

# 30 Days to Financial Fitness

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**Featured in this booklet**

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▧ To change one's life, start immediately, do it  
flamboyantly, no exceptions. ▧

William James

James, a psychologist, was right on the money with the “immediate” part. But does enacting lasting change in your life need to be momentous or flamboyant? Nah.

Instead, most people who have achieved big goals will tell you they've done so little by little, one small step at a time. The person who lost 30 pounds did so by walking an extra mile a day and putting skim milk in her coffee instead of half and half. The author who wrote a best-selling first novel got it done by writing a few pages a night, after he had put his kids to bed.

The same is true when you're aiming to achieve your financial goals. The broad goals of funding a comfortable retirement, paying for college, or buying a first home can seem daunting, particularly when you think through the dollar amounts that you'll need to save. But if you break these broad goals down into smaller, more manageable tasks, and tackle them one at a time, you can begin to make real progress toward your goals.

Through this guide, I'll coach you on completing one financial-planning task per day, with an eye toward getting in the best financial shape of your life. I'll discuss how to invest for goals that are close at hand, how to build a retirement portfolio, and how to make sure your investments are on track from year to year.



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# Week 1

## Get Organized

Before you can make a difference in your finances, it's important to lay the proper groundwork: You need to get organized and have a good view of your financial picture. Helping you get there will be the focus of the first week's tips.

### Day 1

#### Start tracking your expenses

Degree of Difficulty: Easy

Let's start with a fairly easy task: beginning to track your spending habits. There are Web sites and financial software programs devoted to helping keep close tabs on your household's cash flows, but tracking your expenses can be as simple as jotting them down whenever you find yourself opening your wallet or writing a check. Group your expenses into one of two main categories: fixed (i.e., spending that doesn't change and you can't do without) and discretionary. Get a start with this simple PDF worksheet, available at [morningstar.com/goto/budget](http://morningstar.com/goto/budget).

Plan to keep track of your expenses for at least a month; that way you can identify patterns in your spending and zero in on your problem spots. Examining cash flows in this way is the first step in creating a budget that aligns with your priorities and the realities of your life. You may also find that tracking your expenditures will have the salutary effect of causing you to think twice before spending money on things you don't necessarily need.

### Day 2

#### Check your credit report

Degree of Difficulty: Easy

One of the best ways to get your arms around your household's financial health is to check your credit report. You may be tempted to hop on [freecreditreport.com](http://freecreditreport.com) (I know, the catchy lyrics are ringing in my ears, too), but the best place to go for free, comprehensive credit information is [annualcreditreport.com](http://annualcreditreport.com).

Through this site, you can obtain data about your credit history from the three major credit reporting firms: Experian, TransUnion, and Equifax. You won't be able to see your actual credit score—the agencies still charge for this—but you will be able to make sure that your credit report doesn't include any mistakes that could harm your ability to obtain credit at a decent rate in the future. Checking these reports is also a good way to ensure that identity thieves haven't obtained credit in your name. You can obtain free basic reports from the three credit reporters once a year.

I recently obtained my credit reports using [annualcreditreport.com](http://annualcreditreport.com), and found the site to be quite easy to use, so long as I was able to ignore the steady barrage of upsells for paid credit services. After inputting some basic information about myself, including my address, birth date, and Social Security number, I was transferred to the first of the three agencies' sites, where I then answered a few additional security questions.

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TransUnion, Experian, and Equifax display credit information in varying ways, but all three show you the names and some basic payment history related to your credit accounts, both now and in the past. The sites also show you whether you've been late with your payments or have had some other type of problem with a creditor. Eyeball all three credit agencies' reports to ensure that your credit report syncs up with reality, and print each of these reports for further perusal. If you see any information that appears to be incorrect, go to the [Federal Trade Commission's Web site](#) for guidance on filing a formal dispute.

### Day 3

#### Set up a bill-paying system

Degree of Difficulty: Easy to Moderate

If you already have a rock-solid system for paying your bills—perhaps you use your bank's online bill-paying system or that of a third-party provider like Quicken—you get the day off. (Your degree of difficulty for today? Definitely easy!)

But if your desk is awash in random bills, or worse yet, if you checked your credit report and saw a history of late payments, it's time to put a formal bill-paying system in place.

I'm a big believer in online banking. Not only does it cut down on the amount of paperwork you'll be responsible for shredding or filing once it comes into your house, but reducing your reliance on snail mail also helps lessen your vulnerability to identity theft.

Most financial institutions offer online banking these days, and it's usually free of charge and pretty intuitive. Simply head to your bank's website for instructions on how to implement such a program.

Before you opt to bank and pay your bills online, it's essential that your home computing system has up-to-date security protection, including firewalls, antivirus software, and spyware protection. Also make sure that you've downloaded the latest version of your web browser, as it will include the most current encryption technology. Finally, take care when selecting passwords. As always, a combination of letters and numbers will help prevent someone from being able to guess your password. (If you keep a separate document with all of your account numbers, user names, and passwords—and I'll tackle that step on another day—be sure to password-protect it!)

If you don't use an electronic bill-paying system, I'd also recommend logging any incoming bills on to a calendar as soon as you receive them. Plan to mail upcoming bills at least seven days before their due dates. Note the date on which the bill should be mailed, who you owe, and how much. When you sit down to pay your bills for the coming week or month, this approach will help to ensure that nothing falls through the cracks.

