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Intelligent Wealth

# Welcome to Intelligent Wealth

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IN DEPTH GUIDES

# Investment basics for retirement accounts



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# Investment basics for retirement accounts

Achieving retirement security requires more than just saving; it demands a strategic approach to investing that evolves with your life. This guide demystifies essential investment vehicles like Stocks, Bonds, Index Funds, and Annuities, and explains how to maximize tax-advantaged accounts like 401(k)s and IRAs. You will learn to navigate the critical trade-off between risk and return, minimize portfolio-eroding fees, and build a resilient strategy that transitions from early-career growth to pre-retirement preservation.



# An introduction to retirement planning

## Why retirement planning matters

Planning for retirement isn't just about saving money — it's about creating financial security for your future self. With increasing life expectancies and uncertain future social security benefits, the responsibility for funding retirement falls increasingly on individuals.

Many Americans worry they won't have enough money for retirement. Yet with proper planning and consistent investing, achieving retirement security is within reach for most people. The key is starting early and making informed decisions about where to invest your retirement savings.

Some key reasons retirement planning deserves your attention:

- Longer lifespans mean potentially longer retirements to fund
- Healthcare costs typically increase as we age
- Social Security benefits may replace only a portion of your working income
- The earlier you start, the more time your money has to grow

## How this guide will help you

This guide aims to demystify retirement investing by explaining the main types of investments suitable for retirement accounts and how to evaluate which investments match your personal situation.

Whether you're just starting your career or approaching retirement, the principles in this guide will help you make more confident investment decisions.

What you'll learn:

- How different retirement accounts work and their tax advantages
- The fundamental principles that drive successful investing
- The major investment types suitable for retirement portfolios
- How to select investments based on your personal situation
- Practical strategies for managing your retirement investments over time

Remember, investment knowledge is power — the power to secure your financial future.

# Understanding retirement accounts

## Types of retirement accounts

Before diving into specific investments, it's important to understand the different retirement account structures available. The account type you choose affects your tax situation, access to funds, and sometimes investment options.

Employer-sponsored retirement plans are offered through your workplace and often include convenient features like automatic payroll deductions and possibly employer matching contributions.

Individual Retirement Accounts (IRAs) provide tax-advantaged options for retirement saving independent of your employer.

Key retirement account types include:

- Employer-Sponsored Plans: 401(k), 403(b), 457, TSP
- Individual Retirement Accounts: Traditional IRA, Roth IRA
- Small Business Options: SEP IRA, SIMPLE IRA
- Self-Employed Options: Solo 401(k), Defined Benefit Plans

## Tax advantages explained

One of the most compelling reasons to use retirement accounts is their tax advantages. Understanding these benefits can help you maximize your retirement savings.

Tax-deferred accounts, such as Traditional 401(k)s and Traditional IRAs, allow you to contribute pre-tax dollars, effectively reducing your current taxable income. Your investments then grow without being taxed on yearly gains. However, you'll pay ordinary income tax when you withdraw money in retirement.

Tax-free accounts, like Roth 401(k)s and Roth IRAs, take a different approach. You contribute after-tax dollars, meaning you get no immediate tax deduction. However, your investments grow tax-free, and qualified withdrawals in retirement are completely tax-free as well.

Benefits of retirement account tax advantages:

- Reduction or deferral of current income taxes
- Tax-free growth during the accumulation phase
- Potential for lower taxes on withdrawals in retirement
- Protection from creditors in many states

## Contribution limits and deadlines

To encourage retirement saving while limiting tax benefits for higher earners, the IRS sets contribution limits on retirement accounts. These limits are periodically adjusted for inflation.

For employer-sponsored plans like 401(k)s, 403(b)s, and 457 plans, the IRS establishes annual contribution limits that are typically significantly higher than those for IRAs. These plans also offer additional “catch-up” contributions for individuals over a certain age.

Traditional and Roth IRAs have their own annual contribution limits, which are typically lower than employer-sponsored plans. Income limits may restrict Roth IRA eligibility or Traditional IRA deductibility, so it's important to check current guidelines.

Important timing considerations include:

- Employer plan contributions typically must be made by December 31st
- IRA contributions can be made until the tax filing deadline (usually April 15th)
- Starting contributions early in the year maximizes time for growth

# Investment fundamentals

## The power of compound interest

Albert Einstein reportedly called compound interest “the eighth wonder of the world,” noting that “he who understands it, earns it; he who doesn’t, pays it.”

Compound interest is simply interest earned on both your principal (original investment) and previously earned interest. Over time, this creates a snowball effect where your money grows at an accelerating rate.

