

The Morningstar Baby Boomer Retirement Guide

Portfolio strategies for those nearing retirement.

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Everyone wants a secure retirement. And during difficult economic times, it's critical that investors nearing retirement take a hard look at what they've saved—and determine whether those savings are sufficient.

We've created *The Morningstar Baby Boomer Retirement Guide* to help retirement-bound investors examine their portfolios and transition them into retirement.

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Planning Advice for Every Life Stage

By Christine Benz,
Director of Personal Finance

Ross Levin, founding principal of Minneapolis-based Accredited Investors and one of the top financial planners in the United States, understands that successful investing depends as much upon understanding his clients' personal needs and goals as it does on selecting appropriate investments for their portfolios. To help discuss the recent financial crisis and its impact on how individual investors should be managing their portfolios, I recently sat down with Ross for an interview.

Christine Benz: Many pre-retirees have been dealt a huge blow. How would you counsel them?

Ross Levin: Our guiding philosophy for those who are retiring is that once you're living off your portfolio, you need to have three years' worth of spending in cash or cashlike instruments. So if you're very close to retirement, you might have thought that, "Once I retire I'll raise the cash." For those people, it may make sense to put the monthly money that's going into the 401(k) into a risk-free option rather than raising cash in this environment. If they're three years away from retirement and they're putting maximum money into the 401(k), they may be able to raise \$40,000, \$60,000, or \$80,000 in cash over the next few years; that would allow the rest of the portfolio to do what it needs to do to build back.

The key thing for everyone who's thinking about retirement is where are the sources of income going to come from. And there have been a couple of misconceptions that have affected retirees. One is that they thought that their home was going

to be a great source of money. What we've found from our clients, and our clients are a little bit more affluent, is that when they retire, almost none of them have "bought down." They've either stayed in their homes longer than they thought they would or they've bought an equivalent place, and even though it's smaller they're not saving that much money on the buy.

The other thing that people misperceive is what their retirement is going to look like. Most people, and especially after this market, are going to either work a little bit longer or find a way to earn a little bit of money in retirement. And that is so significant. If you use a spending policy and let's say you spend 5% of your assets in retirement, and you could make \$20,000 working, that's equivalent to having \$400,000 of investment assets.

We also love to see those who are in the pre-retirement phase pay off their mortgages, even with interest rates as low as they are. The reason is that we're trying to drive down cash flow, or fixed costs, as much as we can because that creates the most flexibility for people. And what we have found in retirement is that clients need to be flexible because no matter how good your planning is, when clients feel poor, they don't spend as much money, and when they feel rich, they spend more than they're supposed to be spending. So you really want to manage the fixed costs. If the clients' fixed costs are low, then you can encourage them to do things that matter, like take vacations and visit the kids while they still have their health.

Benz: What advice do you have for those who are already retired?

Levin: I've been doing this since 1982, and I will say that not one of my clients' retirements looked the way they thought it was going to look. They lived longer than they thought, they lived shorter than they thought, they were healthier than they thought, they were less healthy than they thought they would be. Almost all of our clients died with too much money. One thing that we've been experiencing a lot lately is one healthy spouse and another spouse has Alzheimer's or ALS or something along those lines. That changes everything for everyone.

The other thing that we've noticed is that clients who are retired may not notice all the sources of investments they have. For example, we have clients who own a home up in Minnesota and a home down in Florida or Arizona. Once they are retired, they choose to only live in one place versus the other—maybe not right away but when they're 75 or 78. So suddenly we sell a home and those proceeds end up coming into the portfolio and that buys us time. One of the things that is really important for those who are retired is to recognize that your picture changes all the time. And again, it's one of the key reasons we stress flexibility.

So right now, immediate annuities are being bandied about in this kind of environment. And we're not big fans of immediate annuities because they are an answer to only two questions: How do I get the most income right now from my portfolio

and how do I know that I will always have some income? While these are important considerations, there are many other things to think about.

There are so many different things that can change during retirement. So we're big fans of making sure we stay flexible and we're also big fans of having experiences in the early years of retirement, because none of our clients, except for health-care expenditures, end up spending more in their 80s than they did in their 60s or 70s.

Of all the products that are out there, the one that's most intriguing to me is longevity insurance, which is not really good yet. But that's where you put some money away and it doesn't pay off until you're 80, and then it creates an income stream from age 80 for the rest of your life. The advantage of that kind of product is that it allows you to do planning with the rest of your assets using a fixed time horizon. So the major question that all of us have is how long we will live, and longevity insurance allows you to not worry so much about that. For much less cost than an immediate annuity, you can lock in a future income stream, which we think is really intriguing.