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## Day 4

### Take stock of assets and liabilities

Degree of Difficulty: Moderate

Now that you're getting warmed up, it's time to move on to the key task that will show you how you're doing financially: checking up on your net worth.

If you keep good records and don't have many financial accounts, enumerating your assets and liabilities will be pretty straightforward and shouldn't be time-consuming. You've got more work ahead of you if your records and portfolio are in a state of sprawl, but think of this as your impetus to streamline and get organized.

To document your assets, simply retrieve your latest account balances and estimate the worth of your personal possessions, including real estate. (Be realistic! Unfortunately, it's probably not worth what it was a few years ago.) On the other side of the ledger, record any debts you owe, including your mortgage; student, home equity, or auto loans; and credit card balances. Subtract your liabilities from your assets and you're looking at your net worth. To streamline the process, you can use Morningstar's Net Worth Worksheet, available at [morningstar.com/goto/networth](http://morningstar.com/goto/networth).

If your net worth is negative or barely positive, you've got your work cut out for you. Creating and sticking to a budget should be a key priority in the year ahead. And even if your net worth is comfortably positive, you should still spend

time digging into the numbers. Is most of your money tied up in a single asset, such as company stock or your house? If so, a key goal should be to diversify your financial assets in the year ahead. Do you have an adequate amount—six months' worth of living expenses at a minimum—stashed in an emergency fund? If you don't, prioritize building up your position in ultrasafe (and unfortunately in today's environment, ultra-low-yielding) investments before investing in longer-term assets like stocks.

## Day 5

### Create a master directory

Degree of Difficulty: Easy

"OK, now that's depressing." That was how one of my single friends responded when I suggested that she document all of her financial accounts in case something should happen to her. But the fact is, singletons aren't the only ones who should be documenting their financial assets. And compiling a master directory with essential account information is apt to be just as valuable for you to rely on while you're alive and well as it would be to your loved ones should something happen to you.

If you've recently completed a net worth statement (Day 4), you've gone through the process of sorting through your various accounts and are in a perfect position to create a master directory. But even if you haven't, creating a straightforward document of your financial accounts shouldn't take long at all.

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Your master directory can be either electronic or paper. In it, include financial assets such as bank, mutual fund, and brokerage accounts; company-retirement plan and pension fund details; real estate holdings; and business interests. Alongside or beneath each account name, include account numbers, URLs, passwords, key contacts, and phone numbers. Include similar details for debts you owe and insurance policies. For guidance, check out Morningstar's Master Directory Worksheet, available at [morningstar.com/goto/directory](http://morningstar.com/goto/directory)

Given the amount of valuable personal information it includes, your master directory would obviously be manna for identity thieves. So once you've created such a document, it's essential that you take steps to keep it safe. If it's a physical document, keep it under lock and key in your house. If you've created an electronic file, password-protect it using a hard-to-guess password. Then alert a trusted loved one of this document's existence as well as details about how to gain access to it in a pinch.

Plan to keep your document up to date, ideally as part of an annual financial checkup.

## **Day 6**

### **Update your filing system**

Degree of Difficulty: Moderate

If organizing your home office is one of your goals, start by revisiting what paperwork you're saving. In my experience, most people save

way more financial documents than they need to, and they do so out of habit more than anything else. Your shredder is your friend.

To help determine what to save and what to toss, think about which documents would be a true headache to replace if you needed to. (Do you like waiting in line or on hold with government offices? Didn't think so.) Social Security cards, car titles, and marriage, birth, death, and divorce documents, as well as the past seven years' worth of tax returns, fall into this group and therefore should either be stored offsite, in a safe-deposit box, or in an at-home fireproof box.

You'll also want to keep a running file at home to hold any documents related to the current year's tax return. For documents that relate to your household's ongoing financial management—including bills—ask yourself whether managing those accounts online and retrieving information on an as-needed basis might not be more efficient than stashing all that financial paperwork at home. The answer is probably yes. And as I noted in Day 3's installment, transacting online also courts less identity-theft risk than does allowing personal information to pass through the mail. Before deciding to go paperless, check up on the thoroughness and ease of use of your financial-service providers' online information systems.

As you sort through your paperwork, you're apt to have come up with a big discard pile. I like to play it safe and shred anything with my name and address on it—if it has more personal information than that, such as an account number, put it

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in the “definitely shred” pile. Among the discard items that can go straight into the recycling bin are annual reports and prospectuses, warranties and manuals for stuff you no longer own, and marketing literature that accompanies bank and investment statements.

### **Day 7**

#### **Check up on your insurance coverage**

Degree of Difficulty: Easy

Week 1 has been all about getting organized and finding your financial baselines—checking up on what assets you have now. But how good a job have you done protecting those assets? Use today to check up on the adequacy of your insurance coverage.

It goes without saying that everyone should obtain the best medical coverage they can afford, as well as coverage for real property such as home and autos. But if you’re still working, your biggest asset is apt to be your own ability to earn a paycheck. One of the best ways to protect that income stream is to obtain disability coverage, which is designed to send you a percentage of your income if you become disabled. Your employer may offer cost-effective coverage; sign up to pay for it using aftertax dollars, meaning that your benefits will be tax-free.