Consider two investors with different approaches: The first investor starts early, investing a modest amount annually for just ten years in their twenties, then stops but leaves the money invested until retirement age. The second investor waits a decade longer to begin, then invests the same amount annually for three times as many years until retirement age.

Despite the second investor contributing significantly more money overall, the first investor often ends up with a larger retirement fund. This illustrates why starting early is perhaps the most powerful retirement strategy of all.

Key principles of compound growth:

- The earlier you start investing, the more time your money has to grow
- Regular contributions amplify the compounding effect
- Compounding works best when left undisturbed for long periods

## Risk vs. return: Finding your balance

Every investment carries some degree of risk, and generally speaking, higher potential returns come with higher risks.

Understanding this relationship is fundamental to building an appropriate retirement portfolio.

The risk spectrum spans from the relative safety of cash and cash equivalents through increasingly volatile investments. At the lower end are cash and cash equivalents such as savings accounts and money market funds, followed by government bonds. Moving up the risk ladder, we find investment-grade corporate bonds, followed by real estate investment trusts.

Stocks typically carry more risk than bonds, with blue-chip stocks from large, established companies being less risky than small and mid-cap stocks. International investments, particularly those in emerging markets, often carry additional risks.

Factors affecting your optimal risk-return balance:

- Your time horizon until you need the money
- Your emotional comfort with market fluctuations
- Your financial capacity to withstand losses
- Your need for growth to meet retirement goals

## **Diversification: Don't put all your eggs in one basket**

Diversification — spreading your investments across different assets — is often described as the only “free lunch” in investing. By holding investments that respond differently to economic conditions, you can potentially reduce risk without necessarily sacrificing returns.

Asset class diversification involves creating a mix of stocks, bonds, and potentially alternative investments. This approach works because different asset classes often perform differently in various economic conditions — when one asset class struggles, another may thrive.

Geographic diversification extends your investments beyond domestic markets to include international opportunities. Sector diversification means spreading stock investments across different industries such as technology, healthcare, financial services, and others.

Benefits of proper diversification include:

- Reduced portfolio volatility while maintaining return potential
- Protection against severe losses in any single investment
- Exposure to more opportunities for growth
- Less emotional stress during market turbulence





# Investment options — stocks

## What Are Stocks?

Stocks (also called equities) represent ownership shares in companies. When you buy a stock, you're purchasing a small piece of that business, entitling you to a portion of its assets and earnings. This ownership gives stocks their growth potential — as companies expand and become more profitable over time, their share prices typically rise.

The stock market has historically provided the highest long-term returns among major asset classes, making stocks a crucial component of retirement portfolios, especially for younger investors with longer time horizons. This return potential comes with higher short-term volatility — the stock market experiences frequent ups and downs.

When considering stocks for your retirement portfolio, remember:

- Stocks have historically offered the strongest long-term growth potential
- Stock values can be volatile in the short term, sometimes declining significantly
- A longer time horizon allows more opportunity to ride out market fluctuations
- Stock mutual funds and ETFs offer simpler ways to invest in equities

### **Growth vs. value stocks**

Growth investing focuses on companies expected to expand their earnings at an above-average rate compared to other companies or the overall market. These companies typically reinvest most of their profits back into the business rather than paying dividends to shareholders. Technology and healthcare innovation firms frequently fall into this category.

Value investing, on the other hand, targets companies trading at prices below what their fundamentals suggest they're worth — essentially looking for bargains in the market. These companies typically have more modest growth prospects but often compensate by paying dividends to shareholders. Financial institutions, industrial companies, and consumer staples businesses frequently appear in value portfolios.

Most retirement portfolios benefit from exposure to both growth and value stocks, as they tend to outperform at different times in economic cycles.

Characteristics that distinguish growth and value stocks:

- Growth stocks: Higher price-to-earnings ratios, rapid revenue increases, lower or no dividends, higher volatility
- Value stocks: Lower price-to-earnings ratios, steadier but slower growth, higher dividend yields, typically less volatile

## Dividend investing for retirement

Dividend investing offers several compelling advantages for retirement investors. First, it creates a natural income stream without requiring you to sell your underlying shares. This can be particularly valuable during retirement when you need regular income from your portfolio.

Companies that consistently pay dividends tend to be more financially stable and mature businesses with predictable cash flows. Many quality companies increase their dividends regularly, providing a growing income stream that can help combat the effects of inflation on your purchasing power throughout retirement.

