Year-End Portfolio Review – Rebalancing Your Assets

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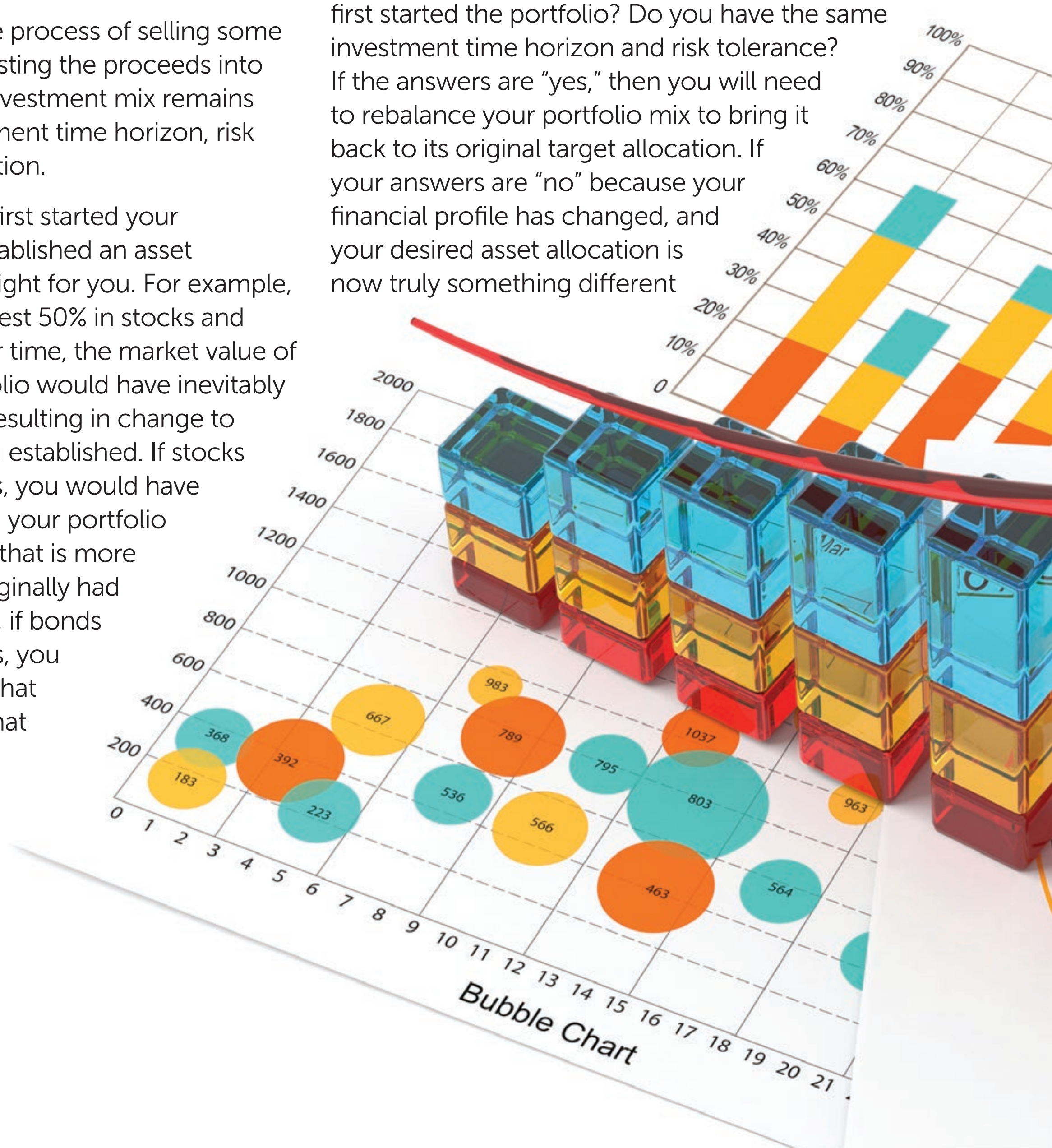
A Wild and Epic year! 2020 has certainly been a very challenging year, to say it kindly. It will likely go down as a wild and epic year. Investors have experienced dramatic market swings and portfolio volatility, testing our nerves and pushing us to question our investment strategies. With the new year beginning, it is a great time to check ourselves in the mirror and reassess our investment strategies. And if a reset to our investment portfolio is needed, a great way to bring about that change is through rebalancing.

What is Rebalancing and Why Rebalance?

Simply put, rebalancing is the process of selling some investment assets and reinvesting the proceeds into others, to ensure that your investment mix remains aligned to your goals, investment time horizon, risk tolerance, and financial situation.

Chances are that when you first started your investment portfolio, you established an asset allocation strategy that was right for you. For example, you may have decided to invest 50% in stocks and 50% in bonds. However, over time, the market value of each asset within your portfolio would have inevitably produced different returns, resulting in change to the overall asset mix that you established. If stocks performed better than bonds, you would have more in stocks than bonds in your portfolio mix, representing a portfolio that is more aggressive than what you originally had intended. On the other hand, if bonds performed better than stocks, you now would have a portfolio that is more conservative than what you had targeted. This result is called “asset allocation drift.” As a result of “asset allocation drift,” you must look in the mirror and reassess what you want out of the portfolio.