Working people with dependents should also have life insurance, and stay-at-home parents should investigate it, too. Term life insurance is going to be the most cost-effective way to go; if your insurance agent recommends a more permanent

type of policy, make sure you thoroughly understand the reasons why he or she finds this type of coverage preferable to a term policy.

Finally, look into obtaining an umbrella policy, or personal liability insurance.

These policies usually sit on top of your homeowners and auto policies, and cover you in case you’re sued for an accident that occurs on your property. If you have contractors, house cleaners, babysitters, or dogwalkers on your property—and everyone does at one point in time or another—an umbrella policy is a must.

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# Week 2

## Build on Your Strategy

Week 1 focused on getting organized and checking up on how you're doing financially. Over Week 2, I'll share tips to help you invest for short- and intermediate-term goals, and in future weeks I'll discuss constructing a portfolio geared toward long-term goals such as retirement.

### Day 8

#### Check your emergency fund

Degree of Difficulty: Easy

Before you begin saving for your goals, it's crucial that you build an emergency fund—a basket of ultra-liquid investments that you can tap in case you lose your job or confront an unanticipated car or home repair.

The typical rule of thumb is to keep three to six months' worth of living expenses in your emergency fund. But perhaps a better way to decide how much to store in cash is to think about how much of a cushion you'd like to have in case you lost your job. If you go through that exercise, you're apt to conclude that three months' worth of living expenses is nowhere near enough. But don't go overboard with your cash hoard, either. After all, interest rates on money market accounts and funds are about as low as they can go, so being too conservative has an opportunity cost. As you calculate your emergency-fund requirement, don't use your real spending patterns to set your living expenses. Think about how much you could get by on in a pinch, excluding dinners out, house cleaners, and vacations.

Compare your emergency-fund target with the amount you have saved in CDs, money market accounts and funds, and checking and savings accounts. Don't include cash holdings that appear in long-term mutual funds. Building your emergency fund up to your target level should trump saving and investing for other goals, such as retirement or college.

### Day 9

#### Get maximum mileage from cash holdings

Degree of Difficulty: Easy to Moderate

Everyone needs cash, both for an emergency fund and to cover upcoming expenses such as your property tax bill or college tuition. Keeping that money safe is important, but the big drawback is that yields on CDs, money market accounts, and other cashlike vehicles are low.

When shopping for the best yields on cash investments, the list of don'ts is almost as long as the list of dos. While it's smart to be opportunistic and scout around for the best yields, my key piece of advice is not to get too cute. Safety is key for this portion of your portfolio, so resist the temptation to park some or all of your assets into a "cashlike" vehicle that offers a higher yield but also a greater risk to your principal. Ultrashort-bond funds and bank-loan funds are a great example of why you shouldn't chase yield: Although some investors had used funds in both categories as a higher-yielding money market substitute, the average fund in these groups lost 8% and 30%, respectively, in 2008's flight to quality.



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CDs usually offer higher yields than money market funds and other cashlike vehicles, and they offer FDIC protection to boot. The big drawback is that you're locking yourself into a fixed rate. Money market fund managers, by contrast, can swap into new, higher-yielding securities if rates move up. My book, *30-Minute Money Solutions*, includes a list of some of the best, most dependable money market funds. Not surprisingly, nearly all of them have very low expense ratios, which in turn enables them to deliver above-average payouts relative to their peers without taking on a lot of extra risk.

If you're in a high tax bracket, another option for your cash is a municipal money market fund, whose income will be free of federal income tax.

#### **Day 10**

##### **Map out your financial goals**

Degree of Difficulty: Easy

Most of us have a running list of financial goals: whether it's paying off our homes, financing college for the kids and grandkids, funding a comfortable retirement, or paying for here-and-now creature comforts like vacations and new cars. Few people, however, take time to document their goals and quantify exactly how much they'll cost, even though that step is key to helping you set your household's financial priorities. It's also pretty easy.

Today, take a moment to jot down your goals. Group them into one of three bands: short-term goals (goals you'd like to achieve in five or

fewer years), intermediate-term goals (five to 15 years from now), and long-term goals (15 years or more in the future). Once you've done that, prioritize your goals within each time frame. Be sure to include debt retirement on your list of goals.

The next step is to estimate exactly how much those goals will cost you. If your goal is close at hand—such as buying a car next summer—quantifying it is straightforward. But if it's a goal that's further in the future or one that you'll pay for over several years, the calculation may be more complicated and you'll also have to factor in inflation. Morningstar Investment Research Center has two calculators especially designed to help you plan for retirement savings and college savings goals. Both tools can be found within the Portfolio tab of Morningstar Investment Research Center.

#### **Day 11**

##### **Invest for mid-term goals**

Degree of Difficulty: Moderate

Yes, current yields on truly safe investments like CDs and money market funds are shrimpy. But if you're building an emergency fund or saving for a goal that's close at hand, the risks of venturing beyond ultra-safe investments outweigh any extra yield you're able to pick up. It's boring, but you'll need to rely on your own savings, rather than investment returns, to do the heavy lifting in these instances.

But what if you're saving for an intermediate-term goal and don't expect to need the money for

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another couple of years or even more? In that case, you can tolerate modest fluctuations in the value of your principal. A core intermediate-term bond fund can fit the bill, and a few of my favorites include Dodge & Cox Income (DODIX), Harbor Bond (HABDX), and Metropolitan West Total Return Bond (MWTRX).

