BUILDING BLOCKS FOR RETIREMENT

Diversification

Variety Pack

Maintaining a diversified portfolio can help you feel more in control during uncertain economic times.

The COVID-19 pandemic has certainly tested the resolve of even the most seasoned investors. To help regain some confidence and sense of empowerment, it may be helpful to review a fundamental principle of investing: diversification. Diversification is spreading your retirement savings and contributions among a variety of investments (e.g., stocks, bonds and cash) to help reduce your risk of over-concentration in a specific investment or asset class.

Diversification Opportunities In Your Workplace Retirement Plan

Although diversification doesn't ensure a profit or prevent a loss in a declining market, taking advantage of the range of investment options offered by your workplace retirement plan may help guard your account against major market swings. You don't need to invest in a whole lot of options; just enough to ensure you have a good mix of different investment types.

Many retirement plans offer investment options that include built-in diversification opportunities. We have summarized a few of these below.

Mutual Funds

Think of a mutual fund as a basket that contains many different investments — that all have something in common — be it companies that together make up a market index, a particular asset class (such as stocks or bonds, international or domestic) or a specific sector (such as companies in the energy, construction, manufacturing, transportation or technology industries). There are also mutual funds that invest solely in companies that adhere to certain ethical or environmental principles (also known as socially responsible funds).

What's nice about mutual funds is that investors are able to purchase collection of investments that are professionally managed. It's instant, easy diversification that lets you avoid researching and buying stocks or other types of investments one by one.

Asset Allocation Funds

Asset allocation funds also offer diversification, professional management and monitoring within a single basket of investments. Within this category are risk-based funds (also known as lifestyle funds) that allocate the money in your retirement account among investment options aligned to your comfort with risk. Age-based funds (also known as target-date or lifecycle funds) correspond with the year you expect to retire and automatically invest more conservatively over time as the date approaches.

Managed Account Or Advice Services

Some plans offer a professionally managed investment advice service that is personalized for each participant. This may appeal to some participants, especially those who would prefer that someone make investment decisions and selections for them. Most investment advice services provide a customized investment strategy, based on your own unique time horizon, risk tolerance and other financial goals. In addition, they automatically rebalance your investments on a regular basis so that your asset allocation strategy (the percentage of your money that's divided up among stock, bonds and cash asset classes) remains in place according to your wishes — especially important during either a market downturn or rebound.

Dollar-Cost Averaging Through Your Investment Fund

The investment funds offered in your retirement plan also offer another potential benefit: dollar-cost averaging. Dollar-cost averaging means investing the same amount of money at regular intervals, no matter how the market is doing. This approach is built into your retirement plan — each pay period you automatically invest the same contribution amount, whether the market is up or down.

When prices are low, you end up buying more shares of the fund. When prices are high, you buy fewer shares with the same amount. Over time, the average price you pay for each share is typically lower than the average market price.

Keep in mind that dollar-cost averaging does not guarantee a profit or protect against a loss in a declining market. You should make sure that your risk tolerance allows you to continue contributing during down markets. But it's a practical and efficient approach to investing that may help give you a sense of control during uncertain times.

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