RETIREMENT 101, PART 2: THE IMPORTANCE OF ASSET ALLOCATION

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In this second installment of our Retirement 101 blog series, we'll be discussing asset allocation. You may be asking yourself why asset allocation is important. So, let's take a look. First off, what is asset allocation? It is the practice of spreading your investments across different asset classes (such as stocks, bonds and cash) in different regions (domestic and international markets) in order to help reduce your risk. The theory behind asset allocation is that different asset classes and different regions perform well under different market, economic and political conditions. Stocks and bonds, for example, tend to have a low correlation, which means they typically do not increase or decrease to the same extent under similar conditions. So, when stocks are down, bonds may not be down as much. Some asset classes have negative correlations, so when one goes down, the other goes up, and vice-versa. By diversifying your investments among different asset classes and regions, you may be able to lower the risk and potential volatility in your portfolio. Traditional asset allocation typically involves stocks, bonds and cash. However, as investors learned in 2008-2009, when unprecedented events happen, there can be unexpected results, such as stocks and bonds moving down together. So, many investors are now including emerging markets and alternative assets (such as commodities and currencies) in their portfolios, as well. Finding the right investment mix for you will depend on your age, your timeframe to retirement and your comfort level with taking risks. Your 401(k) provider or your financial advisor may be able to provide you with a quiz that can help you determine the right asset allocation for you. Exchange-traded funds, or ETFs, can make ideal asset allocation investments within your 401(k). Consider that ETFs: • Are available in a range of domestic, international and emerging market options from small caps to large caps, from municipal bonds to corporate bonds—and everywhere in between. There are many currency and other alternative ETFs as well. • Traditionally track indexes, meaning that they typically offer broad asset class exposure, which may make them a good choice for asset allocation. • Have low fees that may enable more of your investment to be allocated toward your retirement. In future installments, we'll discuss why ETFs may not be as prevalent in 401(k) plans, understanding the features of your 401(k) plan—and much more. For more information on 401(k) plans, visit www.wisdomtree.com/401k. *Read our 401(k) series here.*

Important Risks Related to this Article

Asset Allocation does not eliminate the risk of experiencing investment losses. Ordinary brokerage commissions apply.

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