If you have an even longer time horizon—anywhere between five and 10 years—you can hold stocks as well as bonds. Some of my favorite mutual funds that combine stocks and bonds together are Vanguard Wellington (VWELX) and Dodge & Cox Balanced (DODBX). If you hold one of these funds and are getting close to needing money to fund your goal, you can transition the assets to cash for safe-keeping.

### **Day 12**

#### **Allocate capital like a pro**

Degree of Difficulty: Moderate to Difficult

It's day 12 on the road to financial fitness, so let's take on a more rigorous—but extremely important—task: allocating your household's financial capital. Although Morningstar focuses on helping you invest in stocks, funds, and ETFs, the reality is that investors' highest-impact decisions precede the decision to invest in the market. Do you save enough? And when you have extra cash on hand, do you pay down debt, invest, or do a little of both?

When it comes to the latter decision, it's helpful to think of yourself as a business owner, steering

your cash toward the opportunity that is apt to offer you the best return on your capital.

Paying off debt—even more benign types of debt like mortgage debt or student loans—offers you a knowable return on your money—always a good thing. If you're receiving a tax break on your interest, as is the case with mortgage interest and some student loans, you'll get less of a bang out of paying off the note prematurely. But in my experience, many mortgage-holders overestimate the benefits of their tax-deductible interest.

Investing in the market offers a potentially higher rate of return, but the hitch is that return, unlike paying off debt, isn't guaranteed. When forecasting returns for your investments, be conservative. You can plug in your own return expectations, but I usually use a 6% to 7% rate of return for equities, a 4% return for bonds, and a 2% return for cash. Based on the asset mix of your portfolio, you can then forecast a ballpark return for it. Armed with that information, you can then determine whether investing in the market or paying off debt is the best return on your dough.

### **Day 13**

#### **Explore options for college savings**

Degree of Difficulty: Moderate

As with retirement investments, the college-savings landscape is far more cluttered and complicated

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than it needs to be, with myriad vehicles competing for investors' attention.

Due to their generous contribution limits and the potential for tax-free withdrawals, section 529 college-savings plans have emerged as the vehicle of choice for families looking to sock away a substantial sum for school. I'm happy to report that 529s have generally improved substantially over the past few years, with costs coming down and the quality of investment options going up. Some investors, however, would like to invest for their kids outside the confines of a dedicated college-savings vehicle like a 529 or Coverdell Education Savings Account. If that's you, you have a couple of options.

Setting up a UGMA/UTMA account is one simple way to go, but the drawbacks probably outweigh the pluses, in my view. The assets become the property of the child once he or she reaches the age of majority (varies by state but usually age 18 or 21), when some young people may not yet be equipped to make good financial decisions. And if you're pretty sure your child is college-bound, you should know that those UGMA/UTMA assets will work against your child in financial aid calculations.

For those reasons, investors looking to save outside of a dedicated college-funding vehicle like a 529 or Coverdell should consider saving for their kids in one of a couple of ways. The first would be simply to hold tax-efficient investments, such as low-turnover exchange-traded and index funds, indi-

vidual non-dividend-paying stocks, municipal bonds/funds, or tax-managed mutual funds, within the confines of the parents' taxable account. Withdrawals won't be tax-free, as is the case with qualified withdrawals from a Coverdell or 529, but it's straightforward and investors gain the added flexibility to use the money outside of college expenses, penalty free, if the need arises.

Another option is to use a Roth IRA to save for your kids. In a Roth, you can pull out your contributions (not your gains), tax-free, at any time and for any reason, making the vehicle a great multi-tasker for those looking to save for retirement and college at once. The key drawbacks? Roth contribution limits are pretty low—currently \$5,000 for those under 50 and \$6,000 for those over—and pulling money out for your kids leaves less money at work for retirement. Test your knowledge of various college saving plans with Course 210: How to Invest for College, one of our Portfolio Investment courses located on the Help & Education tab of Morningstar Investment Research Center.

#### **Day 14**

#### **Don't be too aggressive when saving for college**

Degree of Difficulty: Moderate

The bear market of 2008 forced many retirees and pre-retirees to recalibrate their plans and, in some cases, to make meaningful reductions in the quality of their day-to-day lives. But it also had a huge impact on another, much younger group: college-bound students.

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Unfortunately, many college-savings plans, including several professionally run 529s, were far too skewed toward stocks in the later stages of their investment paths coming into 2008, resulting in big savings shortfalls for students getting close to college.

If that experience had a silver lining, though, it was that it underscored the importance of holding on to what you already have versus gunning for big returns in your child's college-savings plan, particularly as college draws near.

Many of the investment pros running 529 college-savings programs have scaled back the equity holdings of their age-based options to make them more conservative, and added index funds in place of poorly chosen actively managed funds, in the hopes of reducing the risk of a big shortfall at the worst possible time. Investors managing the asset allocations of their own college-savings programs should also take the lessons of 2008 to heart.

Here are a few quick tips:

- ▶ By the time your child hits the teenage years, more than 50% of his or her college fund should be in bonds and cash.
- ▶ By the time your child is a junior or senior, equities should compose only a small slice (less than 20%) of his or her college dough.

If you have to boost your college savings using a combination of financial aid, student loans, or work-study, it's better than risking the money you have been able to set aside.