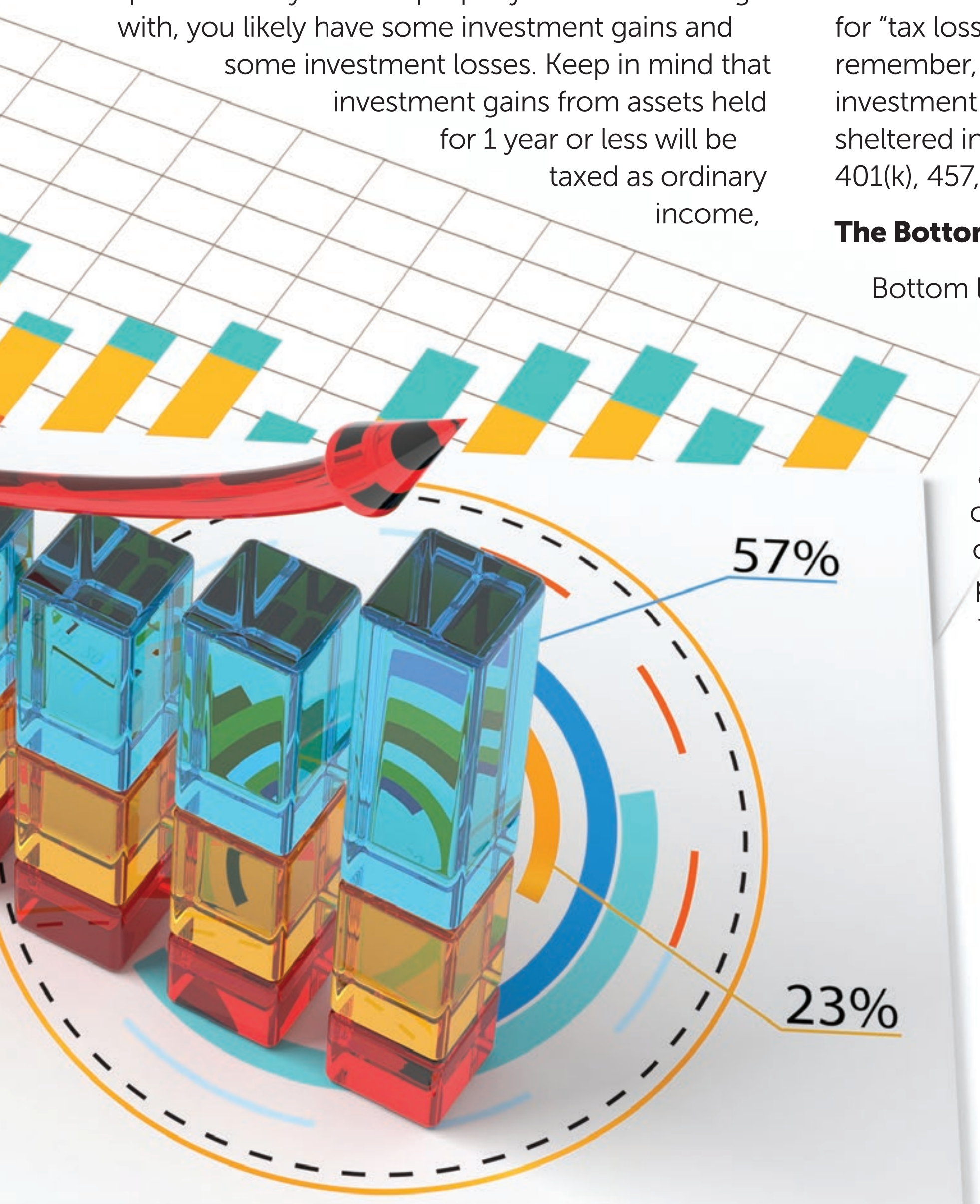
Do you have the same goal in mind as when you first started the portfolio? Do you have the same investment time horizon and risk tolerance? If the answers are “yes,” then you will need to rebalance your portfolio mix to bring it back to its original target allocation. If your answers are “no” because your financial profile has changed, and your desired asset allocation is now truly something different



than your original asset allocation, you will still need to ensure that your actual portfolio mix represents your desired portfolio mix – and this may, or may not, require rebalancing, depending on how far off your current portfolio mix is from your desired portfolio mix.

Tax Considerations When Rebalancing Outside Your Retirement Accounts

When rebalancing your investment portfolio that is in a taxable account (outside your tax-sheltered retirement savings accounts), you will also need to consider tax implications. If you were properly diversified to begin with, you likely have some investment gains and some investment losses. Keep in mind that investment gains from assets held for 1 year or less will be taxed as ordinary income, while investment gains from assets held for more than 1 year will be taxed at a more favorable capital gains rate. However, investment losses can help you reduce taxes by offsetting gains. If you have more capital losses than gains, you can use up to $3,000 a year to offset ordinary income and carry over the rest to future years. This process of offsetting investment gains with investment losses for tax benefit is referred to as "tax loss harvesting." This strategy transforms an investment that has lost money into a "tax benefit" and helps you to reduce taxes now and in the future. So, a volatile market with many ups and downs that creates investment winners and losers can be an opportunity for "tax loss harvesting" and produce tax benefits. But remember, "tax loss harvesting" only applies to taxable investment portfolios – not your retirement tax-sheltered investment portfolios, such as 403(b), 401(k), 457, or IRA.



The Bottom Line

Bottom line, when you rebalance, the goal is to align your investment portfolio with your desired asset allocation – whether that is your original target allocation or something totally different. The desired asset allocation should be based on your current financial circumstances (not the ones from when you first started your portfolio), including your goals, investment time horizon, and risk tolerance. And given the likely gyrations that you experienced in your portfolio during the 2020, and the new year beginning, there's no better time than now to rebalance. By rebalancing, you can ensure that your portfolio correctly represents what you want. If you are interested in examining how rebalancing may benefit you, please give us a call at **800.986.6222**.