The other thing that we've become much more appreciative of is long-term care coverage. For our wealthy clients, from a financial standpoint, long-term care often doesn't make sense, but we're finding clients who want to own the policies even if it doesn't make sense because it allows them to spend more of their assets on other things that are more important, because they know they won't have to rely on their assets for long-term care. So

there are other reasons than financial why that kind of product can make sense.

Benz: You said that a lot of your clients died with too much money. How do you work against that?

Levin: The way we try to manage that is to ask, "What is it that you're spending your money on?" So when we see someone with too much money, we're not encouraging them to buy another Rolex. We're encouraging them to see whether there are things that are going to make a difference in their lives, things that they could have done with their money that they'll regret not doing.

So, for example, one of our clients, when they were 69, took their grown kids and their grandkids on a cruise together. The parents paid for it, and it was a big deal. And, by coincidence, unbeknownst to either of the parents, the mother was diagnosed with Alzheimer's about six months later. That cruise could not have happened at a different point in time.

Now they're worried about her care and what's going to happen, but that cruise got a tremendous amount of mileage for them. That experience with the whole family was such a wonderful thing, and should she pass away from Alzheimer's, the kids will always have that experience to talk about. If she passed away with another \$50,000 in the bank, would that have been more significant than what they did with that money?

This article appeared in the May 2009 issue of PracticalFinance.

Is Your Retirement Portfolio on Track?

By Morningstar Analysts

You will not work a day beyond your 55th birthday. And you plan to spend your retirement sipping lemonade on Capri and stiffening your neck by watching two weeks of tennis at Wimbledon. You have no intention of being a stay-at-home retiree.

You might not have much choice, though.

Most likely, Social Security and your pension or retirement plan will only partially subsidize your dreams. According to a recent Congressional Budget Office report, the average worker who retired at age 65 in 2008 will receive a benefit amounting only to about 40 percent of his preretirement earnings. Pensions or employer-sponsored retirement plans don't always cover the rest. Your own savings will more than likely make the difference between a retirement of jet-setting and one of sweater knitting.

So, in addition to monitoring your retirement portfolio and rebalancing as necessary, you should also calculate whether that portfolio is returning what it needs to be returning for your dream retirement. Here's how to do just that.

What Will Your Income Be?

The first step is determining what your regular retirement income will be, excluding your income from your own savings.

Request a Personal Earnings and Benefit Estimate Statement from the Social Security Administration (call 800-772-1213 or visit www.ssa.gov) to find out what you can expect each month from Social Security. Some people already receive this

yearly, but if you haven't seen it yet, submit the form (which you can download or request over the phone), and the Social Security Administration will send you a list of estimated benefits, including your monthly retirement check in today's dollars. (Remember that Social Security benefits rise with inflation.)

If your Social Security benefits seem too skimpy, they may be. Not reporting name changes, using a name other than the one on your Social Security card, or entering an incorrect Social Security number can lead to inaccurate benefits calculations. Troubleshoot by checking your benefits every few years.

Projecting what your retirement or pension plan will provide requires more legwork.

First, know the factors behind your expected future payments. Defined-benefit plans, such as a pension, often are linked to Social Security payments; consequently, a fatter Social Security benefit could mean a slimmer pension check.

Second, be persistent about seeking information. Some plans will update you regularly about your benefits as you near retirement. Others aren't as accommodating. Pester your employer's human-resources department for more information. If you get the run-around, turn to Washington. Call the Pension and Welfare Benefits Administration (800-998-7542) to find the Department of Labor office in your area. Also take a look at the Department of Labor's free Protect Your Pension pamphlet

(http://www.dol.gov/ebsa/Publications/protect_your_pension.html).

Finally, don't overlook those pensions owed you from brief employment stints or from companies that have merged out of existence or gone belly up. Check the Pension Search Directory (<https://search.pbgc.gov/mp/mp.aspx>) online to discover whether you're one of the thousands of people who haven't claimed forgotten pensions.

How Much More You'll Need

Compare your expected pension and Social Security income with the amount of income you think you'll need. Determine whether or not your current investments will cover the difference between the two figures. Remember that you probably won't need the entire lump sum of your retirement costs the minute you retire. More than likely, your investments will continue to grow during your retirement.

Many Web-based programs demand a major assumption: the return you expect from your investments. Since 1926, large-company stocks typically have returned about 11% per year, according to Ibbotson Associates' *Stocks, Bonds, Bills, and Inflation*. Investors retiring in 10 years or sooner should assume an even lower return—perhaps 7%-8% per year. It's always better to use conservative projections and be surprised on the upside.

Intermediate-term bonds have returned about 5% per year, on average, a fair return to use for your bond positions. For cash, use the 3.7% average return of Treasury bills.

