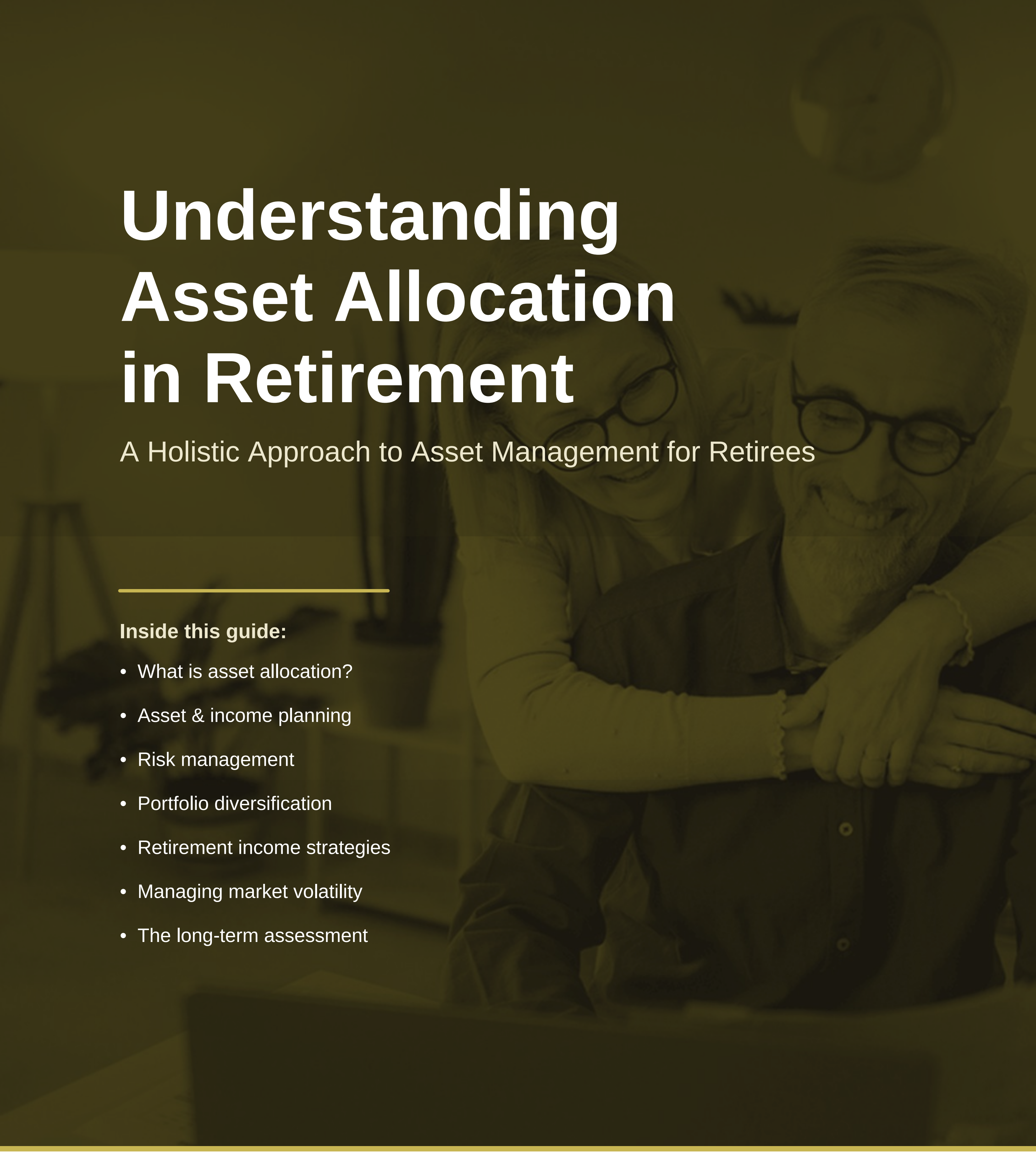

Understanding Asset Allocation in Retirement

A Holistic Approach to Asset Management for Retirees

Inside this guide:

- What is asset allocation?
- Asset & income planning
- Risk management
- Portfolio diversification
- Retirement income strategies
- Managing market volatility
- The long-term assessment

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Welcome

Saving for retirement and spending in retirement are two different disciplines. During your working years, time was your ally: paychecks kept arriving, downturns were buying opportunities, and the goal was simply growth. In retirement, the equation changes. Your portfolio must now produce income, keep pace with decades of inflation, and survive market declines it can no longer “wait out” with new contributions.

