Online Sources Can Help You Put the Pieces Together

The Portfolio Management Puzzle

by Amy B. Crane

Putting retirement, college savings and taxable mutual fund accounts together to create a coherent portfolio can look more complicated than completing a 1,000-piece jigsaw puzzle. But if you want to control your portfolio, rather than having it control you, it's a job best done with a plan and a regular timetable.

The pile of financial statements many investors face can seem downright overwhelming. Many two-income families with kids have a couple of 401(k) accounts and IRAs for the grownups as well as Coverdell Savings Accounts, Section 529 plans and maybe even Uniform Gifts to Minors Act accounts for the kids. Many retirees and single people also face the difficulty of dealing with multiple investment accounts.

Dealing with this confusing mishmash of accounts isn't a lost cause: By using tried-and-true portfolio management techniques, you can take control of your portfolio. You need to formulate lifetime goals, then set up an investment plan to reach them. Savings discipline and portfolio management is what gets you from goal to reality.

"Keeping your portfolio on the rails isn't that difficult when you know where you're going and have the right tools," says Dennis Genord, NAIC's manager of mutual fund education. "Start out by picking quality mutual funds, then monitor them a couple of times a year to see if they're still up to your standards. Look at all your investments — not just your funds — and make sure your portfolio is balanced for risk and reward."

Where To Begin

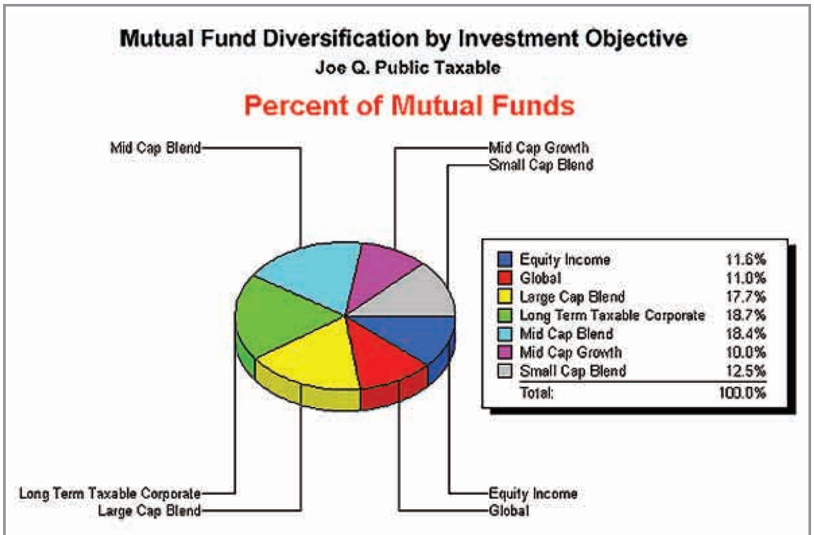
To make sense of what you already own, sit down and look at all of your investments. If your portfolio is loaded online or in investing or personal finance software, so much the better. If not, don't fret, but you need to figure out what you own in stocks, bonds, stock and bond funds, money market funds and cash.

If you're using software or an online portfolio and are up-to-date, you can figure out where you are quickly. Portfolio Record Keeper, NAIC's official record-keeping software, shows the breakdown of mutual funds by report and graph based on investment objective *(see graphic, below)*. Knowing the diversification of funds by investment objective provides valuable information in analyzing risk and return goals, says Matt Willms of QUANT IX SOFTWARE, Inc., which publishes PRK. You can look at the diversification of your entire stock, bond and fund portfolio.

If you're not using PRK or another program such as Quicken or MS Money, you might find helpful *SmartMoney* magazine's One Asset Allocation System at http://cs.smartmoney.com/oneasset. Asset allocation is the practice of dividing up your investments into different investing vehicles *(see "Financial Planner," April 2001* Better Investing: *www.better-investing.org/articles/bi/104/1156)*.

Standard & Poor's Financial Communications Center has 20 calculators (http://fc.standardandpoors.com/htdocs/corp_v2/calculators_edups.html), including an asset allocation calculator to help you figure out your desired allocations based on your age, present financial situation and risk tolerances. The current asset allocation calculator helps you figure out your situation today.

FinanCenter has planning tools that focus on financial planning, asset allocation and college and retirement savings (www.financenter.com/products/planners). The calculators are meant to answer specific questions, such as "Should I sell my funds now and invest the money elsewhere?" and "When will I recover my costs?"



