Ea$y Money – Wealth: Investments

What it is: All sources of retirement income are important to your overall retirement security. When you invest, you are putting your dollars at risk or taking a chance. The outcome can be a loss or gain. Potential return on an investment can be current income (such as interest, dividends, or rent) and/or capital gains (in which an investment has increased or appreciated in value). The combination of income and capital gains is the total return from an investment. (source: Growing Your Nest Egg: Risk and Return)

How it works: Investment and savings choices should be based on your comfort level with risk and knowledge of the potential return. Low risk investments offer the comfort of knowing your contributions will not be lost. The risk associated with these choices is inflation. As the price of goods and services increases, the return on the investments may be too low. To grow the account you may have to make higher deposits over time. During retirement you will need to use both earnings and principle to cover living expenses. The assets in this investment choice may be depleted more rapidly.

Stocks and other investments have the potential for greater gain resulting in the potential for sufficient income to pay retirement expenses. These investments also have financial risks and the impact of the associated risks can be loss of income flow and loss of principle. At the high risk end of investment options are choices that can have financial risk, market risk, and marketability risk.

Why it matters: Asset Allocation and Diversification are the division of your money among different risk levels or within a specific risk level. In simple terms, it means not putting all your retirement eggs in one basket.

Who should care? Investment portfolios are not static—they change over time. When you are young, you can have a greater allocation in high risk choices that might give you a higher return allowing your balance to grow more quickly. A typical allocation for young investors can be 80 percent in stocks and other high risk/return investments, 20 percent in bonds. An older investor who has fewer years remaining in the workforce and less time before distributions will occur could have 50 percent in stocks and other high risk/return investments, 20 percent in bonds, and 30 percent in cash accounts. Financial firms have attempted to make this reallocation of assets simple by introducing target date funds. Investors indicate the year they are most likely to retire when they open the account and adjustments are automatically made as the target date nears.

NOTE: This information is provided as an educational service and is not intended as, nor should it be considered legal advice but provides general information.

For more information:

- Iowa State University Extension and Outreach Money Blogs tips, http://blogs.extension.iastate.edu/moneytips/
- Iowa State University Extension and Outreach publication PM1821, *Growing Your Nest Egg: Risk and Return-- Retirement: Secure Your Future*
- Iowa State University Extension and Outreach Human Sciences website at www.extension.iastate.edu/humansciences/
- Internal Revenue Service http://www.efile.com/tax-service/tax-calculator/tax-brackets/