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### **Fidelity Adjusts Target Funds' Sights**

Fidelity announced this week that it was overhauling its Freedom funds, which are designed to offer a one-stop retirement saving and spending solution for investors, in an attempt to provide better long-term performance. Going forward, the funds will feature a heavier emphasis on stocks than bonds, and will delay the "glide path" from equity-heavy to bond-heavy allocations until later in life.

The changes reflect Fidelity's best thinking on the future of the markets and investing for retirement—in short, the firm believes that planning for retirement will become more difficult, going so far as to say that investors may need to reset their expectations for income in retirement or hold off on retiring until they are older. Fidelity also recommends that younger investors start a retirement account as soon as possible and that all investors contribute as much as possible—sound advice.

These findings are based on extensive research into several areas, from savings, spending and life expectancy trends among its investors, to expected returns for various asset classes, to running computer simulations of how different portfolio configurations might perform over time. While the firm believes that its ultimate target of a 20%/80% split between equities and fixed-income and cash is still appropriate, it thinks that returns for bonds and U.S. stocks over the next 20 years will be lower than their historical averages. In the end, Fidelity determined that it needed to rework its target-date funds to help investors achieve better outcomes (i.e., not outliving their savings).

As mentioned above, the first part of the adjustment is to increase exposure to stocks, both domestic and international, while reducing exposure to fixed-income holdings, particularly shorter-duration bonds and cash. The example Fidelity gave was its Freedom 2020 fund (designed for investors who plan to retire in the year 2020), which will move from a 53% allocation to equities (39% domestic, 14% foreign), 39% in bonds and 8% in cash to 61% equities (43% domestic, 18% foreign), 32% in bonds and 7% in cash.

The firm has also changed when and how its target date funds' allocations will begin to shift to their final stages. The Freedom

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funds, which use an investor's expected retirement year to determine allocations, will start with a 90% equity and 10% fixed-income split and stay there until about age 45 (approximately 20–25 years from retirement), when they will begin to increase exposure to fixed income and reduce exposure to stocks. Fidelity says age 84 is the ideal target age for the final, more conservative allocation to go into effect (assuming a life expectancy of 93 years).

It might seem surprising that Fidelity settled on 84 years old, when presumably investors will be a decade or more into retirement, as the final allocation stop. This is where the retirement savings element comes into play—Fidelity says that most investors do not contribute enough to their retirement accounts to justify moving to a more conservative strategy any earlier, and the greater return potential of a heavier weight to equities is needed to ensure protection against inflation and a sufficient level of income to last through retirement.

The changes that Fidelity is making reflect the shifting nature of saving for retirement, given longer life expectancies and the current low yields on fixed-income investments and cash. While we believe that custom, diversified portfolios of active managers serve investors better than one-size-fits-all "solutions," Fidelity's research is intriguing and reflects the evolution of thought on how investors should plan for the future.

### **Vanguard Aims at Volatility**

Following a growing trend in the mutual fund and ETF industry, Vanguard has announced its intention to open a low volatility fund, Vanguard Global Minimum Volatility, which it says should be available at some point before the end of 2013. Funds like this are designed to weather market downturns with fewer losses, but also will not typically gain as much as the market when it is humming along.

Vanguard's fund will be focused on stocks, investing about half of its assets in the U.S. and the other half in international markets. It will also hedge against foreign currencies in an attempt to diminish the potential volatility of its overseas investments.

Global Minimum Volatility is slated to be managed by a team of three managers from Vanguard's in-house Equity Investment Group, James Troyer, James Stetler and Michael Roach. The trio co-manages Vanguard's Strategic Equity and Strategic Small-Cap Equity funds, and also manages a portion of assets of Vanguard's Energy, Equity Income, Explorer, Growth and Income, Market Neutral, Morgan Growth, U.S. Value and Windsor II funds. They represent Vanguard's go-to crew for quantitatively managed equity portfolios.

The new fund is currently planned to have Investor and Admiral shares, which will charge 0.30% and 0.20% in expenses, respectively. The minimum initial investment for the Investor shares will be \$3,000; for the Admiral shares, it will be \$50,000.

As a category, low volatility funds have really only begun to hit the market over the last two years, so their efficacy in avoiding a big drop in the markets, like we saw during the financial crisis from 2007 to 2009 or when the tech market bubble burst in 2000, has yet to be determined. There is certainly an appetite for this kind of investment, as the ETFs in the space have already garnered \$11 billion in assets. It will be interesting to see the reception for Vanguard's entry to the space and how it stacks up to its competitors.

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