Advantages of dividend investing for retirement:

- Creates a natural income stream without selling assets
- May provide more portfolio stability
- Growing dividends can help offset inflation
- Historically, dividend stocks have provided competitive total returns

## How to evaluate stocks

While individual stock selection requires significant research and ongoing monitoring, understanding basic evaluation metrics can help you make informed decisions about stock mutual funds and ETFs in your retirement accounts.

The price-to-earnings (P/E) ratio is one of the most commonly used valuation metrics. It represents the price you pay for each dollar of a company's earnings. A lower P/E ratio may indicate a better value, though "normal" P/E ratios vary significantly by industry and growth expectations.

The price-to-book (P/B) ratio compares a company's market value to its book value — essentially what would be left if the company liquidated all assets and paid all liabilities. Dividend yield shows the annual dividend payment as a percentage of the current stock price.

Important stock evaluation considerations:

- A company's competitive advantages and market position
- The quality and experience of the management team
- Consistency of earnings and revenue growth
- Financial strength and sustainable business practices

For most retirement investors, directly picking individual stocks isn't necessary — well-diversified stock mutual funds and ETFs provide exposure to equities with less company-specific risk and less required research.

# Investment options — bonds

## Understanding bonds

Bonds are debt instruments issued by governments, municipalities, or corporations to raise capital. When you buy a bond, you're essentially lending money to the issuer in exchange for regular interest payments and the return of principal at maturity.

Bonds serve several important roles in retirement portfolios. First, they generate income through regular interest payments. Second, they typically offer greater capital preservation than stocks, with less price volatility. Third, bonds often move differently than stocks in response to economic conditions, providing valuable diversification.

The relationship between bonds and interest rates is crucial to understand: When interest rates rise, existing bond prices fall (and vice versa). This inverse relationship means that bonds can lose value when rates increase — something many investors don't fully appreciate.

Key bond characteristics to understand:

- **Face value (par value)** — The amount returned at maturity
- **Coupon rate** — The fixed interest rate paid by the bond
- **Maturity date** — When the principal is returned to the investor
- **Credit quality** — The issuer's ability to make payments

## Types of bonds for retirement

Various types of bonds offer different characteristics in terms of safety, income, and tax implications, allowing you to select those best suited to your retirement strategy.

Treasury bonds, notes, and bills are issued by the U.S. federal government and are considered the safest bonds available. Treasury Inflation-Protected Securities (TIPS) offer a unique feature: their principal value adjusts based on inflation as measured by the Consumer Price Index.

Municipal bonds ("munis") are issued by states, cities, counties, and other local government entities to fund public projects. Their primary advantage is that interest is typically exempt from federal taxes and may be exempt from state taxes for residents of the issuing state.

Corporate bonds are issued by companies to fund operations or expansions. They offer higher yields than government bonds to compensate for higher risk. International bonds, issued by foreign governments or corporations, provide geographic diversification.

Popular bond types for retirement portfolios:

- **Government bonds** — Maximum safety, moderate income, no state/local taxes
- **TIPS** — Inflation protection, lower current income, good for preserving purchasing power
- **Municipal bonds** — Tax advantages, moderate yields, better for high-income investors
- **Corporate bonds** — Higher income, more credit risk, good for diversification

## Interest rates and bond performance

Understanding how interest rate changes affect bonds is crucial for retirement investors, especially in a changing rate environment.

Duration is a key concept that measures a bond's sensitivity to interest rate changes. Bonds with longer maturities and lower coupon rates typically have higher durations, making them more sensitive to interest rate changes.

In a rising rate environment, shorter-duration bonds generally outperform longer-duration bonds. Conversely, in a falling rate environment, longer-duration bonds typically outperform. This relationship allows investors to position their bond portfolios based on their interest rate outlook.

Bond interest rate considerations:

- Longer-term bonds are more sensitive to rate changes than shorter-term bonds
- Higher coupon bonds are less sensitive to rate changes than lower coupon bonds
- Floating-rate bonds adjust their interest payments as market rates change

Bond mutual funds and ETFs don't have a fixed maturity date like individual bonds

## Bond laddering strategy

Bond laddering is a strategy where you buy bonds with staggered maturity dates. As each bond matures, you reinvest the proceeds into a new bond at the long end of your ladder. This approach provides several benefits for retirement investors.

The primary advantage of laddering is that it provides regular liquidity as bonds mature, giving you access to principal without having to sell bonds in the secondary market. Laddering also reduces the impact of interest rate fluctuations on your bond portfolio.

For example, a five-year ladder might initially consist of bonds maturing in 1, 2, 3, 4, and 5 years. When the 1-year bond matures, you'd reinvest in a new 5-year bond, maintaining the ladder structure.