Making It All Add Up

If your current portfolio isn't generating the type of return you'll need for your retirement, consider the following.

1. Rethink your retirement lifestyle. Separate your needs from your wants. One way to save big: Lower your housing costs. Moving from a \$300,000 home to a \$200,000 home not only means more cash in your pocket but probably lower upkeep expenses too.
2. If retirement is far enough away, get more aggressive. Trade some of your bond funds for conservative equity funds, or swap in more growth-stock exposure.
3. Put off retirement, or work part-time. People of full retirement age (65-67 depending on when you were born) can receive their full Social Security benefits, no matter what their earnings are. Even if you begin receiving Social Security before reaching full retirement age, you can earn up to a certain amount and still receive full benefits.
4. Save more now so you can spend more later. This is hard. It's also common sense. Americans have shockingly low savings rates, shockingly high debt, and an alarming tendency to overspend.
5. Don't forget to reevaluate your situation every three to five years.

A version of this article appeared on Morningstar.com on December 31, 2008.

Playing It Safe (but Not Too Safe for Retirement)

By Christine Benz,
Director of Personal Finance

It would be hard to blame someone for feeling a bit jealous of David and Cynthia Bennett, particularly in this era of reduced nest eggs and reduced expectations. They've both had good careers and have earned solid incomes. They've never spent extravagantly, instead saving assiduously to fund what they hoped would be an early retirement. The spreadsheet they sent me detailing their investments was carefully categorized by investment style, along with notations about whether they hold the asset in a company retirement plan, IRA, or taxable account.

Lately, however, the pair have been worrying that the market turmoil of the past year could derail their carefully laid plans. Cynthia, 60, has retired from her job as a teacher at a private school. David, also 60, is still working, but he had been planning to retire from his position as an executive at a health-care company in two years. With their investment portfolio shrinking from \$2.2 million to a still-robust \$1.8 million over the past year, David and Cynthia would like to be sure that their assets will last throughout what they hope will be a long retirement. They'd like to be able to spend what they need to maintain their active lifestyle, do some traveling during retirement, and spend time with their grandchildren. They'd also like to maintain a conservative portfolio mix for peace of mind. David and Cynthia have targeted a portfolio with a third each in stocks, bonds, and cash.

Separately, David and Cynthia would also like some help streamlining their portfolio. With more than 35 individual holdings, their record-keeping

is unwieldy and holding so many funds also mutes the gains from their top performers.

The Before Portfolio

The most notable thing about David and Cynthia's current portfolio, apart from its enviable size, is that it's far tamer than their targets for it. They currently have roughly 60% in cash, 30% in stocks and stock funds, and the remainder in bond funds. Most of their cash is in their taxable accounts. David says that he's currently investing 25% of his \$200,000 salary in his 401(k), his employee stock-purchase plan, and his traditional IRA. (He earns too much to contribute to a Roth IRA.)

David notes that he's been guilty of chasing mutual funds based on their short-term results, but I don't see a lot of evidence of that in the couple's current holdings. In fact, the vast majority of their mutual funds are Morningstar Fund Analyst Picks, which we select for the quality of management and strategy rather than short-term performance. The pair's equity and bond holdings skew heavily toward the Vanguard family of funds, giving their aggregate portfolio an average expense ratio of just 0.41%.

What non-Vanguard funds they own are among the best in their categories, including **Fidelity Contrafund** FCNTX, **T. Rowe Price Mid-Cap Growth** RPMGX, and **Artisan International** ARTIX. In addition, David and Cynthia hold five funds that Morningstar categorizes as "conservative allocation"—funds that own both stocks and bonds, such as **Oakmark Equity & Income** OAKBX and **Dodge & Cox Balanced** DODBX.

The pair also hold a small handful of individual stocks, including hard-hit names like **Citigroup C** and **Ford F** as well as the stock of David's employer, which lost more than half of its value last year. Overall, their portfolio is well diversified, but it skews slightly toward the value side of the Morningstar Style Box.

The After Portfolio

Based on scenarios I ran using Morningstar's Asset Allocator tool and T. Rowe Price's Retirement Income Calculator, I feel confident that David and Cynthia's portfolio will easily last throughout their retirement, even with a conservative asset mix and a higher spending rate than they're targeting. One of the key reasons is that David is expecting a pension payment of \$3,000 per month; that payout, combined with Social Security, will fulfill much of the couple's spending needs.