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# Week 3

## Build on Your Strategy

Week 1 of my financial fitness program helped you gear up, first by checking up on your household's financial health and then by getting organized. The tasks in Week 2 focused on investing well for short- and intermediate-term goals. In the last two weeks of our financial fitness regimen, we'll focus on a key concern for most investors: Successfully building and monitoring a long-term portfolio.

### Day 15

#### Conduct a "quick and dirty" portfolio checkup

Degree of Difficulty: Easy to Moderate

A good starting point is to take a snapshot of where your portfolio is right now, with an eye toward flagging any notable trouble spots. The best tool for the job is Morningstar's Portfolio X-Ray, located on the Portfolio tab of Morningstar Investment Research Center. Simply plug in tickers for each of your holdings (use CASH\$ for cash), then hit "Show Instant X-Ray" for a look at your portfolio's stock/bond/cash mix and breakdown by investment style, sector, and geographic breakdown.

That's a lot of information, and may not be valuable without some context. To help make sense of what you're looking at, click on the "Interpreter" tab under "Edit Holdings." As you do so, run through the following checklist and take notes as you go along:

**1. Is your stock/bond/cash mix in line with your targets?** (Don't have targets? Look to Morningstar's Lifetime Allocation Indexes, available at [morningstar.com/goto/LAIndexes](http://morningstar.com/goto/LAIndexes), for guidance.)

Take note if your allocation to any one asset class is more than five or 10 percentage points higher or lower than your targets. If it is, it's time to rebalance.

**2. Are you making big, inadvertent sector bets?** Compare your weightings to the S&P 500's (provided in X-Ray). Again, look for big bets of five or 10 percentage points or more.

**3. How about investment-style bets?** To help provide a reference point, the 5000 Index, a measure of the broad market, recently had the following breakdown in the Morningstar style box: 24% large value, 24% large blend, 23% large growth, 7% in the mid-value and mid-blend boxes, 8% in mid-growth, and 2% in each of the small-cap boxes.

**4. Is a big share of your portfolio in a single stock?** To see, click on the "Stock Intersection" tab. Positions amounting to five or 10 percentage points higher or lower than your targets can ramp up your portfolio's risk level.

**5. Do you have an adequate emergency fund?** Make sure you have a bare minimum of three months' worth of living expenses in a cash or cash-like vehicle. If you have extra time, click the individual security names at the bottom of the main X-Ray page to see data and analyses for the stocks, mutual funds, and ETFs in your portfolio.

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## Day 16

### Check up on the quality of your company retirement plan

Degree of Difficulty: Moderate to Difficult

If you're earning a match on your 401(k) plan contributions, it's a no-brainer to invest at least enough to get the full match amount. But what if your company isn't matching, or if you'd like to make a larger contribution to your retirement than you're being matched on? Is it best to stick with the 401(k) or turn to another vehicle like a Roth IRA?

The answer to that question depends, at least in part, on the quality of your plan. To help determine whether your plan is worth investing in or is a stinker, ask your HR administrator for a document called a Summary Plan Description, which lays out crucial information about your 401(k).

Beware: This document is apt to be crammed with legalese and is not likely to be easy reading. But after a little bit of hunting, you should be able to locate your plan's administrative expenses. These fees may be depicted in percentage or dollar terms; if the latter, divide your plan's costs by the total dollars in the plan. If your plan doesn't have any additional administrative costs, that's a good sign. But if it layers on additional administrative fees that amount to 0.50% or more per year, that's a red flag that your plan is a costly one. Check to see whether your plan includes other bells and whistles, such as a brokerage window, which allows you to invest in options out-

side the plan; the ability to take a loan; and the ability to make Roth 401(k) contributions.

After that, conduct a quick checkup of the breadth and quality of your plan's holdings using the data and Analyst Reports on Morningstar Investment Research Center. Look for a good array of core-type mutual funds: large-cap U.S. and foreign stock offerings, balanced funds, and core intermediate-term bond funds. For stock funds, look for expense ratios of less (preferably much less) than 1% per year, though specialized funds like international and small-cap offerings may charge a touch more. For bond funds, expense ratios of less than 0.75% are ideal. Read Morningstar's Analyst Reports for a quick checkup on the quality of the options in your plan.

If your plan checks out well on the above measures, funding it up to the maximum allowable level is apt to be a good use of your cash, thanks to the tax-deferred compounding that company-retirement plans afford. Before doing so, however, you should also deploy some of your retirement assets into a Roth IRA, which offers the opportunity for tax-free withdrawals in retirement.

## Day 17

### Maximize your match

Degree of Difficulty: Easy

During the 2008-09 recession, many companies reduced their 401(k) matching contributions or even eliminated them altogether. If you're not earning any matching funds on your 401(k),

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my usual advice is to fund a Roth IRA up to the maximum allowable level first. The reason is that you can put anything you'd like into a Roth IRA, and you won't have to pay any additional administrative expenses to invest in one, in contrast with many 401(k) plans. Roth IRA investors also enjoy tax-free compounding and tax-free withdrawals in retirement. If you find yourself with additional assets to invest after that, turn to your 401(k) (provided it's a good one!).

If you are lucky enough to earn matching contributions on your 401(k), plan to take advantage of each and every one of those dollars. This is particularly relevant if A) you're highly compensated and B) you expect to receive a bonus early in the year. That's because you're only allowed to contribute a certain dollar amount to your 401(k) in each calendar year. (In 2011, employees under age 50 can contribute \$16,500, while those over 50 can contribute \$22,000.) If you receive a big bonus early in the year and you're contributing a bigger percentage of your salary to your 401(k) than your employer is matching, there's a chance that you'll hit your dollar contribution limit well before the year is over. In turn, you won't be able to take full advantage of any matching contributions your employer would've made in the remainder of the year.

