



## Broken Models: Model Portfolios Need Repair

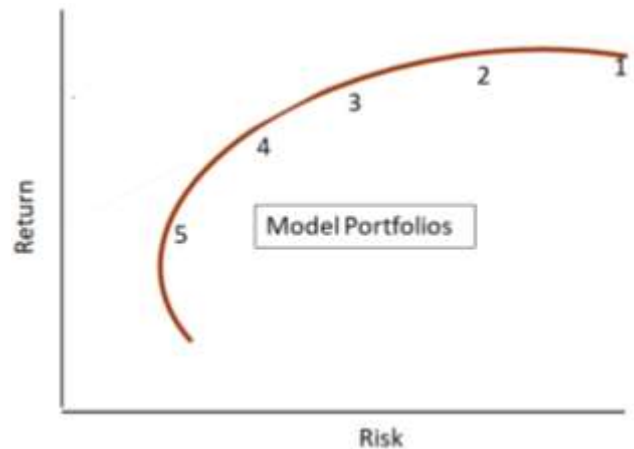
Ron Surz [Ron@TargetDateSolutions.com](mailto:Ron@TargetDateSolutions.com) (949)488-8339

- Model portfolios are useful for managing client assets, but they are oversimplified and inappropriate for many.
- Now is the time to fix these models before they break.
- Risk has different meaning for different ages, so age needs to be integrated with risk.

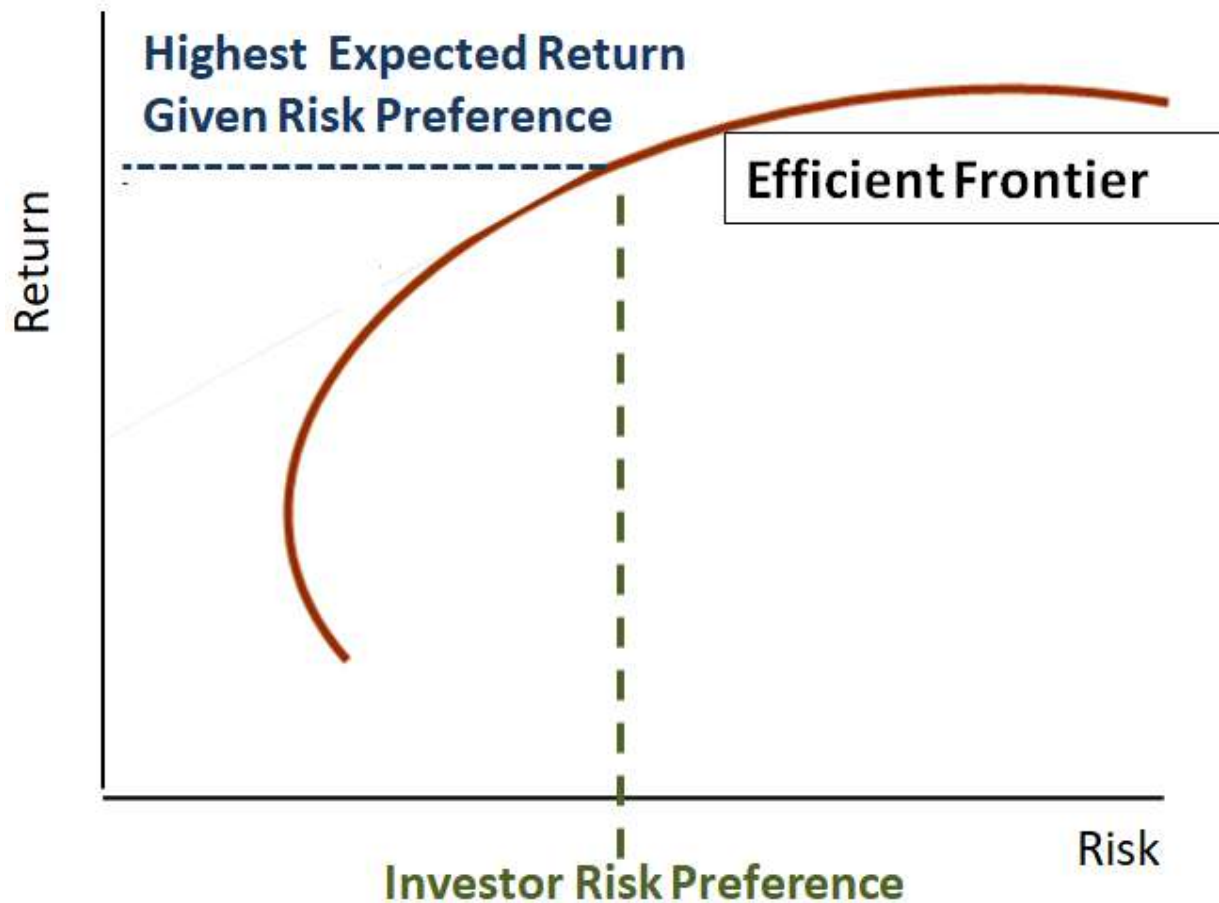
*It is the neglect of timely repair that makes rebuilding necessary.* Richard Whately, English Writer



