

LIFE-CYCLE INVESTING

## The way to go in financial planning?

As you advance through different life stages, you will be looking to protect the nest egg that you have built up over the years.



LIFE-CYCLE investing is an investment concept that has gained popularity in the United States and United Kingdom. In the US, life-cycle portfolios are the fastest-growing type of retirement or pension fund for employees.

In this article, **NORMAN WU**, senior director of UOB Asset Management, explores the concept of life-cycle investing in the context of financial planning.

Life-cycle funds are generally balanced portfolios where the asset allocation is adjusted automatically between global equities and global bonds to suit an investor's life stage. Compared to global bonds, global equities generally yield higher returns but carries a higher risk. Against this background, the rationale behind the concept of life-cycle investing seems logical:

- When you are young and have an income, you can generally afford to take more risks to get more returns. You are building up your nest egg. Hence, a larger portion of your wealth can be invested in equities.

- As you grow older, your risk appetite will gradually drop and your investment portfolio should increasingly change from more equities to more bonds. In other words, as you advance through different life stages, you will be looking to protect the nest egg that you have built up over the years.

This shift in asset allocation over different stages of a life cycle to increasingly lower risks in investments provides some protection from extremely negative outcomes nearer the retirement age, when an investor is generally less able to withstand investment risks and shocks to his nest egg.

The idea is that your money should work harder in the earlier years and become more stable in the later years of your life.

In addition, investing in a life-cycle fund may help investors instill some investment discipline for the long-term. For example, setting aside some funds for financial goals such as the children's education and personal retirement.

In Singapore, there are several life-cycle funds with different time horizons.

Nonetheless, there are some concerns raised over this investing concept.

One is that life-cycle asset allocation should consider other factors such as the size of an investor's overall investment portfolio in addition to the number of years till his retirement. For example, you can continue to take more risks if you have a larger investment portfolio, compared to other investors of the same age with a smaller portfolio.

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Another point is that life-cycle funds may eliminate upside potential, depending on the market cycle and an investor's life stage.

For instance, the life-cycle portfolio of an investor who is in his late life stage will largely consist of bonds, and this could deprive the investor of the upside potential should investment markets go up.

However, such analyses are typically based on historical returns and may not represent future performance.

The jury is still out on the life-cycle investing concept. Like any other investments, life-cycle investing is not a one-size-fits-all solution. Ultimately, an investor needs to consider his own needs and goals.

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