Check with your employer to find out whether your 401(k) contribution is being deducted from your bonus. If it is, you may want to lower the percentage amount that you're contributing to your 401(k) before you receive the bonus. In so doing, you'll ensure that your own contributions are

spaced throughout the year, and you'll be able to take full advantage of your employer's matching contributions.

## Day 18

### Maximize the benefits of an IRA

Degree of Difficulty: Easy

If you have most of your retirement assets in a company-retirement plan and are using an IRA to supplement what you already have, you can use your IRA in one of two ways.

You can hold core-type investments, which tend to be mainstays in most 401(k) plans: index stock and bond funds, large-cap actively managed funds, balanced funds, and so forth.

Alternatively, you can use your IRA to fill holes in your company retirement plan. For example, say your plan includes adequate stock funds, but its bond funds charge more than 1% per year in annual expenses—sure to cut into your long-term returns. If that's the case, you can fill your company retirement plan with the decent stock funds and leave the bond portion of your portfolio to an IRA. Morningstar's Portfolio X-Ray tool can help you see where you've got holes in your existing asset mix. Simply go to the Portfolio tab of Morningstar Investment Research Center.

You can also use your IRA to include asset types not commonly found in company retirement plans, including funds dedicated to real estate investment trusts, commodities, or Treasury

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Inflation-Protected Securities. All of these investment types do a good job of diversifying a portfolio that's composed primarily of conventional stocks and bonds. They also can be a headache when held outside of tax-sheltered accounts, because they generate a lot of taxable income. So, they're ideal holdings for an IRA.

### Day 19

#### **Look to target-date funds for cheap asset-allocation advice**

Degree of Difficulty: Easy

There are many different tools to help you arrive at a stock/bond mix that makes sense for you. They will look at your age, years until retirement, the amount of assets you've been able to stash away, other sources of income you expect to have in retirement, and so forth.

I encourage you to seek out a range of opinions to help determine an optimal asset allocation mix because it's an important topic. Many brokerage firms and fund companies offer free asset-allocation tools on their sites, or you might consider consulting with a financial advisor to help you come up with a stock/bond/cash mix tailored to your own situation.

One other idea is to look for asset-allocation guidance via some of the target-date funds geared toward people in your age range. Target-date funds aren't perfect, as evidenced by the big 2008 losses incurred by certain overly aggressive funds geared toward investors getting close to

retirement. But looking at a few different target-date series can help you get a sense for what's reasonable.

Morningstar began rating target-date series back in November 2009. Among the most highly rated lineups, per our analysts, are Vanguard's Target series (fairly middle-of-the-road asset-allocation mixes) and T. Rowe Price's Retirement series (more aggressive and stock-heavy).

### Day 20

#### **Manage your portfolio for tax efficiency**

Degree of Difficulty: Moderate

Although utilizing tax-sheltered vehicles like IRAs and 401(k)s can help you dodge the tax collector, at least temporarily, there are occasions when you'll need to save in your taxable accounts. Perhaps you're socking money away for a goal that's close at hand, for example, or maybe you've maxed out your contributions to the tax-sheltered vehicles available to you.

If that's the case, there are still some steps you can take to reduce the tax effects on these investments. One of the key steps you can take is to limit your own trading activity, thereby reducing the taxable capital gains you'll owe from year to year. I'm also a big fan of actively pruning your taxable portfolio's losers, which helps you offset capital gains from your winners. Finally, it pays to be careful about what types of investments you hold in your taxable accounts. High-turnover stock funds, whose short-term capital



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gains are taxed as ordinary income, are a definite “don’t,” as are high-income-producing investments such as REITS and junk-bond funds.

On the “buy” list for taxable investors are low-turn-over exchange-traded funds and index funds, municipal-bond funds, individual stocks, and tax-managed funds.

### **Day 21**

#### **Use a “bucketing” system when constructing your retirement portfolio**

Degree of Difficulty: Moderate to Difficult

One of the most daunting aspects of managing your finances is figuring out how to transition from accumulation mode into retirement, or “harvest” mode.

One intuitive way to construct a retirement portfolio is to create various buckets of money based on when you expect to tap them for living expenses. Bucket number one contains living expenses for the next two to five years, and therefore should consist of highly liquid investments like CDs and money market funds. This is money you can’t afford to lose.

Bucket number two should be positioned for living expenses in years five through 15, and therefore you can afford to take on slightly more risk. Intermediate-term bond funds and even conservative stock funds or balanced fund are good choices for the intermediate sleeve of your retirement portfolio.

Those assets you don’t expect to tap for at least 15 years can be stashed in stocks and stock mutual funds. Because you’ve established you have a fairly long time horizon for this money, you won’t be unduly upset if the stock market has periodic hiccups.

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# Week 4

## Stay on Track

We've tackled a lot of tasks in the first three weeks of our financial fitness regimen, including finding our baselines and getting organized (Week 1), identifying appropriate investments for short- and intermediate-term goals (Week 2), and implementing strategies for running an effective long-term portfolio (Week 3).

