When You're Serious…

by Bradley R. Newman, CFP®

Are You Missing The Target? Or Set It And Forget It?

You can't argue that 2015 has been a bit frustrating for investors, especially those who are nervous about an impending retirement. At best, we could refer to the investing environment as volatile; through the end of August portfolio gains have been difficult to find this year. As investors have grown increasingly frustrated, many have become attracted to the idea of utilizing *Target-Dated* funds as a means of getting portfolio management based on the broad parameters associated with their proximity to retirement.

The concept of the *Target-Dated* fund is that you pick a fund created around your anticipated retirement date, i.e. 2015, 2025, 2035, etc., and that the mutual fund managers will invest your dollars appropriately based on that retirement date. The fund managers are supposed to adjust your investment mix to account for both changes to the macroeconomic environment and for the fact that you are incrementally approaching your retirement date.

Unfortunately, many investors are getting neither appropriate investment portfolios, nor the ongoing management they have expected.

Is Set It and Forget It Appropriate?

The original concept for *Target-Dated* funds, and the subsequent marketing of these products, is notably different than the reality that investors in *Target-Dated* funds have experienced since their creation over a decade ago.

The impetus for the creation of these funds was to provide an option for people, who did not have the interest or knowledge required to manage their investments, with an option that would make the appropriate adjustments as the landscape of the investment world evolved and as they moved closer to retirement. Unfortunately the typical experience in these funds has been a static allocation, and it is exceedingly likely that no changes were made during the recent 10% correction. While market timing is never prudent, the recent volatility certainly created opportunities.

How Do I Know What I'm Getting?

It would seem reasonable to assume that *Target-Dated* funds from different companies would recommend similar levels of stock/bond exposure for someone that is planning to retire in the year 2025; however, the differences across *Target-Dated* funds with this mandate is staggering. Of the 202 *Target-Dated* funds reviewed by Morningstar, Inc. with a 2025 target, the level of stock market exposure ranges from a low of 24.1% to a high of 70.5%; this is a differential of 46.4%.

The point is not to debate what the appropriate level of stock exposure should be for someone set to retire ten years from now, because each person's situation and circumstances will impact that answer. The point is that there is little consistency found across the universe of *Target-Dated* funds charged with the same goal. Additionally, it is very likely that very few of the people who own these funds know how much stock exposure they have or if that level is appropriate for their circumstances.

I'm Paying How Much?

In addition to the *Target-Dated* universe having wide disparities in investment strategies, there are also significant variations in the costs between the funds. For example, in the same universe of funds with a target year of 2025, the annual expense ratios can range from 0.1% to 1.7%. To put that in perspective, that differential on a retirement account valued at $500,000 translates into an additional $8,000 in annual expenses. Remember that there is nothing inherently wrong with paying a fee if you are getting a commensurate benefit; however, you need to be able to quantify your benefit relative to the cost.

Aren't The Returns Similar?

The discrepancies in the level of stock market exposure and the wide variations in the internal fees are just two examples of the inconsistencies and issues within the *Target-Dated* fund universe. The bottom line is that, even with the uniform mandate of creating an investment portfolio for someone that is planning to retire in 2025, the inconsistency among the investment returns is staggering: last year the best performing fund the 2025 category produced a gain of +7.4% while the worst performing fund created a gain of only +1.3%. On that same portfolio of $500,000, the cost of making a wrong decision, within what should be a tightly clustered group of funds, could have produced a net gain/loss differential of 6.1% or $30,500.

You Deserve A Customized Solution

As with most aspects of the investment world, things are not necessarily as they appear and should not be taken at face value. If you choose to use a *Target-Dated* fund, don't rely on the date found in the name of the fund, do you homework in order to determine if that fund will actually be appropriate for your situation.

Bradley R. Newman, CFP® is with Roof Advisory Group, Inc., an independent investment management and financial advisory firm based in Harrisburg. The firm is a fee-only Registered Investment Advisor that provides portfolio management and financial planning services for individual and institutional clientele. The firm's email address is invest@roofadvisory.com.