Asset allocation — how your savings are divided among stocks, bonds, cash, and other investments — is the single decision that most shapes whether your money lasts. This guide from Commonwealth Guardians explains how allocation works, how it should evolve for retirees, and how to build a portfolio designed to fund your life rather than simply beat a benchmark.

> **How to use this guide**
> Read it straight through, or jump to the section that matches your question. Along the way, planning notes highlight where personalized advice tends to add the most value. When you are ready, your Commonwealth Guardians advisor can review your current allocation against your income needs, risk capacity, and time horizon.

Contents

SECTION 1

What Is Asset Allocation?

Asset allocation is the way your portfolio is divided among the major categories of investments — called **asset classes** — each of which behaves differently. Decades of research suggest that this mix, far more than picking individual stocks or timing the market, drives the vast majority of a portfolio's long-term behavior: its growth, its income, and how sharply it falls in bad markets.

The major asset classes

Asset class	Primary role	Main risk
Stocks (equities)	Long-term growth; inflation protection	Short-term price declines
Bonds (fixed income)	Income; stability; dampen stock swings	Interest-rate and credit risk
Cash & equivalents	Liquidity; near-term spending; safety	Loses purchasing power over time
Real assets / alternatives	Diversification; inflation hedge	Complexity; sometimes illiquid

Why allocation changes in retirement

- **You are now a net seller.** Withdrawals replace contributions, so losses early in retirement do more damage than the same losses did while you were saving.
- **Your horizon is long — but layered.** A 65-year-old couple may need income for 30 years. Money needed next year and money needed in 2050 should not be invested the same way.
- **Risk changes meaning.** The relevant risk is no longer a bad quarter — it is running out of money, or being forced to cut your lifestyle.

There is no one “right” mix

Old rules of thumb — like “own your age in bonds” — ignore what matters most: your spending needs, guaranteed income sources, health, taxes, and legacy goals. Two 68-year-olds with identical portfolios may need very different allocations because their lives are different.

> **Planning note**
>
> Your allocation should be an output of your retirement income plan — not a number picked from a questionnaire. The right starting question is not “what's my risk tolerance?” but “what does this portfolio need to do for me, and by when?”

SECTION 2

Asset & Income Planning

Holistic asset management starts by connecting what you **own** to what you will **spend**. Before choosing investments, map both sides of your personal balance sheet.

Step 1: Inventory your income sources

- **Guaranteed income:** Social Security, pensions, and annuity payments — reliable, often inflation-adjusted, and payable for life.
- **Portfolio income:** Withdrawals, dividends, and interest from IRAs, 401(k)s, and taxable accounts — flexible but market-dependent.
- **Other sources:** Part-time work, rental income, business interests, or expected inheritances.

Step 2: Map your spending

- **Essential expenses:** Housing, food, healthcare, insurance, taxes — the non-negotiables.
- **Lifestyle expenses:** Travel, hobbies, gifts, dining — important, but flexible in a bad year.
- **Irregular and later-life costs:** Home repairs, new vehicles, and potential long-term care.

Step 3: Find your income gap

Subtract guaranteed income from essential spending. The result — your **income gap** — is the job your portfolio must do every year. The size and certainty of that gap, more than any risk questionnaire, should shape how much of your portfolio sits in stable assets versus growth assets.

Don't forget account location

Where you hold assets matters almost as much as what you hold. Placing tax-inefficient assets (like taxable bonds) in tax-deferred accounts, and tax-efficient growth assets in Roth or taxable accounts, can add meaningful after-tax return without adding risk.

> **Planning note**
>
> A retiree whose guaranteed income covers 90% of essential expenses can afford a very different portfolio than one whose guaranteed income covers 40%. Same age, same savings — very different right answers.

SECTION 3

Risk Management

In retirement, “risk” is not one thing. Managing it well means naming each risk and assigning the right tool to each — because the tool that fixes one risk often worsens another.