Breaking Down Mutual Funds. As shown here using Portfolio Record Keeper software, investors can view their mutual fund holdings by investment objective.

The Nuts and Bolts of Asset Allocation

Christine Povenmire, a Certified Financial Planner in Columbus, Ohio, believes that the most important decision for most people is to determine their desired breakdown between stocks and bonds. Brian Lewis, a National Investors Association director and a director with the Puget Sound Chapter in Seattle, tracks his allocation of mutual funds, individual stocks and other assets in a model he created using Excel software. "I slice and dice things multiple ways, striving to stay within defined percentages in terms of international versus domestic; actively managed versus index; the asset classes of stocks, bonds, real estate, precious metals and cash; growth versus value; sector diversification; and a target yield for the overall portfolio."

Remember that asset allocation is one tool in your portfolio management toolbox. Keeping tabs on the quality of your mutual funds and other investments is vital as well.

Maintaining Portfolio Quality

With more than 14,000 mutual funds available for investment, picking the best ones can be daunting. NAIC's mutual fund tools aid investors in finding, comparing and tracking quality funds. These include the Check List, Comparison Guide and Trend Report for stock and bond funds.

The Trend Report allows you to track a fund you own over time, examining key variables to see whether anything has changed. "I use the Trend Report to screen for changes in my funds," says Gary Simms, a director with the Heart of Illinois Chapter in Peoria, Ill. "Management is a biggie in actively managed funds. I ask why if there are changes going on in this category.

"I look at what has happened to a comparable index fund in terms of performance. If the index has gone into negative returns and my current stock fund has had a similar return, I'm not too concerned. If the index fund went up 10 percent and my stock fund went down 5 percent, I ask why."

Red Flags

When checking up on your portfolio, look for the following red flags:

▲ **Change in fund management:** "If a solo manager of an actively managed fund leaves, that's a huge warning sign," says Zoe Brunson, a fund analyst with Standard & Poor's. "If one manager in a team leaves, that's a warning but isn't as significant. At the larger corporate level, changes in top management, a merger with another fund company or an acquisition can lead to changes in overall investment philosophy and style."

▲ **High costs or substantial jump in costs:** "Keeping costs low is vital because fund costs cut directly into your returns," Genord says. "Compare your results to those of low-cost index funds; if your fund isn't beating the index fund, why pay more? Also pay attention to loads and marketing and distribution fees."

▲ **Changes in fund asset flow:** "Pay attention when a fund starts to get more assets," Brunson says. "An increase in assets can impact a small-cap fund, where you're wondering if the fund will stay true to its style or become more broad. In some funds asset size matters, while in others it doesn't — it depends on the manager's style."

▲ **High turnover or a rise in the turnover rate:** "If you're (holding funds) in a taxable account, portfolio turnover is important," Povenmire says, because taxes can cut into your returns, especially if you're in a higher bracket.

▲ **Major changes in the fund's sector profile or top holdings:** "In the portfolio, if a fund manager is making significant changes to his top 10 holdings ... is that a call on the future direction of the market or a style shift?" Brunson asks. "Big changes in a portfolio can lead to more volatility."

Portfolio Weeding and Feeding

If you're analyzing your portfolio for the first time or haven't checked it in a while, you may not be as diversified as you thought. A common mistake many investors make is to be overly concentrated in one area, Brunson says. "You may own three funds, but if all of them are large-cap growth funds, you're not diversified," she says.

Rebalancing can protect investors to a degree from down markets, but employing this practice takes discipline, Povenmire says. She follows Morningstar's advice to rebalance a portfolio every 18 months based on asset allocation guidelines.

It pays to be tax-savvy when you sell. Simms uses PRK to track the cost basis of his funds so that when he does rebalance, he can select specific lots to sell to minimize his tax liabilities. He checks his portfolio in December so that he can take advantage of any tax savings before the end of the year.

For Lewis, weeding and feeding his portfolio boils down to a few simple rules: "Don't own too many mutual funds — keep life fairly simple. Spend a fair amount of effort upfront to buy funds that you'll be comfortable holding for years. Review your asset allocation annually, and look at your funds in the context of everything you own, including retirement accounts." ■

Amy B. Crane, a freelance writer based in Erie, Pa., writes about mutual funds for BI. *An NAIC member for six years, Amy is the author of the second edition of* The NAIC Mutual Fund Handbook. *She was a founder of the NAIC Online Investor's School and has taught stock and fund investing classes.*