Advantages of bond laddering include:

- Regular access to principal as bonds mature
- Reduced impact from interest rate changes
- Automatic reinvestment at current rates
- More predictable income stream

For most retirement investors, bond mutual funds and ETFs provide a simpler alternative to building a bond ladder directly, offering professional management and instant diversification.





# Investment options — index funds

## The power of passive investing

Index funds are mutual funds or exchange-traded funds (ETFs) designed to track a specific market index, such as the S&P 500 or the Bloomberg U.S. Aggregate Bond Index. Instead of trying to beat the market through active management, index funds aim to match market performance by holding all (or a representative sample) of the securities in the target index.

This passive investment approach offers several compelling advantages for retirement investors. Perhaps most importantly, index funds typically have significantly lower expense ratios than actively managed funds. These lower costs translate directly into higher returns for investors over time.

Studies consistently show that most actively managed funds underperform their benchmark indexes over extended periods, especially after accounting for fees and expenses. This performance gap tends to widen over longer time horizons, making index funds particularly well-suited for long-term retirement investing.

Benefits of index fund investing include:

- Lower costs that compound significantly over time
- Broad diversification within the target asset class
- Consistent adherence to stated investment objectives
- Simplicity of selection and monitoring

## Popular index funds for retirement

Several types of index funds are particularly well-suited for retirement portfolios, providing broad exposure to different market segments at low cost.

Total stock market funds track broad U.S. stock market indexes that include companies of all sizes — large, mid, and small-cap stocks. S&P 500 index funds focus on the 500 largest U.S. companies, which represent about 80% of the U.S. stock market by value.

International stock index funds track indexes of non-U.S. stocks, providing geographic diversification beyond the domestic market. Total bond market index funds track broad bond market indexes that typically include thousands of bonds across different sectors, maturities, and credit qualities.

Popular index fund categories for retirement portfolios:

- **Broad market funds** — Comprehensive coverage of entire markets
- **Large-cap funds** — Focus on bigger, more established companies
- **International funds** — Exposure to non-U.S. markets
- **Bond index funds** — Broad fixed-income exposure
- **Specialized sector/style funds** — Targeted exposure to specific market segments

## Expense ratios and why they matter

The expense ratio is the annual fee a fund charges investors, expressed as a percentage of assets. This seemingly small number has an out-sized impact on long-term returns, especially for retirement accounts with decades-long time horizons.

Fund expenses directly reduce your investment returns dollar for dollar. If a fund earns a 7% return before expenses and has an expense ratio of 1%, your actual return is reduced to 6%. This difference might seem minor in a single year, but compounds dramatically over time.

Index funds typically offer significantly lower expense ratios than actively managed funds because they don't need to pay for extensive research teams or high-priced portfolio managers. The difference in cost between the average active fund and the average index fund has historically been around 0.60–0.70 percentage points.

- The impact of expenses is magnified by these factors:
- Compound effect over long investment periods
- Higher-cost funds rarely deliver enough out-performance to justify their fees
- Every dollar saved in fees remains invested to generate future returns

## Building a core portfolio with index funds

One of the simplest and most effective retirement investment approaches is the “core and explore” strategy using index funds. This approach creates a strong foundation with broad-market index funds while allowing some flexibility for more specialized investments.

The core portion of your portfolio, typically representing 80–90% of your investments, consists of broad-market index funds covering major asset classes. This might include a total U.S. stock market index fund, an international stock index fund, and a bond index fund.

The explore portion, representing the remaining 10–20% of your portfolio, can include more specialized investments. These might be specialized index funds targeting specific market segments, actively managed funds in areas where skilled management may add value, or individual securities.

For many investors, a simple three-fund portfolio consisting of a total U.S. stock market index fund, an international stock index fund, and a bond index fund provides all the diversification needed for successful retirement investing.

Steps to build an index fund portfolio:

1. Determine your appropriate asset allocation based on risk tolerance and time horizon
2. Select low-cost, broad-market index funds for each major asset class
3. Consider whether any specialized funds would complement your core holdings
4. Implement a regular rebalancing schedule to maintain your target allocation

# Investment options — target-date

## What are target-date funds?

Target-date funds (TDFs) are all-in-one mutual funds designed to simplify retirement investing. They automatically adjust their asset allocation — the mix of stocks, bonds, and other investments — to become more conservative as you approach and enter retirement.

