refers to what is usually a fund of funds with an allocation the provider deems is appropriate for the fund's target date. So, as is the case with Fidelity's 12 Freedom funds and Vanguard's 11 Target Retirement funds, the name will usually include a year, which is generally the investor's planned retirement date. As the date nears, fund allocations will become more conservative, with the goal of preserving capital and providing a lower-risk income stream in retirement. The idea is to provide a one-size-fits-all approach to retirement investing in the form of a single investment.

Fidelity's Freedom funds have over five million shareholders and nearly $90 billion invested in them, with the first having been rolled out in 1996. The firm says it is tweaking the funds to increase the international exposure to reflect the fact that overseas markets are a larger part of the global market, and have also become less risky to invest in over the long term. The additions to commodities and TIPS are intended increase diversification and lower inflation-related risk.

While Fidelity didn't go into too many specifics on how the changes will effect each of the 12 funds, they did show a projected allocation for the Freedom 2020 fund, which you can see in the table below, alongside the fund's current allocation, and for comparison, Vanguard's Target Retirement 2020 fund's allocation through August.

	Fidelity Freedom 2020		Vanguard Target Retirement 2020
	Current	Projected	Current
Domestic Equity Funds	52%	41%	55%
Commodities	-	7%	-
International Equity Funds	13%	17%	14%
Bond Funds	33%	26%	32%
TIPS	-	7%	-
Short-Term Funds (Cash)	2%	2%	-

As you can see, the changes aren't drastic, with 11% moved from domestic funds into a combination of commodities and international funds and 7% moved from bond funds into TIPS. In some of the funds with target dates farther off, such as Freedom 2050, the allocation moves may be more marked, but for now, Fidelity isn't saying. It is worth noting that the Vanguard fund's most recent allocation looks a lot like the Fidelity fund's departure point, so perhaps the move is, in part, to distinguish two similar products from each other.

It's also worth mentioning that while Fidelity and Vanguard have somewhat similar takes on how to allocate their lifecycle funds, if you look at other fund providers' funds, you will see vastly different strategies. For example, PIMCO's RealRetirement 2020 fund has nearly half of its assets in bonds and TIPS, about 20% in international stocks, 20% in real assets (tangible assets such as real estate or coins, as opposed to shares of company stock or bonds) and 10% in domestic stocks. So the industry itself is confused on how best to allocate these products, which should be a red flag for investors.

It is our opinion that target or lifecycle funds are not a suitable investment for most people, for several reasons beyond the confusion on how to allocate. The first is that a given firm's lifecycle funds are often not constructed using the best funds the firm has to offer. In both Fidelity and Vanguard lifecycle funds, this is the case, with the firm's best actively-managed funds eschewed for funds with broader objectives or indexes. Another potential problem is the number of funds used in constructing these funds of funds. While Vanguard showed some restraint, using five funds in the Target Retirement 2020 fund (a well-diversified portfolio generally doesn't need many more funds than that), Fidelity has managed to jam 24 different funds into the Fidelity Freedom 2020 fund! This is far too many management teams and styles, in our opinion.

For those reasons, we think the one-size-fits-all approach to investing is not a great idea—most investors should have a larger list of criteria for their portfolio than just a date when they may retire. For the health of your retirement investments, we recommend putting in a little extra effort (or talking to a trusted investment adviser) and constructing a portfolio tailored to your needs rather than taking the easy way out and hopping on a lifecycle fund.

About Adviser Investments

Adviser Investments is an independent, professional money management firm specializing in Fidelity and Vanguard mutual funds. With 1,500 clients and $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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