In the final full week on the road to financial fitness, I'll share more tips for investing well before and during retirement, as well as strategies for keeping your portfolio on the right track through varying market environments.

### Day 22

#### Look for opportunities to streamline

Degree of Difficulty: Moderate

Today's task is one that's relevant to investors of all ages and of all life stages: combating portfolio sprawl.

Diversification is a good thing, of course, but you can also overdo it. It requires time and research to keep track of important developments at stocks and mutual funds, and that task is compounded when you have many different accounts. (The paperwork coming into your house can also get ugly.) And the more investments you have, the greater the likelihood that your portfolio will behave like the market. There's nothing inherently wrong with market-like performance but you don't want to pay active management fees when an index fund would have done the job just as well.

So what are some strategies for beating back the sprawl? Index mutual funds and exchange-traded funds that track a broad market segment are a good place to start if you're trying to streamline your financial life; our Fund Favorites list includes plenty of top notch index options. The link can be found right on the Morningstar Investment Research Center home page.

Alternatively, you could take advantage of all-in-one options, either by using a target-date fund or a stock/bond hybrid fund such as Vanguard Wellington (VWELX), Dodge & Cox Balanced (DODBX), or T. Rowe Price Spectrum Growth (PRSGX). And if you're managing multiple accounts geared toward a single goal—for example, you and your spouse each have IRAs and 401(k)s, as well as taxable assets earmarked for retirement—think of them as a single entity rather than running each account as a well-diversified whole. Doing so gives you the freedom to pack a significant share of your assets into the best investments available to you within each account. Use Morningstar's Portfolio X-Ray tool to make sure the whole portfolio is diversified and that the asset allocation is in line with your target.

### Day 23

#### Decide between Roth and traditional 401(k) contributions

Degree of Difficulty: Moderate

There's been a lot of buzz about converting traditional IRAs to Roths. But what about a Roth

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401(k), if your company offers one? Should you take the tax hit on your contributions in exchange for tax-free withdrawals later on, as is the case with Roth 401(k)s, or should you go the traditional 401(k) route? In that case, you'll make pretax contributions and have your balance taxed upon withdrawal.

As with the Roth versus traditional IRA decision, this one rests on one big swing factor: whether you expect to be in a higher tax bracket in retirement than you are now. But unless you're quite close to retirement, the answer to that question is all but unknowable.

However, a few categories of individuals are good candidates for making all or at least part of their 401(k) contributions Roth-style. The first would be younger savers who aren't earning a lot currently but may do so in the future. For them, their own earnings trajectory, plus the possibility that future tax rates will trend higher across the board, make a strong argument for a Roth 401(k) and IRA.

Another good candidate for Roth 401(k) contributions is the upper-income individual who has a lot of retirement assets sitting in a traditional 401(k) plan but has heretofore earned too much to contribute to a Roth IRA. Because there's no income limit on Roth 401(k) contributions, the vehicle offers a great way for such individuals to get some of their retirement assets into the Roth column.

If you're conflicted after you investigate the pros and cons, one idea is to split your contributions between the two types of vehicles.

## Day 24

### Get a 'backdoor' Roth IRA

Degree of Difficulty: Easy

Are you a higher-income saver? Lucky you. You can make your investment dollars go even further by taking full advantage of every tax-advantaged option available to you.

Last week I discussed how people who are contributing the full allowable amount can maximize their employer matches by spreading their contributions throughout the year.

One other newer strategy for those with higher incomes is to start a Roth IRA. At first blush a Roth might appear to be off limits to you due to income limitations; you can't make any Roth contribution if you're a single filer earning more than \$120,000 and have the ability to contribute to a company retirement plan; that level goes up to \$177,000 for married couples filing jointly.

But you can get into a Roth through the back door (until Congress closes the loophole) by first opening a traditional nondeductible IRA then immediately converting to a Roth. Income limits used to apply to Roth conversions, but beginning in 2010, people of all income levels have been able to convert. And if you convert shortly after you open your traditional deductible IRA, there

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will be few if any tax consequences. (Note: This strategy may not be effective for those in certain situations—for example, those who already have assets in SEP or SIMPLE IRAs—so check with a tax specialist before embarking on any type of conversion.)

### **Day 25**

#### **See if you're on the right track for retirement savings**

Degree of Difficulty: Moderate

Most of the tasks in my 30-day financial fitness regimen have centered around helping you get your investment program up and running. But once you do, it's essential that you periodically check in to make sure that your portfolio is on track to help you meet your goals.

For another set of (virtual) eyes on your investment program, turn to T. Rowe Price's free Retirement Income Calculator, one of many good tools available on financial-service firms' websites. You'll be prompted to enter some information about yourself—your birth date, your expected retirement date, your current asset level and allocation, and your desired level of income in retirement. (You won't be asked to provide any personally identifying information, such as your name or Social Security number, though, so don't worry about anyone contacting you with a sales pitch.) The calculator will then give you a gauge of whether your portfolio in its current incarnation will support your desired level of income.

The bottom line with all of these tools is that they help you assess whether your portfolio can realistically support your goals. And the sooner you make that determination, the better positioned you will be to make changes so you don't fall short.

### **Day 26**

#### **Get a plan for your retirement portfolio**

Degree of Difficulty: Moderate

Amassing enough assets to retire is the heaviest lifting that any of us will do in our investing lives. But even after you've cleared that hurdle, it's still important to have a plan for managing your assets during retirement.