Each target-date fund has a specific year in its name (e.g., “Target Retirement 2045” or “Retirement Fund 2060”), intended to roughly match your expected retirement date. The further away the target date, the more aggressively the fund invests initially.

Target-date funds have become enormously popular in 401(k) plans — many employers even use them as the default investment option for automatically enrolled participants. Their simplicity makes them particularly appealing for newer investors or those who prefer a hands-off approach.

Key advantages of target-date funds:

- One-decision investment solution for retirement
- Automatic rebalancing and age-appropriate risk adjustment
- Professional portfolio management
- Broad diversification across multiple asset classes

## How they work — the glide path explained

The “glide path” refers to how a target-date fund’s asset allocation changes over time. Think of it as the trajectory of a plane gradually descending for landing as retirement approaches.

A typical target-date fund begins with a high allocation to equities when retirement is far away — often 85-95% stocks for funds with target dates 40+ years out. As you move through your career and approach retirement, the fund gradually shifts its allocation, reducing the equity portion and increasing the allocation to bonds and sometimes cash equivalents.

By the time you reach retirement, the allocation has typically shifted to a more conservative stance, with perhaps 20-40% in stocks and the majority in bonds and cash equivalents. This more conservative positioning focuses on generating income and preserving capital during your retirement years.

Target-date fund providers differ in their approach to the glide path, particularly in how they manage the allocation after the target date is reached. Some providers use a “to retirement” approach, reaching their most conservative allocation at the target date. Others employ a “through retirement” approach, continuing to reduce equity exposure for several years after the target date.

The three stages of a typical glide path include:

- **Accumulation Phase** — High equity allocation for maximum growth potential
- **Transition Phase** — Gradually decreasing equity exposure as retirement approaches
- **Distribution Phase** — Lower equity allocation with focus on income and preservation

## Pros and cons for retirement investors

Target-date funds offer significant advantages that explain their growing popularity in retirement portfolios. Their simplicity allows investors to make a single investment decision rather than selecting and monitoring multiple funds. This “set it and forget it” approach can be particularly valuable for investors who lack the time, interest, or expertise to manage their own asset allocation.

These funds provide automatic rebalancing without investor action, maintaining the target allocation regardless of market movements. Professional management is another key benefit, with investment professionals handling asset allocation decisions based on long term strategic planning.

However, target-date funds also have limitations to consider. Their one-size-fits-many approach is based primarily on your expected retirement date and cannot account for individual circumstances beyond age, such as risk tolerance, other income sources, or specific financial goals.

Cost is another consideration. While target-date fund expenses have generally declined over time, some offerings have higher expense ratios than building a portfolio of individual index funds. Limited customization is another potential drawback — you cannot adjust allocations for specific goals or personal risk tolerance while maintaining the automatic glide path feature.

Important considerations for target-date funds include:

- Simplicity versus customization needs
- Cost comparison with building your own portfolio
- Alignment of the glide path with your risk tolerance
- Philosophy differences between fund providers

## Selecting the right target year

Choosing the appropriate target-date fund involves more than simply selecting the fund with the year closest to your expected retirement date. Several important factors should influence your decision.

Your personal risk tolerance may differ from the assumptions built into the standard target-date offering. If you're more conservative than average, you might consider a fund with an earlier target date than your actual retirement year. This would provide a more conservative allocation with less volatility.

Other income sources can significantly impact your target-date fund selection. If you'll have substantial guaranteed income from sources like pensions or rental properties, you might select a more aggressive (later) target date fund since you have more capacity to weather market volatility.

The investment provider's approach to glide path design is also important to consider. Some providers tend to be more conservative in their equity allocation, while others maintain higher equity exposure longer.

Key factors in selecting the right target-date fund:

- Your actual planned retirement age
- Personal risk tolerance relative to average investors
- Other sources of retirement income
- The provider's glide path philosophy
- The fund's expense ratio





# Investment options — annuities

## Types of annuities

Annuities are contracts between you and an insurance company where you make a lump-sum payment or series of payments in exchange for regular disbursements, beginning either immediately or at some point in the future. While often controversial due to complexity and sometimes high fees, certain types of annuities can play a valuable role in retirement planning.

Fixed annuities function somewhat like certificates of deposit (CDs), paying a guaranteed interest rate for a specified period. Your principal is protected from market fluctuations, and the insurance company bears the investment risk.

Variable annuities allow you to invest in a selection of “sub accounts” similar to mutual funds. Your returns depend on the performance of these investment options. While variable annuities offer potential for higher returns than fixed annuities, your principal is not guaranteed.