Because the Bennetts can count on so much steady income in retirement (another enviable position to be in), they can feel confident deploying some of their cash. As has been a theme in recent Portfolio Makeovers, I think bonds represent a happy medium for this couple. Given that they'll be deploying some of their cash from their taxable accounts and the fact that they're in the 28% tax bracket, I'd recommend adding to their municipal-bond funds. Vanguard Intermediate-Term Tax-Exempt and Vanguard Short-Term Tax-Exempt are both well-managed municipal-national funds that don't venture heavily into risky credits. If the Bennetts amass more than 1,000,000 with Vanguard, they'll qualify for the firm's Flagship

service, which entitles them to free financial-planning advice, among other perks.

To help fulfill the couple's secondary goal of streamlining, I'd cut their moderate-allocation funds, including Dodge & Cox Balanced, **T. Rowe Price Capital Appreciation PRWCX**, **Fidelity Balanced FBALX**, and Oakmark Equity & Income. Nearly all are terrific funds, but they're redundant with some of the pair's other holdings. I would also recommend that David and Cynthia sell some of their struggling individual stocks and book tax losses.

In addition, the pair should consider paying their mortgage down more aggressively than they have been. In fact, given their conservative asset mix, retiring that debt might provide a bigger bang for their buck than investing in bonds. They currently pay \$1,725 per month to service their mortgage and have 10 years left on their loan. I'd recommend ratcheting up that payment by at least a few hundred dollars a month. In so doing, they'll be on track to retire worry-free.

A version of this article appeared in the March 2009 issue of *Morningstar PracticalFinance*.

David and Cynthia's Portfolio: Before

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
Vanguard Total Stock Market Index VTSMX	★★★	LB	99,093	0.15
Vanguard 500 Index VFINX	★★★	LB	70,064	0.15
Fidelity Contrafund FCNTX	★★★★★	LG	67,017	0.89
Vanguard Inflation-Protected Securities VIPSX	★★★★	IB	51,095	0.2
Vanguard Total Bond Market Index VBMFX	★★★★★	CI	46,579	0.19
Dodge & Cox Income DODIX	★★★★	CI	41,215	0.44
Vanguard Wellington VVWELX	★★★★★	CA	37,830	0.29
Dodge & Cox Stock DODGX	★★★★	LV	37,532	0.52
Company Stock	★★★★★	Health	31,610	N/A
Vanguard S/T T/E VWSTX	★★★★	MS	28,282	0.15
Vanguard L/T T/E VMLTX	★★★★★	MS	27,970	0.15
Vanguard Mid Cap Index VIMSX	★★★	MB	18,505	0.21
Vanguard Primecap VPMCX	★★★★★	LG	18,473	0.43
Dodge & Cox International DODFX	★★★	FV	16,203	0.65
Cash	N/A	N/A	1,002,744	N/A
Total (including 23 holdings not shown)			1,837,553	

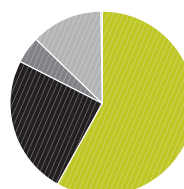
Super Sector Weighting (%)

Information	16.07
Service	49.85
Manufacturing	34.07

Top Three Sectors (%)

Health Care	20.39
Financial Svcs	16.23
Industrial Matls	12.40

Asset Allocation (%)

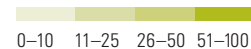


Cash	59.96
U.S. Stock	25.11
Foreign Stock	4.87
Bonds	12.80
Other	0.27

Equity Style (%)

Value Blend Growth

28	20	23	Large
6	7	9	Medium
2	2	2	Small



David and Cynthia's Portfolio: After

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
Vanguard Total Stock Market Index VTSMX	★★★	LB	216,695	0.15
Dodge & Cox Stock DODGX	★★★★	LV	150,000	0.52
Dodge & Cox Income DODIX	★★★★	CI	200,000	0.44
Dodge & Cox International DODFX	★★★	FV	50,000	0.65
Vanguard Inflation-Protected Securities VIPSX	★★★★	IB	100,000	0.2
Vanguard Total International Stock VGTIX	★★★	FB	50,000	0.15
Vanguard Short-Term Bond Index VBISX	★★★★★	CS	100,000	0.18
Vanguard Total Bond Market Index VBMFX	★★★★★	CI	100,000	0.19
Vanguard Primecap VPMCX	★★★★	LG	70,000	0.43
Loomis Sayles Bond LSBRX	★★★	MU	50,000	0.94
Vanguard L/T T-E VMLTX	★★★★★	MS	25,000	0.15
Vanguard S/T T-E VWSTX	★★★★	MS	75,000	0.15
Vanguard Int/T T-E VVITX	★★★★★	MI	50,000	0.15
Third Avenue Value TAVFX	★★★	WS	50,000	1.11
Vanguard Windsor II VWNFX	★★★	LV	19,248	0.32
Company Stock	★★★★★	Health	31,610	N/A
Cash	N/A	N/A	500,000	N/A
Total			1,837,553	