The five risks every retiree faces

Risk	What it is	Primary defenses
Market risk	Portfolio declines from falling markets	Diversification; cash reserves; right-sized stock exposure
Sequence-of-returns risk	Poor returns early in retirement while withdrawing	Cash/bond buffer; flexible spending; withdrawal guardrails
Inflation risk	Rising costs eroding purchasing power over decades	Adequate stock exposure; inflation-linked income (e.g., Social Security COLAs)
Longevity risk	Outliving your money over a 25–35 year retirement	Lifetime income sources; sustainable withdrawal rates
Health & long-term care risk	Large, unpredictable late-life expenses	Insurance; earmarked reserves; HSA assets

Sequence risk deserves special attention

Two retirees can earn the same average return over 25 years and end up in completely different places, purely because of the **order** in which returns arrive. Deep losses in the first five years of retirement — while withdrawals are being taken — can permanently impair a portfolio, because shares sold in a downturn never recover. This is why the years just before and after retirement are called the “fragile decade.”

Risk tolerance vs. risk capacity

- **Tolerance** is emotional: how much decline you can watch without abandoning the plan.
- **Capacity** is financial: how much decline your plan can absorb without cutting essential spending.
- Your allocation must respect the **lower** of the two. A portfolio you abandon in a panic was never the right portfolio.

> **Planning note**
>
> The goal is not to eliminate risk — a “riskless” portfolio quietly loses to inflation for 30 years. The goal is to take only the risks you are paid to take, in amounts your plan can survive.

SECTION 4

Portfolio Diversification

Diversification means owning investments that don't all rise and fall together, so no single holding, sector, or bad year can sink the plan. It is the closest thing investing offers to a free lunch — reducing risk without necessarily reducing expected return.

Diversify on multiple levels

- **Across asset classes:** Stocks, bonds, cash, and real assets respond differently to growth, recession, and inflation.
- **Within stocks:** Large and small companies, U.S. and international markets, and a spread of sectors — not concentrated in one theme or a former employer's shares.
- **Within bonds:** Varied maturities and credit quality; short-term bonds for stability, intermediate for income.
- **Across tax treatments:** Taxable, tax-deferred, and Roth accounts give you flexibility in which “bucket” funds each year's income.

Common diversification mistakes

- **Concentration by attachment:** Holding a large legacy position in one stock — often an old employer — because of loyalty or embedded capital gains.
- **Overlap in disguise:** Owning five funds that all hold the same large U.S. companies is one bet, not five.
- **Home bias:** Ignoring international markets concentrates your retirement in one country's economy.
- **Chasing winners:** Piling into whatever led the last decade — leadership rotates, and it usually rotates after you arrive.

Rebalancing: diversification's maintenance plan

Markets constantly push your mix off target — a strong stock run can quietly turn a 60/40 portfolio into 70/30, right when risk matters most. Rebalancing on a schedule (or when an asset class drifts beyond a set band) systematically trims what has run up and replenishes what has lagged — enforcing “sell high, buy low” without forecasting.

> **Planning note**
> In retirement, rebalancing can double as your paycheck: withdrawals are taken from whichever asset class is overweight, keeping the portfolio on target while raising cash for spending.

SECTION 5

Retirement Income Strategies

Once the allocation is set, the next question is how to turn a portfolio into a reliable monthly paycheck. Three proven frameworks — often blended — do most of the work.

Strategy 1: The bucket approach

- **Bucket 1 — Now (years 1–2):** Cash and equivalents covering near-term spending, so market swings never touch this year's groceries.
- **Bucket 2 — Soon (years 3–10):** High-quality bonds providing income and refilling Bucket 1.
- **Bucket 3 — Later (years 10+):** Stocks and growth assets with time to ride out full market cycles and outpace inflation.

Strategy 2: The floor-and-upside approach

Secure your essential expenses with guaranteed income — Social Security (often maximized by delayed claiming), pensions, and possibly an income annuity — creating a “floor” no market can break. The remaining portfolio can then invest for growth with genuine confidence, because a bad market threatens vacations, not the mortgage.

Strategy 3: Total-return with guardrails

Keep one diversified portfolio and withdraw a sustainable percentage — commonly starting near 4%, adjusted for your age and market conditions — with pre-agreed “guardrails”: modest spending trims after bad markets, raises after strong ones. Flexibility is the price of a higher starting income.

Sequence withdrawals for taxes

Which account you tap each year — taxable, tax-deferred, or Roth — changes lifetime taxes substantially. Coordinating withdrawals with Social Security timing, Roth conversions in low-income years, required minimum distributions (beginning at age 73, rising to 75 for those born in 1960 or later), and Medicare premium thresholds is where income planning and tax planning meet.