Indexed annuities represent a middle ground between fixed and variable annuities. Their returns are linked to a market index (like the S&P 500) but with downside protection. They typically cap your potential gains in exchange for eliminating or limiting losses.

Immediate annuities convert a lump sum into a lifetime income stream, with payments beginning shortly after purchase (typically within a year). Deferred annuities delay income payments until a future date you select.

The major types of annuities include:

- **Fixed Annuities** — Guaranteed interest rate with principal protection
- **Variable Annuities** — Market-based returns with investment risk
- **Indexed Annuities** — Market-linked returns with downside protection
- **Immediate Annuities** — Convert lump sum to lifetime income now
- **Deferred Annuities** — Begin income payments at a future date

## Guaranteed income in retirement

One of the most compelling features of certain annuities is their ability to provide guaranteed lifetime income, regardless of how long you live or how markets perform. This feature essentially allows you to create a “personal pension” to supplement Social Security and other retirement income sources.

Guaranteed income helps ensure that your essential expenses are covered throughout retirement, regardless of market performance or longevity. Having a source of guaranteed income may allow for more aggressive investing with your remaining assets.

Guaranteed income can also provide peace of mind during volatile markets. When you know that your essential expenses are covered regardless of market performance, you're less likely to make emotional investment decisions during downturns.

Income annuities offer various features that can be tailored to your specific needs. You can choose between covering just yourself (single life) or including a spouse (joint life), with joint coverage reducing the payment but providing extended security.

Key benefits of guaranteed lifetime income:

- Protection against longevity risk (outliving your money)
- Coverage of essential expenses regardless of market conditions
- Potential for more aggressive investing with remaining assets
- Peace of mind during market volatility

## Understanding fees and surrender periods

Annuities, particularly variable and indexed types, often come with multiple layers of fees that can significantly impact returns. Understanding these costs is essential for making informed decisions about whether annuities are appropriate for your retirement plan.

Mortality and expense (M&E) charges cover the insurance guarantees and often fund sales commissions. Administrative fees cover account maintenance. For variable annuities, the underlying sub-account expenses for investment management add another layer of costs. Optional benefit riders, such as guaranteed minimum income or withdrawal benefits, add yet another expense.

Most annuities also impose surrender periods — typically 5-10 years — during which withdrawals above a certain amount incur surrender charges. These charges typically start high and decline gradually each year until the surrender period expires. This limited liquidity can be problematic if your financial situation changes unexpectedly.

Some direct-sold annuities from companies like Vanguard, Fidelity, and TIAA offer significantly lower costs than many commission based products, sometimes with no surrender charges.

Important fee considerations for annuities include:

- Total annual expenses compared to alternative investments
- Length and structure of surrender periods
- Fees for optional riders and whether their benefits justify the cost
- Tax implications of annuity withdrawals

## When annuities make sense (and when they don't)

Annuities can be appropriate financial tools in specific situations but are not universally suitable for all retirement investors. Understanding when they might make sense — and when they likely don't — can help you make informed decisions about their place in your portfolio.

Annuities may be appropriate if you've maximized contributions to tax-advantaged retirement accounts and are seeking additional tax deferral. Income annuities can make sense if you have sufficient assets to benefit from the guaranteed income but don't need access to all of your principal.

If you're highly concerned about longevity risk — the possibility of outliving your money — immediate or deferred income annuities can provide insurance against this risk. Some investors simply value the peace of mind that comes with guaranteed income over maximum growth potential.

Conversely, annuities may not be appropriate if you may need access to your principal during the surrender period. If you have not yet maximized contributions to 401(k)s, IRAs, and other tax advantaged accounts, it generally makes sense to fund these options first before considering annuities.

Situations that might warrant annuity consideration:

- Need for guaranteed lifetime income beyond Social Security
- Desire for tax-deferred growth after maximizing other retirement accounts
- Strong concern about outliving your money
- Anxiety about market volatility affecting retirement security



# Finding your strategy

## Assessing your risk tolerance

Risk tolerance is your emotional and financial ability to withstand investment losses without making counterproductive decisions. Understanding your personal risk tolerance is essential for building a retirement portfolio that you can stick with through market cycles.

Your risk tolerance consists of two components that sometimes conflict. Risk capacity is your financial ability to endure losses, based on objective factors like your time horizon, income stability, and other assets. Risk willingness is your emotional comfort with investment fluctuations, based on subjective factors like personality, past experiences, and investment knowledge.

To assess your risk tolerance accurately, consider how you would react in challenging market scenarios. Would you stay invested if your portfolio lost 20% in three months? How would you feel if your friends were earning higher returns in different investments?