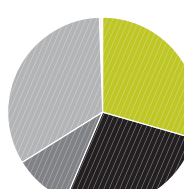
Super Sector Weighting (%)

Information	20.21
Service	50.00
Manufacturing	29.71

Top Three Sectors (%)

Health Care	22.38
Financial Svcs	16.75
Industrial Matls	11.16

Asset Allocation (%)



Cash	29.65
U.S. Stock	27.00
Foreign Stock	9.58
Bonds	33.29
Other	0.49

Equity Style (%)

Value Blend Growth

30	24	26	Large
6	4	5	Medium
2	1	1	Small



Categories

CI Intermediate Bond	LG Large Growth
CA Conservative Allocation	LV Large Value
CS Short-Term Bond	MB Mid Blend
FB Foreign Large Blend	MI Muni Intermediate
FV Foreign Large Value	MS Muni Short
IB Inflation-Protected Bond	MU Multisector
LB Large Blend	WS World Stock

Weighing Options for an Early Retirement

By Christine Benz,
Director of Personal Finance

“Can we afford to retire?”

That’s a question a lot of pre-retirees are asking themselves these days, and it’s one that Sue Jacobs recently posed to me in an e-mail request for a Portfolio Makeover.

At 59, Sue, a former community-college administrator, is already retired. Her husband Garrett, 58, is still working, but his position as a state employee currently involves a commute that takes up roughly three hours a day. Given all the time Garrett logs in the car and his limited time for leisure during the workweek, it’s no wonder this couple is seeking a lower-stress alternative to their current way of life.

Like many couples, however, this pair’s investment portfolio has taken a hit during the recent down market, making them question their one-time plan of retiring before they’re both 60. The value of the real estate they own has also declined. In addition to their primary residence, the couple owns some vacant land and a rental property, both of which they purchased a few years ago when the real estate market was booming. Sue and Garrett thought they might use the rental property as a vacation home once they retired, but are now questioning that strategy given that they currently have a tenant whose rent payments cover the mortgage.

The Before Portfolio

My first impression of the Jacobs’ portfolio is that it’s extraordinarily busy. Garrett’s 457 plan (the

equivalent of a 401(k) plan for government workers) is streamlined, holding just a moderate-allocation fund, **Nationwide Destination Moderate** NSDMX, as well as **Vanguard’s Small Cap Index** NAESX. But Sue’s Fidelity portfolio has more than 60 separate holdings, including 30 stock funds. Nearly all of Sue’s holdings are decent to good, but many of them overlap with one another. Sue says she would love to reduce her number of holdings, but she is concerned about selling some of her positions given the pounding they took last year and early in 2009.

The pair’s equity exposure is also on the light side, at just 45% of their portfolio. That might seem reasonable given their ages, but this couple expects that their combined pensions will cover more than half of their estimated \$6,000 monthly living expenses in retirement. Social Security, when they begin taking it, will also reduce their need to tap their portfolio for living expenses. Because they can rely on multiple income sources in retirement, they can safely hold a higher equity position than retirees who are relying solely or mostly on their portfolios.

The After Portfolio

The Jacobs haven’t rebalanced their portfolio since the market downturn, so I would start the makeover by bringing their portfolio back in line with their target equity allocation of 65%. In the process, I would streamline their equity holdings by increasing their weightings in stock funds that are truly best of breed and jettisoning those that are less impressive. On the list of keepers are

Fidelity Low-Priced Stock FLPSX, **Oakmark Equity & Income** OAKBX, and **Selected American Shares** SLADX. On the chopping block, I'd put **Fidelity Balanced** FBALX, which has had a manager change within the past year, as well as **Fidelity Canada** FICDX; a position in **Vanguard's Health Care exchange-traded fund** VHT also seems unnecessary.

Sue also has several individual bank stocks, both common stock and a preferred; together they're responsible for the portfolio's overweighting in that hard-hit sector. Given the couple's time horizon and the fact that these companies earn decent ratings from Morningstar's equity analysts, I'd be inclined to hang on.

To help accommodate a higher equity weighting, I'd strip some assets out of the couple's cash holdings. Yields are skimpy these days, and this couple's cash weighting is arguably too high given their modest income needs.

In terms of Sue's central question of whether she and Garrett can retire, I would say the answer is a qualified yes, largely because this couple can rely on pension income to defray more than half of their income needs. In the near term that means they'll be withdrawing less than 4% of their portfolio to cover their living expenses, and that number will go even lower once they begin taking Social Security.

