For Your Benefit

Maximizing Your Retirement Investment Strategy

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Whether you are transitioning into retirement over the next five years or are already in retirement, the following items should be considered on a regular basis to maximize your retirement investment strategy:

Asset Allocation: Since approximately 90% of your investment return depends on your asset-allocation decision, it is important to revisit your allocation on a regular basis. My experience indicates that an individual's perception of his allocation is quite different than the actual allocation. This disconnect between perception and reality means one may be taking on unnecessary portfolio risks.

Assume your current asset allocation is 20% fixed income, 75% U.S. equities, with the remaining 5% international equities. Whether this allocation is appropriate depends on your risk tolerance. If you have a moderate tolerance for risk, you may want to maintain a target asset allocation of 40% fixed-income and 45% U.S. equities and 15% international equities. To do this, you would need to liquidate 30% U.S. equities and invest 20% in fixed-income holdings, even though interest rates are rising, and an additional 10% in international equities.

In 2006, I continue to recommend diversifying overseas in both developed and emerging markets to boost returns and reduce portfolio volatility. In addition, I recommend underweighting U.S. small and medium cap equities, as well as REITs, due to their impressive rally of more than 70% over the past three years. Rebalancing your portfolio to your target asset allocation will help reduce the emotion factor and enable you to maintain a long-term perspective.

Retirement-Plan Distributions: In most cases, I recommend deferring your retirement-plan distributions until age 70½ to take advantage of tax-deferred compounding within your tax-deferred retirement accounts. However, this strategy will not be beneficial if you expect to be in a higher tax bracket when you begin taking distributions. If higher tax rates are a concern, consider rolling over a portion of your retirement assets into a Roth IRA each year. This will generate income tax on the rollover amount, but avoid future income taxes on the Roth IRA distributions.

Income-Tax Planning: Minimizing federal and state income taxes should be deeply embedded in your retirement investment strategy. As a general rule, allocate your fixed-income holdings and tax-inefficient equity funds (i.e., U.S. small and medium cap, REITs, and emerging markets) in your tax-deferred accounts. In contrast, allocate your low turnover equity funds, such as index funds, to your taxable account to take advantage of the 15% federal tax on capital gain and qualified dividends. Another way to reduce your income-tax burden is to avoid state income taxes on your retirement-plan distributions by establishing residency in a state without an income tax, such as Florida.

These are just a few ideas to help maximize your retirement investment strategy and provide peace of mind that you are doing the right things to achieve your goals.