Misaligning your investments with your risk tolerance often leads to buying high and selling low — one of the most damaging investing behaviors. A portfolio that lets you sleep at night, even if theoretically “suboptimal,” will likely produce better real-world results because you’ll be able to stick with it during market turbulence.

Key aspects of risk tolerance assessment:

- Balancing objective risk capacity with subjective risk willingness
- Considering your reactions to previous market downturns
- Understanding the difference between temporary and permanent losses
- Recognizing that risk tolerance may change over time

## Time horizon — the key to investment selection

Your time horizon — how long until you need the money — is perhaps the single most important factor in determining appropriate investments. Longer time horizons generally allow for greater risk taking, while shorter horizons typically require more conservative approaches.

With long time horizons of 20+ years, most financial experts recommend higher allocations to equities to maximize growth potential. The greater volatility of stocks becomes less concerning when you have decades before needing the money, as short-term fluctuations have historically been smoothed out over longer periods.

Medium time horizons of 10-20 years generally suggest a balanced approach with significant but not overwhelming equity exposure. As the time horizon shortens within this range, gradually increasing the allocation to bonds becomes prudent.

With short time horizons of less than 10 years, most investors should consider higher allocations to bonds and cash equivalents with an emphasis on capital preservation. Reduced equity exposure helps protect against the risk of having to sell investments during a market downturn.

Your time horizon affects investment selection in several ways:

- Longer horizons allow more exposure to higher-risk, higher return investments
- Shorter horizons require greater emphasis on capital preservation
- Different portions of your portfolio may have different time horizons

## Understanding and minimizing costs

Investment costs directly reduce your returns, and their impact compounds over time. Focusing on costs is one of the few reliable ways to improve expected outcomes.

Expense ratios are annual fees charged by mutual funds and ETFs, expressed as a percentage of your investment. These ongoing costs can vary dramatically between similar funds — from below 0.05% for some index funds to over 1% for certain actively managed funds.

Trading costs and tax costs can also substantially impact your after tax returns, especially in taxable accounts. Hidden costs like cash drag (uninvested cash in portfolios), transaction costs within funds, and foreign tax withholding can further reduce returns.

The impact of reducing investment costs can be dramatic over a retirement timeframe. This effect makes cost minimization one of the most powerful tools in retirement planning.

Ways to minimize investment costs include:

- Using low-cost index funds for core portfolio positions
- Comparing expense ratios between similar funds
- Limiting portfolio turnover to reduce trading costs and tax impacts
- Evaluating whether advisory services justify their fees

## Creating your personal investment policy

An investment policy statement (IPS) is a written document that outlines your investment goals, strategies, and guidelines. While often associated with institutional investors, creating a personal IPS can dramatically improve your retirement investing outcomes.

A good personal IPS begins with clearly defined investment objectives, including your primary financial goals, the return requirements to meet those goals, and your risk tolerance and capacity. Your IPS should detail your asset allocation strategy, including target percentages for each asset class and criteria for rebalancing.

The main benefit of a written IPS is that it serves as an emotional circuit breaker during market extremes. When markets are soaring or plunging, you can refer to your IPS rather than making decisions based on fear or greed. This disciplined approach helps avoid common behavioral investing mistakes.

A well-constructed personal IPS includes:

- Specific, measurable financial goals
- Clear guidelines for asset allocation and rebalancing
- Defined criteria for selecting and monitoring investments
- Protocols for regular review and appropriate adjustments

# Putting it all together

## Life stage investment approaches

While everyone's situation is unique, certain investment approaches tend to be appropriate for different life stages. Understanding these general frameworks can help you develop a strategy suited to your current phase of life.

### **Early career primary focus — growth**

During the early stages of your career, with potentially decades until retirement, your portfolio should generally emphasize growth. This typically means a higher allocation to equities, including both domestic and international stocks. With a long time horizon, you can likely afford to weather market volatility in pursuit of higher expected returns.

Early career investors benefit from:

- Taking advantage of employer retirement plan matching
- Establishing regular, automatic contributions
- Focusing on low-cost, broadly diversified investments

### **Mid-career primary focus — balanced growth**

As you progress through your career, you may want to begin moderating risk while still maintaining significant growth potential. This often involves gradually increasing your bond allocation while maintaining a substantial position in domestic and international equities.

Mid-career priorities often include:

- Maximizing retirement contributions as income increases
- Balancing retirement saving with other financial goals
- Beginning to refine your target retirement date and income needs

### **Pre-retirement primary focus — preservation with growth**

With retirement on the horizon, your portfolio should balance the continuing need for growth with greater emphasis on capital preservation. The increasing allocation to bonds and cash equivalents can provide more stability and income, while still maintaining enough exposure to stocks to help your portfolio keep pace with inflation.