That said, I'll admit that the potential for longevity and the still-shaky economy make me nervous

about anyone retiring early these days, particularly couples who could live another 30 years or more. For that reason, I'd recommend that Sue and Garrett consider taking additional steps to ensure that their portfolio will last throughout their retirement years. Garrett has the opportunity to work part-time in a position closer to home. Doing so is a personal decision, but working a few more years, if only on a part-time basis, will help reduce their portfolio withdrawals until Social Security kicks in. (In general, I'm also a believer in deferring Social Security as long as you possibly can, given how rapidly payments step up past the age of 62.) Continuing to work would also allow Garrett and Sue to prepay the mortgage on their primary residence, thereby bringing them into their retirement years debt-free. Finally, Sue and Garrett should also purchase long-term care insurance. They're in good health, but they have a history of Alzheimer's disease in their families. Having this insurance will keep long-term care costs from gobbling up their hard-earned nest egg.

A version of this article appeared in the July 2009 issue of *Morningstar PracticalFinance*.

Sue and Garrett's Portfolio: Before

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
Nationwide Destination Moderate NSDMX	★★★★	MA	55,809	0.90
Fidelity Government Income FGOVX	★★★★	GI	29,833	0.45
Oakmark Equity & Income OAKBX	★★★★★	MA	26,499	0.81
Fidelity Low-Priced Stock FLPSX	★★★★	MB	26,436	0.98
Fidelity Int. Muni Income FLTMX	★★★★★	MI	25,535	0.38
Fidelity Balanced FBALX	★★★★	MA	25,276	0.61
Fidelity Canada FICDX	★★★★★	FB	25,302	1.00
Fidelity Diversified International FDIVX	★★★★	FG	23,865	1.02
Loomis Sayles Bond LSBRX	★★★	MU	21,335	0.94
Vanguard Health Care ETF VHT	★★★	SH	18,197	0.20
Loomis Sayles Global Bond LSGLX	★★★★	IB	17,023	1.00
Associated Banc-Corp ASBC	★★★★	Bank	16,733	N/A
Fidelity Capital & Income FAGIX	★★★	HY	16,405	0.74
Fidelity Spartan Extended Mkt FSEMXX	★★★	MB	16,500	0.10
Cash	N/A	N/A	119,469	N/A
Total (including 43 holdings not shown)			674,481	

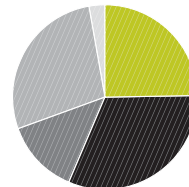
Super Sector Weighting (%)

Information	13.47
Service	55.05
Manufacturing	31.48

Top Three Sectors (%)

Financial Svcs	24.23
Health Care	16.64
Industrial Matls	11.74

Asset Allocation (%)

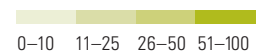


Cash	24.51
U.S. Stock	31.62
Foreign Stock	12.92
Bonds	27.48
Other	2.56

Equity Style (%)

Value Blend Growth

22	16	20	Large
12	7	8	
5	5	6	Small



Sue and Garrett's Portfolio: After

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
Selected American SLADX	3	LB	100,000	0.59
Fidelity Contrafund FCNTX	5	LG	67,055	0.94
Fidelity Intermediate Muni Income FLTMX	5	MI	50,000	0.38
Fidelity Short-Intermediate Muni Income FSTFX	4	MS	50,000	0.47
Nationwide Destination Moderate NSDMX	4	MA	55,809	0.90
Dreyfus Appreciation DGAGX	4	LB	45,000	0.96
Fidelity Low-Priced Stock FLPSX	4	MB	40,000	0.98
Oakmark Equity & Income OAKBX	5	MA	26,499	0.81
iShares Barclays TIPS Bond TIP	4	IP	25,000	0.20
PIMCO Commodity Real Return PCRRX	1	NR	25,000	0.99
Fidelity Growth Company FDGRX	4	LG	25,000	0.96
Fidelity Diversified International FDIVX	4	FG	24,168	1.02
Loomis Sayles Bond LSBRX	3	MU	20,000	0.94
Vanguard Small Cap Index NAESX	3	SB	14,835	0.23
Associated Banc-Corp ASBC	3	Banks	16,934	N/A
Wells Fargo Preferred Stock	N/A	Banks	14,520	N/A
US Bancorp USB	4	Banks	13,335	N/A
Oakmark International Small Cap OAKEX	3	FS	10,000	1.41
Treasury Bond	N/A	N/A	8,700	N/A
Cash	N/A	N/A	42,626	N/A
Total			674,481	

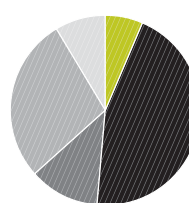
Super Sector Weighting (%)