Most investment advisors use model portfolios and those that do usually rely on models provided by their firms. These models employ Modern Portfolio Theory (MPT) to identify a family of portfolios along the efficient frontier, like the 5 portfolios shown on the right, ranging from high risk (1) to low (5).



The advisor's job is to determine the client's risk preference and map it into a model as shown in the following:



This well established approach is plain and simple. The problem is that it is too simple because it ignores a critical and obvious aspect of the client, namely age. As we explain in the following, risk has different meaning for different ages. Model portfolios need to be repaired to integrate risk with age. If current portfolio models were cars they would be cruising without steering wheels. They need fixing before it is too late.

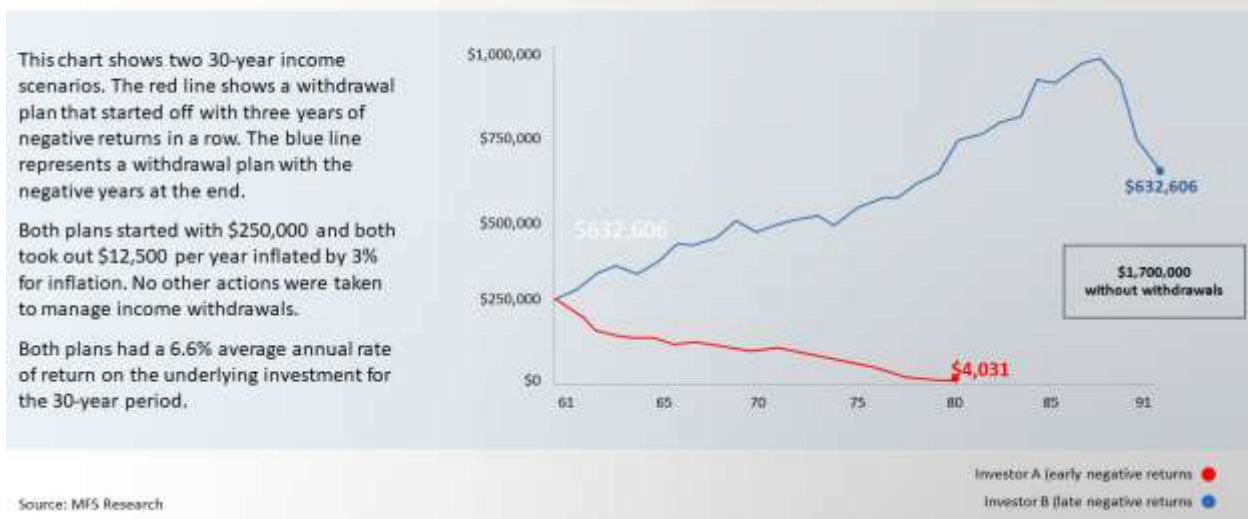
### **The importance of age**

Our age is the best indicator of the time we have to invest, the most important factor in setting an investment strategy. Diversification is the only free lunch in investing, but its

benefits work best over many years. In addition to having enough time for diversification to work, our future earning power is always greatest when we're young, which means we can take bigger risks knowing we'll recover by the time we retire.

But as our working life comes to an end **Sequence of Return Risk** is a very real and serious threat, although most don't grasp its gravity. Our lifestyle can be ruined if we are unfortunate enough to experience losses during the transition from working life to retirement, even if markets subsequently recover. We each get to do this only once. It is the obligatory running of the gauntlet in lifetime investing. Here's an example:

