

# Asset Allocation

## What does it mean to stay the course?

- It doesn't mean do nothing; it means have a plan and stick with it.
- Asset allocation is the key power tool that enables you do stick with your plan.

## What is asset allocation?

- Your portfolio's mixture of asset classes
- Why hold stocks in your portfolio? Returns
- Why hold bonds in your portfolio? Shock absorbers
- A big change in the stock market is 30%. A big change in the bond market is 6%

## Why is asset allocation important?

- There's no free lunch. Higher risk gives higher returns and vice versa.
- Vanguard's analogy: asset allocation is like climate; specific investments are like weather (San Francisco vs. Boston). Investments do well at different times.
- Your asset allocation determines the overall risk of your portfolio
- 88% of your investing experience (volatility and returns) are due to asset allocation.

## What are some considerations when setting your asset allocation?

- **Time horizon**
  - How long do you plan to keep the money invested
  - How soon will you begin withdrawing
  - Over how long a period of time?
- **How much do you need to earn** to meet your goal?
- **How risk-averse are you?** Can you stay the course when the market drops 30% as it did in the fall of 2008?
- If you had a 50-50 asset allocation, your portfolio value would have dropped only 15% instead of 30%
- **How stable are your other sources of income?**
- Rule of thumb: Consider 60-40, then factor in your own situation.

## Then what stocks/bonds/funds should you invest in?

1. **DIY:** A broadly diversified portfolio that matches your asset allocation
2. **Life strategy fund:** your chosen allocation of assets all in one fund
3. **Target retirement fund:** a life strategy fund that becomes more conservative over time