Information	14.72
Service	51.86
Manufacturing	33.43

Top Three Sectors (%)

Financial Svcs	22.78
Energy	11.77
Consumer Goods	11.73

Asset Allocation (%)

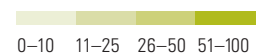


Cash	6.61
U.S. Stock	44.82
Foreign Stock	12.07
Bonds	28.06
Other	8.44

Equity Style (%)

Value Blend Growth

21	21	25	Large
9	6	8	
3	3	3	Small



Categories

FB Foreign Large Blend	MI Municipal Intermediate
FG Foreign Large Growth	MS Municipal Short
GI Intermediate Government	MU Multisector
HY High Yield Bond	NR Natural Resources
IB World Bond	IP Inflation-Protected Bond
LB Large Blend	SB Small Blend
MA Moderate Allocation	SH Health
MB Mid Blend	

Hitting a Pothole on the Road to Retirement

By Christine Benz,
Director of Personal Finance

Less than a year ago, Frank and Angela Greco (not their real names) thought they were cruising into the next great phase of their lives.

Frank, 57, was employed in a sales role in the financial-services industry, while Angela, 52, had recently returned to work full-time in an administrative position at an insurance company. With all three of their children grown, out of the house, and through college, the couple was starting to dream about their next steps: retirement in less than a decade, hopes for weddings and grandchildren, and finally taking the trips they had deferred while they were raising their kids and paying for school.

Less than one year and one bear market later, this couple has seen their dreams upended. Not only has their investment portfolio taken a hit, but Frank's company was shaken badly during the mortgage crisis and subsequent market meltdown. His former employer was acquired by a larger firm late last year, and Frank's position was eliminated along with thousands of others at his company. With it went Frank's low-six-figure paycheck, as well as the couple's sanguine attitude about the future.

The Grecos have reacted quickly to make the best of a bad situation. Angela is still employed full-time and has secured health-care insurance, once covered by Frank's company, through her employer. Frank negotiated a solid buyout package, amounting to one year's worth of salary, from his former company. He has also started a computer-consulting business.

His young business hasn't come close to supplanting the paychecks he earned from his former employer, though, and he and Angela are getting nervous about what the future holds. Angela's salary barely covers the Grecos' mortgage and property taxes, so the couple has been dipping into the proceeds from Frank's buyout package to pay for additional living expenses. Also, the couple would like advice on stabilizing their investment portfolio. Although they've recouped some lost ground over the past month and a half, their portfolio is currently worth \$800,000, down from \$1.2 million in late 2007.

The Before Portfolio

Taken together, the Grecos' portfolio has 50% in stocks and stock funds, another 25% in bonds, and the remainder in cash. Frank's 401(k) portfolio, the largest portion of the couple's assets, features a number of solid offerings from the American Funds group. Unfortunately, Frank also held a large position in the stock of his former employer in his 401(k) plan. He sold his shares in late 2008, but only after the stock had taken a drubbing. Angela's 401(k) plan, while a relatively small portion of their overall portfolio, is solid, featuring a stake in **T. Rowe Price Blue Chip Growth** TRBCX as well as a smaller stake in **T. Rowe Price Spectrum Income** RPSIX.

Frank has wisely used his IRA to shelter the bulk of their fixed-income investments, whose taxable income distributions make them a good fit within the IRA wrapper. Frank's IRA also holds a handful of income-producing stocks and smaller

positions in a global-stock fund and a commodity exchange-traded fund.

The pair also has another large asset: their house, which they estimate is worth \$600,000, even in the currently depressed real estate market. They purchased their five-bedroom home in a major metropolitan area in 1996, and roughly \$125,000 remains on their mortgage. Their payments on the house, including mortgage, taxes, and insurance, amount to \$2,600 per month.

The After Portfolio

I consider the Grecos' asset allocation to be pretty reasonable for this couple. The couple's cash should cover their needs for additional income for the next few years. That means they don't have an imminent need to move additional assets into fixed-income securities, and sticking with their current asset allocation will also give their equity portfolio a chance to rebound following the bear market.

I'm usually hesitant to recommend that someone leave their 401(k) assets in their old plan, largely because many 401(k) plans charge participants additional administrative costs above and beyond what the individual funds charge; rolling over 401(k) assets to an IRA also affords far more choices than are typically available with a 401(k). In Frank's case, my major hesitation is that his 401(k) plan doesn't include as many fixed-income choices as I'd like to see.

I would also suggest adjustments to Frank's IRA portfolio. **Loomis Sayles Bond** LSBRX, while a

solid fund, is too aggressive to serve as a core fixed-income holding; I would recommend reducing it and deploying some of those assets into a wide-ranging, highquality fund such as **Harbor Bond** HABDX.