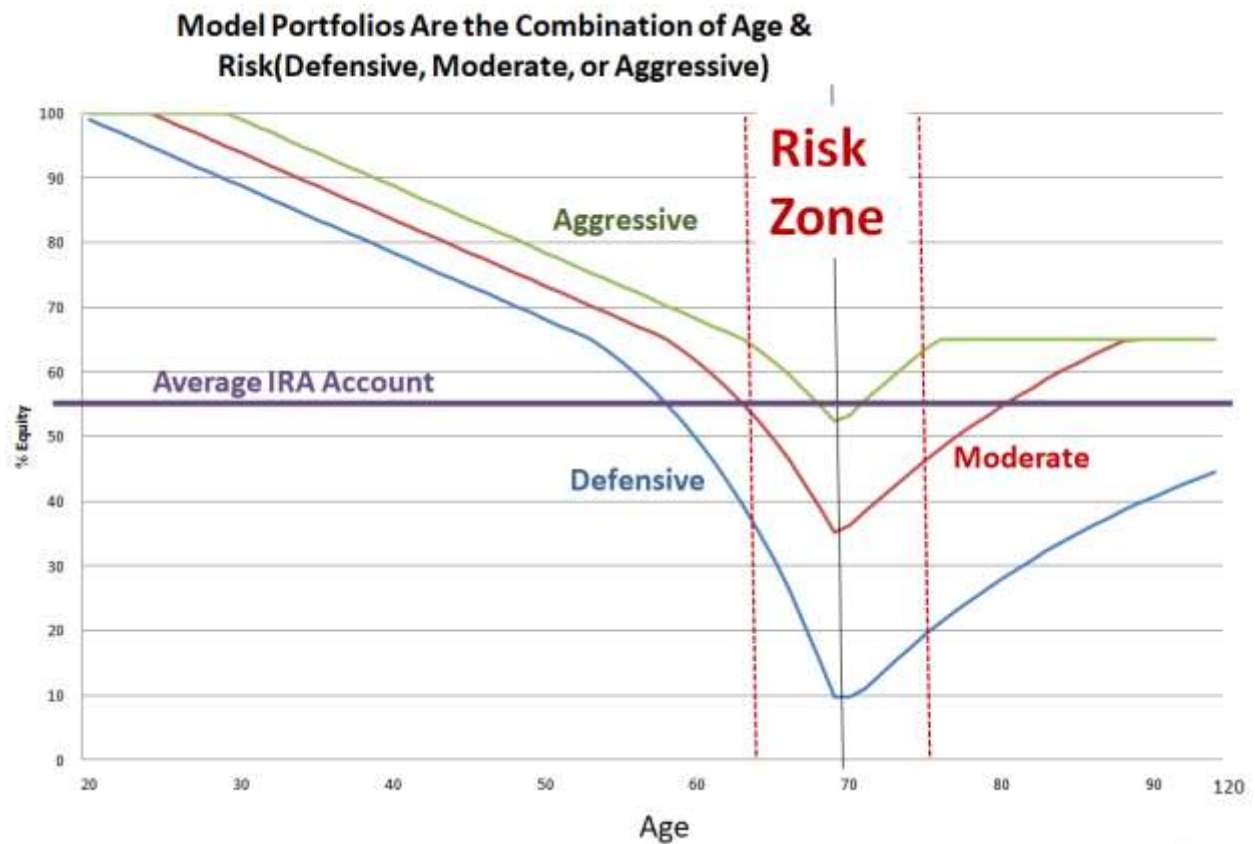
## Sequence of Return Risk



## Fixing models

We have seen an evolution in age-based modeling with the recent introduction of target date funds (TDFs) which have grown from nothing a few years ago to over \$1.5 trillion today. The idea behind TDFs is good but current glide paths are wrong because they do not defend against sequence of return risk, so they are destined to devastate again. Accordingly, we need two repairs to achieve the best model portfolios: (1) TDF glide paths need fixing and (2) these repaired glide paths need to be integrated with investor risk.

Sequence of return risk is managed with a [V-shaped glide path](#) that is very defensive in the Risk Zone that spans the 5 years before and after retirement. There is currently only one such glide path. With this correction, renovated portfolio models are constructed along risk-based TDF glide paths as shown in the following:



## Conclusion

How do your portfolios stack up against those shown in the graph above? You may want to consider some repairs.

For more information, please visit our repair shop at [Age Sage](#)

### Why [Age Sage](#)

- ✓ The first and only Robo Analyst for Boomers and adults.
- ✓ All models are entirely composed of ETFs
- ✓ Consistent with DOL best interest standards

- ✓ We're a Robo Analyst that helps advisors rather than a Robo Advisor that competes with them.
- ✓ More than 12,000 models. See [Broken Models](#). Age matters. All solutions are AGE-and-risk based.
- ✓ No account minimum
- ✓ \$50 buys a custom age-and-risk specific multi-asset global asset mix: broad diversification.
- ✓ Total portfolio fee for "Least Expensive" is less than 6 bps (.06%). Compare to 100 bps (1.0%) for other multi-asset portfolios
- ✓ Solutions provided for various platforms, like Fidelity, Vanguard & Schwab. Even Socially Responsible / ESG.
- ✓ Uses a patented and time-tested target date fund glide path
- ✓ Could be converted into a "[cult](#)" (DFA is my hero)