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Provided by Jerry K. Ask Investment Services

Monitoring Your Portfolio

You probably already know, you need to monitor your investment portfolio and update it periodically. Even if you've chosen an asset allocation, market forces may quickly begin to tweak it. For example, if stock prices go up, you may eventually find yourself with a greater percentage of stocks in your portfolio than you want. If stock prices go down, you might worry that you won't be able to reach your financial goals. The same is true for bonds and other investments.

Do you have a strategy for dealing with those changes? You'll probably want to take a look at your individual investments, but you'll also want to think about your asset allocation. Just like your initial investing strategy, your game plan for fine-tuning your portfolio periodically should reflect your investing personality.

The simplest choice is to set it and forget it - to make no changes and let whatever happens happen. If you've allocated wisely and chosen good investments, you could simply sit back and do nothing. But even if you're happy with your overall returns and tell yourself, "if it's not broken, don't fix it," remember that your circumstances will change over time. Those changes may affect how well your investments match your goals, especially if they're unexpected. At a minimum, you should periodically review the reasons for your initial choices to make sure they're still valid.

(Continued on page 2)

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S&P 500 Top Ten Largest Stocks:

Apple
Google
Microsoft
Exxon Mobil
Berkshire Hathaway
Wells Fargo
Johnson & Johnson
General Electric
JP Morgan Chase
Facebook

-Putnam Research
S&P Dow Jones Indices
6/30/15

Even Things Out

To bring your asset allocation back to the original percentages you set for each type of investment, you'll need to do something that may feel counterintuitive: sell some of what's working well and use that money to buy investments in other sectors that now represent less of your portfolio. Typically, you'd buy enough to bring your percentages back into alignment. This keeps what's called a "constant weighting" of the relative types of investments.

Let's look at a hypothetical illustration. If stocks have risen, a portfolio that originally included only 50% in stocks might now have 70% in equities. Rebalancing would involve selling some of the stock and using the proceeds to buy enough of other asset classes to bring the percentage of stock in the portfolio back to 50. The same would be true if stocks have dropped and now represent less of your portfolio than they should; to rebalance, you would invest in stocks until they once again reach an appropriate percentage of your portfolio. This example doesn't represent actual returns; it merely demonstrates how rebalancing works. Maintaining those relative percentages not only reminds you to take profits when a given asset class is doing well, but it also keeps your portfolio in line with your original risk tolerance.

When should you do this? One common rule of thumb is to rebalance your portfolio whenever one type of investment gets more than a certain percentage out of line - say, 5 to 10%. You could also set a regular date. For example, many people prefer tax time or the end of the year. To stick to this strategy, you'll need to be comfortable with the fact that investing is cyclical and all investments generally go up and down in value from time to time.

Forecast the Future

You could adjust your mix of investments to focus on what you think will do well in the future, or to cut back on what isn't working. Unless you have an infallible crystal ball, it's a trickier strategy than constant weighting. Even if you know when to cut back on or get out of one type of investment, are you sure you'll know when to go back in?

Mix It Up

You could also attempt some combination of strategies. For example, you could maintain your current asset allocation strategy with part of your portfolio. With another portion, you could try to take advantage of short term opportunities, or test specific areas that you and your financial professional think might benefit from a more active investing approach. By monitoring your portfolio, you can always return to your original allocation.

Another possibility is to set a bottom line for your portfolio: a minimum dollar amount below which it cannot fall. If you want to explore actively managed or aggressive investments, you can do so - as long as your overall portfolio stays above your bottom line. If the portfolio's value begins to drop toward that figure, you would switch to very conservative investments that protect that baseline amount. If you want to try unfamiliar asset classes and you've got a financial cushion, this strategy allows allocation shifts while helping to protect your core portfolio.

Points to Consider

- Keep an eye on how different types of assets react to market conditions. Part of fine-tuning your game plan might involve putting part of your money into investments that behave very differently from the ones you have now. Diversification can have two benefits. Owning investments that go up when others go down might help to either lower the overall risk of your portfolio or improve your chances of achieving your target rate of return. Asset allocation and diversification don't guarantee a profit or insure against a possible loss, of course. But you owe it to your portfolio to see whether there are specialized investments that might help balance out the ones you have.

- Be disciplined about sticking to whatever strategy you choose for monitoring your portfolio. If your game plan is to rebalance whenever your investments have been so successful that they alter your asset allocation, make sure you aren't tempted to simply coast and skip your review altogether. At a minimum, you should double-check with your financial professional if you're thinking about deviating from your strategy for maintaining your portfolio. After all, you probably had good reasons for your original decision.

- Check to see that the nature of what you've invested in hasn't changed. For example, you may have a mutual fund that's investing more overseas now than it was when you originally bought it. That could mean that your overall international exposure is higher now than when you first invested. This kind of "style drift" can affect the risk you're taking without your knowing it.

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"Someone's sitting in the shade today because someone planted a tree a long time ago."

–Warren Buffet

"Although it's easy to forget sometimes, a stock share is not a lottery ticket... it's part-ownership of a business."

–Peter Lynch

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- Some investments don't fit neatly into a stocks-bonds-cash asset allocation. You'll probably need help to figure out how hedge funds, real estate, private equity, and commodities might balance the risk and returns of the rest of your portfolio. And new investment products are being introduced all the time; you may need to see if any of them meet your needs better than what you have now.

Balance the Costs Against the Benefits of Rebalancing

Don't forget that too-frequent rebalancing can have adverse tax consequences for taxable accounts. Since you'll be paying capital gains taxes if you sell a stock that has appreciated, you'll want to check on whether you've held it for at least one year. If not, you may want to consider whether the benefits of selling immediately will outweigh the higher tax rate you'll pay on short-term gains. This doesn't affect accounts such as 401(k)s or IRAs, of course. In taxable accounts, you can avoid or minimize taxes in another way. Instead of selling your portfolio winners, simply invest additional money in asset classes that have been outpaced by others. Doing so can return your portfolio to its original mix.

You'll also want to think about transaction costs; make sure any changes are cost-effective. No matter what your strategy, work with your financial professional to keep your portfolio on track.

There is no guarantee that any investment strategy will be successful; all investing involves risk, including the possible loss of principal.