I would also suggest that the Grecos give serious consideration to downsizing, and they say they have begun to do so. They note that they have been looking at condos and townhouses in their community and have found a few they like in the \$300,000 range. Were they to sell their home for \$600,000, they could purchase a smaller home outright, bank some cash, and get rid of their largest monthly outlay. (They would still have to pay real estate taxes and an assessment fee, but those two items would cost less than \$1,000 a month.) Not only does this step make financial sense, but it would also provide this couple with some much-needed peace of mind.

A version of this article appeared in the July 2009 issue of *Morningstar PracticalFinance*.

Frank and Angela's Portfolio: Before

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
T. Rowe Price Blue Chip Growth TRBCX	★★★★	LG	22,309	0.71
T. Rowe Price Growth Stock PRGFX	★★★★	LG	12,115	0.71
T. Rowe Price Spectrum Income RPSIX	★★★★	MU	59,248	0.70
American Funds Investment Co of Am AIVSX	★★★★	LV	174,526	0.57
American Funds Capital Income Build CAIBX	★★★	IH	169,843	0.55
American Funds EuroPacific Growth AEPGX	★★★★★	FB	96,342	0.74
American Funds High Income AHITX	★★★	LG	9,210	0.67
Loomis Sayles Bond LSBRX	★★★★	MU	93,500	0.94
ExxonMobil XOM	★★★★★	Energy	6,588	N/A
Kraft KFT	★★★★★	Consumer	11,235	N/A
Fidelity Worldwide FWWFX	★★★★	WS	23,500	1.19
iPath Dow Jones-AIG Commodity Index DJP	N/A	NR	35,000	0.75
Pfizer PFE	★★★★★	Drugs	21,090	—
Cash	N/A	N/A	115,900	N/A
Total			850,406	

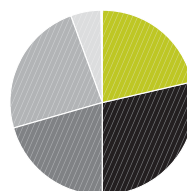
Super Sector Weighting (%)

Information	24.25
Service	32.99
Manufacturing	42.77

Top Three Sectors (%)

Consumer Svcs	15.42
Health Care	14.58
Telecom	10.94

Asset Allocation (%)



Cash	21.49
U.S. Stock	28.70
Foreign Stock	20.45
Bonds	23.92
Other	5.45

Equity Style (%)

	Value	Blend	Growth	
	35	30	27	Large
	4	2	2	Medium
	0	0	0	Small

0-10 11-25 26-50 51-100

Frank and Angela's Portfolio: After

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
T. Rowe Price Blue Chip Growth TRBCX	★★★★	LG	34,424	0.71
T. Rowe Price Spectrum Income RPSIX	★★★★	MU	59,248	0.70
Harbor Bond HABDX	★★★★★	CI	100,000	0.55
Vanguard Total Bond Market Index VBVMFX	★★★★	CI	75,000	0.20
Vanguard High-Yield Corporate VWEHX	★★★★	HY	25,000	0.27
Vanguard Total Stock Market Index VTSMX	★★★	LB	109,601	0.16
Vanguard Equity-Income VEIPX	★★★★	LV	100,000	0.30
Dodge & Cox International DODFX	N/A		100,000	—
Loomis Sayles Bond LSBRX	★★★★	MU	32,320	0.94
Royce Total Return RYTRX	★★★★	SV	25,000	1.12
ExxonMobil XOM	★★★★★	Energy	6,588	N/A
Kraft KFT	★★★★★	Consumer	11,235	N/A
iPath Dow Jones-AIG Commodity Index DJP	N/A	NR	35,000	0.75
Pfizer PFE	★★★★★	Drugs	21,090	N/A
Cash	N/A	N/A	115,900	N/A
Total			850,406	

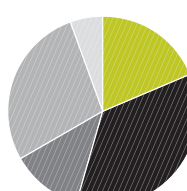
Super Sector Weighting (%)

Information	16.66
Service	42.65
Manufacturing	40.69

Top Three Sectors (%)

Health Care	16.89
Financial Svcs	15.56
Industrial Matls	13.06

Asset Allocation (%)



Cash	18.69
U.S. Stock	35.79
Foreign Stock	12.20
Bonds	27.85
Other	5.46

Equity Style (%)

	Value	Blend	Growth	
	33	25	19	Large
	7	5	5	Medium
	2	2	1	Small

0-10 11-25 26-50 51-100

Categories

CI Intermediate Bond	LV Large Value
FB Foreign Large Blend	MU Multisector
HY High-Yield Bond	NR Natural Resources
IH World Allocation	SV Small Value
LG Large Growth	WS World Stock



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