Because encountering a bear market early in your retirement years can have a devastating impact on portfolios that are too aggressively positioned, it's important to have a sizable dose of bonds and cash by the time you retire. Because no one can predict the future, there's no right answer about how much any of us should have in stocks, bonds, and cash. But Morningstar's Lifetime Allocation Indexes, developed in conjunction with asset-allocation specialist Ibbotson Associates,

provides asset allocations for investors of various expected retirement dates and risk tolerances.

Another key task for retirees and pre-retirees is to determine a realistic portfolio withdrawal rate.

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Finally, if you've saved for retirement in various accounts—and most of us have—your retirement portfolio strategy must also include a plan for tapping those assets. As a general rule of thumb, you'll want to tap your taxable accounts first, deductible IRAs and company-retirement plan assets second, and Roth assets last.

### Day 27

#### **Make sure your retirement portfolio includes inflation protection**

Degree of Difficulty: Easy

If you're already retired or getting ready to do so, one of the key risks that you'll need to guard against is inflation. Social Security payments are adjusted for inflation, but the paychecks you'll take from your retirement portfolio will grow smaller and smaller—in real terms—as the prices on the stuff you buy trend up. It's therefore important to position your portfolio to address that threat.

Although investors often debate the best investments to guard against inflation, with some favoring so-called hard assets like commodities and gold, Treasury Inflation-Protected Securities (TIPS) provide the most direct way to do so. The principal values of TIPS adjust upward to keep up with inflation, as measured by the Consumer Price Index, giving investors a straightforward, low-cost way to ensure that their portfolios keep up with higher prices.

At times investors appeared to have paid too high a price for the peace of mind that TIPS afford. But as a long-term strategic hedge against

higher inflation, TIPS serve a worthwhile role. Morningstar's Lifetime Allocation Indexes include as much as 25% of the fixed-income portfolios for retirees in TIPS.

### Day 28

#### **Get your estate plan in gear**

Degree of Difficulty: Moderate

I firmly believe that it needn't be difficult to tackle many important financial-planning tasks on your own. But one area where I wouldn't advise a DIY approach is in the realm of estate planning. Do-it-yourself wills and other estate-planning documents abound on the web, but estate planning is complicated, and the consequences of mis-managing it are great. This is one area where paying for professional advice can be money well spent.

That's not to say you won't have some involvement, however. Before you visit with an estate-planning attorney, take stock of your major assets, including investments, real estate, and business interests. If you took stock of your net worth (Day 4) or put together a Master Directory (Day 5) you'll be well on your way.

Also consider whom you'd like to inherit your assets, as well as the key individuals you would like to make decisions on your behalf after you become incapacitated or die. Parents of minor children should also think about whom they'd like to look after their children if they become unable to do so.

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## Day 29

### Put in place a system for tracking cost basis

Degree of Difficulty: Easy to Moderate

When it comes to matters of money and investing, my mantra is focus on what you can control. In the “can’t control” column are a grab bag of macro-economic factors: interest rates, the level of inflation, and the direction of dollar. On the flipside, you have a lot more control over your own savings rate, the composition of your portfolio, and even the amount of investment-related taxes you pay.

Maxing out your contributions to available tax-sheltered vehicles and selecting tax-efficient investments for your taxable accounts (Day 20 in our financial fitness regimen) are two key ways you can reduce Uncle Sam’s cut of your investment returns. One other lever is selling your losing holdings to offset taxable capital gains from winning holdings in your portfolio.

Key to executing this strategy is keeping good record of your cost basis—the price you paid for individual securities in your taxable portfolio, including commissions and other expenses. The more precise your record-keeping, the better you can take advantage of more sophisticated tax-loss selling methods, such as specific share identification. Brokerage and mutual fund firms, as well as financial software packages, have begun providing increasingly sophisticated tools for tracking your cost basis. But setting up your own tracking system isn’t difficult. Simply get in the habit of recording the

name and number of shares you purchased, as well as the dollar amount and the date on which you purchased them. (Don’t forget reinvested dividends.)

## Day 30

### Schedule regular checkups

Degree of Difficulty: Moderate

Investors often make the mistake of checking up on their portfolios too frequently, or worse yet, only after big market moves, when they’re most inclined to make rash decisions. To help avoid that pitfall, schedule regular checkups in advance. For most people, one comprehensive portfolio review per year is plenty, and much better than obsessing on a daily basis. Year-end—ideally around Thanksgiving, before the holidays gear up—is a good time to conduct your annual portfolio review, because you can still make adjustments to reduce your tax hit.

Morningstar’s Portfolio X-Ray tool makes it easy to monitor your portfolio on an ongoing basis. Simply type in your holdings – as either a dollar amount or percentage based on a hypothetical investment of \$10,000 – and click view your Portfolio X-Ray.

If you feel information overload setting in, here are some tips to help you focus on the most important factors: Create an Investment Policy Statement, available at [morningstar.com/goto/investmentpolicy](http://morningstar.com/goto/investmentpolicy), to articulate your investing goals and track your progress. Also, follow the steps in my “quick and dirty” portfolio checkup (Day 15.)

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For more tips, check out the articles and videos on Morningstar Investment Research Center. You can find all of my articles under Authors: Christine Benz or sort by a collection such as Personal Finance to continue on your path to financial fitness.



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