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## How much does asset allocation matter to retirees?

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By Editor Test      Wed, Apr 18, 2012

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*"Financial advisers will be of greater help to their clients if they focus on a broad array of tools – including working longer, controlling spending, and taking out a reverse mortgage," says a new paper from the Center for Retirement Research at Boston College.*

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Who was likelier to live a long life: the fitness nut who lifted weights and gobbled fish oil capsules while sailing on the Titanic's maiden trip, or the couch potato who lost his boarding pass and missed the ill-fated voyage entirely?

To put the question another way: why do investors spend a Titanic amount of time tinkering with their portfolios' asset allocations when other factors—like choosing a retirement age—are bigger determinants of financial well-being in retirement?

That's the question that three scholars at the Center for Retirement Research at Boston College raise—and answer—in a new article transparently entitled, "How important is asset allocation to financial security in retirement?"

Working longer can overcome sub-par investment performance. That's not to say, however, that the authors recommend working longer and ignoring asset allocation during their accumulation years.

"I would never recommend working a day longer than necessary!" said Anthony Webb, who wrote the paper with CRR director Alicia Munnell and Natalia Orlova. In an email to RIJ, he wrote, "The idea was to give a sense of the relative power of the various levers, not to suggest that some of the levers should remain unused."

To prove their point, the authors evaluated the weight of several factors in determining whether a hypothetical person will reach his or her retirement savings goal and (based on the 4% rule) achieve an adequate retirement income.

To weigh the impact of allocation, they simulated the effect of moving from a conservative portfolio to a hypothetically ideal equity portfolio returning 6.2% a year. They compared that with the effects of other factors: the age when people started saving, the age when they decided to retire, whether or not they tapped home equity in retirement, and how fast they spent their savings.

The higher rate of return turned out to be the weakest factor. For the average person, the best way to maximize financial wellbeing in retirement is to take Social Security at 67 instead of 62, the paper suggested. Achieving the 6.2% return would allow that person to retire at age 66.5—just six months earlier. In comparison, buying a reverse mortgage could reduce retirement age by 18 months and thrift during retirement could reduce it by a year.

"Given the relative unimportance of asset allocations," the paper concluded, "financial advisers will be of

greater help to their clients if they focus on a broad array of tools – including working longer, controlling spending, and taking out a reverse mortgage.”

The effect of asset allocation was weakest for less affluent households, because rate of return matters less when there are fewer assets. But the overall results were similar for people of all wealth levels and risk appetites.

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