> **Planning note**
>
> Most of our clients end up with a blend: a guaranteed floor under essentials, a short-term buffer for calm, and a growth engine for the long haul. The right proportions depend on your income gap from Section 2.

SECTION 6

Managing Market Volatility

Market declines are not a flaw in the plan — they are a feature of markets the plan must already expect. Historically, temporary declines of 10% or more have occurred every year or two, and bear markets of 20% or more roughly every several years. A retirement plan that only works in calm markets is not a plan.

Build the plan before the storm

- **Hold a spending buffer.** One to two years of withdrawals in cash and several more in short-term bonds means downturns don't force stock sales at the bottom.
- **Right-size stock exposure in advance.** If a 30% stock decline would break your plan — or your resolve — the time to adjust is before it happens, not during.
- **Write down the playbook.** An investment policy that pre-decides what you will do in a decline replaces adrenaline with process.

What to do during a downturn

- **Spend from the buffer,** not from depressed stocks.
- **Rebalance into weakness** on your schedule — buying stocks at lower prices is how recoveries are captured.
- **Harvest tax losses** in taxable accounts and consider Roth conversions while values (and the resulting tax) are temporarily lower.
- **Trim flexible spending modestly** if the decline is deep — small, early adjustments prevent large, forced ones later.

The most expensive mistake

Selling out after a decline and waiting for “things to feel safe” converts a temporary loss into a permanent one. Markets historically recover before the news does, and missing just a handful of the strongest rebound days can lower long-term returns dramatically. The investors who suffer most in volatile markets are usually those who react most.

> **Planning note**
> Volatility is the toll the market charges for long-term returns. Our job is to structure your portfolio so you never have to pay that toll at the worst possible moment.

SECTION 7

The Long-Term Assessment

Asset allocation is not a one-time decision. Your plan should be assessed on a regular rhythm — annually in depth, and whenever life changes — so the portfolio keeps matching the life it funds.

Review on a schedule

- **Quarterly:** A light check — cash buffer level, any rebalancing bands breached, withdrawals on track.
- **Annually:** A full assessment — spending vs. plan, allocation vs. targets, tax opportunities (conversions, loss harvesting, charitable giving), and updated income projections.
- **At life events:** Health changes, loss of a spouse, a home sale, an inheritance, or a move — each can change the right allocation overnight.

Let the allocation evolve with your retirement

Research increasingly supports a **dynamic** approach rather than a straight-line reduction in stocks. Many retirees benefit from de-risking into the “fragile decade” around retirement, then allowing equity exposure to drift gradually upward as sequence risk fades and the remaining horizon (and legacy goals) justify growth. Later life often shifts priorities again — toward simplicity, guaranteed income, and long-term care readiness.

Measure what matters

- **Funded status:** Are projected assets and income still sufficient for projected spending — with margin?
- **Sustainable withdrawal rate:** Is this year's spending consistent with the plan lasting to your planning horizon?
- **After-tax, after-inflation results:** Benchmarks are trivia; purchasing power is the scoreboard.
- **Plan resilience:** Would the plan still work after a 25% market decline, higher inflation, or a long-term care event?

> **Planning note**
>
> The best question at every annual review is not “did we beat the market?” but “is the plan still on track — and what changed in your life this year?”

SECTION 8

Your Next Step

A portfolio built years ago — for a different market, a different tax code, and a different stage of your life — deserves a fresh look. An hour spent pressure-testing your allocation against your actual income needs is one of the highest-value exercises in retirement planning.

An allocation checklist

- List every account and holding in one place — including old 401(k)s and concentrated stock positions.
- Calculate your true overall stock/bond/cash mix across all accounts combined.
- Map guaranteed income against essential expenses to find your income gap.
- Confirm you hold 1–2 years of planned withdrawals in cash or short-term reserves.
- Check each account's asset location for tax efficiency.
- Stress-test the plan against a major market decline and a long-term care event.
- Set a rebalancing rule — calendar-based or band-based — and write it down.

Let's review your allocation

Commonwealth Guardians provides comprehensive portfolio and retirement income reviews. As independent advisors, we are free to recommend the strategy that serves you best — not a product list. Contact us to schedule a complimentary allocation review.