Pre-retirement planning involves:

- Developing a more specific retirement income plan
- Considering whether to shift some assets to guaranteed income sources
- Preparing psychologically for the transition from accumulation to distribution

## Early retirement primary focus — income and stability

The early years of retirement represent a particularly critical period for your portfolio. Taking substantial losses during this phase can permanently impair your retirement security due to sequence-of returns risk.

Early retirement considerations include:

- Implementing a sustainable withdrawal strategy
- Positioning assets for tax-efficient withdrawals
- Maintaining sufficient growth potential for later retirement years

## Monitoring and rebalancing

Once you've established your retirement investment strategy, regular maintenance ensures it continues to serve your goals effectively.

Portfolio monitoring involves reviewing your investments periodically — typically 2-4 times per year — to ensure they remain aligned with your goals. Focus on whether your asset allocation remains in line with your targets rather than obsessing over short term performance of individual investments.

Rebalancing involves periodically adjusting your portfolio back to your target asset allocation. Without rebalancing, your portfolio will naturally drift toward higher-performing assets, potentially increasing risk beyond your comfort level.

Several rebalancing methods can be effective, including calendar rebalancing (adjusting at set intervals) and percentage-of-portfolio rebalancing (triggering adjustments when asset classes drift beyond predetermined thresholds).

Effective portfolio maintenance requires:

- Regular but not excessive monitoring
- Disciplined rebalancing to maintain your target allocation
- Focus on your overall strategy rather than individual investments
- Avoiding emotional responses to market movements

# Common mistakes to avoid

Learning from the mistakes of others can help you avoid costly errors in your retirement investing journey. By understanding these common pitfalls, you can develop strategies to overcome them.

Emotional decision-making represents perhaps the most significant challenge for many investors. This includes panic selling during market downturns, chasing performance by investing in recently successful sectors or funds, and attempting to time the market based on headlines or predictions.

Inadequate diversification leaves your portfolio vulnerable to specific risks that could be mitigated. Common diversification mistakes include overconcentration in employer stock, home country bias (insufficient international exposure), and focusing too heavily on familiar sectors or companies.

Cost inattention gradually erodes returns over time. This includes ignoring expense ratios when selecting funds, paying for active management without sufficient value to justify the higher costs, and excessive trading leading to commission costs and tax inefficiency.

Mistakes to avoid in retirement investing:

- Making decisions based on emotions rather than your long term plan
- Concentrating too much of your portfolio in a single investment
- Paying excessive fees or trading costs
- Mismatching your risk level with your time horizon
- Ignoring tax consequences of investment decisions

# Next steps in your retirement journey

Building and managing a retirement investment portfolio is an ongoing process. Here are practical next steps to implement what you've learned from this guide.

Begin by taking inventory of your current retirement accounts and investments. Calculate your current asset allocation across all accounts to understand your starting point. Review expenses on your existing investments to identify opportunities for cost reduction. Set up automatic contributions to retirement accounts to ensure consistent investing.

In the near term, develop or revise your investment policy statement based on the principles covered in this guide. Adjust your portfolio to align with your target asset allocation, making changes gradually if significant shifts are needed. Establish a regular portfolio review schedule with calendar reminders to ensure consistent monitoring.

For ongoing development, continue your investment education through books, courses, or podcasts from reputable sources.

Consider whether working with a financial advisor would benefit your situation, particularly if you have complex needs or struggle with investment discipline.

Many excellent resources can support your continued learning about retirement investing. Books like "The Bogleheads' Guide to Investing," "A Random Walk Down Wall Street," and "The Four Pillars of Investing" provide solid foundations in investment principles.

Websites like [Investor.gov](https://www.investor.gov) (SEC's educational website) and your 401(k) provider's educational resources often offer free, unbiased information.

Remember that successful retirement investing is not about finding the perfect investment or timing the market perfectly. It's about creating a sensible plan based on time-tested principles, implementing it consistently, and maintaining the discipline to stick with it through market cycles.

The journey to retirement security is a marathon, not a sprint. Each step you take to implement sound investment practices brings you closer to your goal of a financially secure retirement.



# Conclusion

Investing for retirement doesn't need to be complicated. By understanding the basic investment options — stocks, bonds, index funds, target-date funds, and annuities — and applying key selection criteria like risk tolerance, time horizon, and cost awareness, you can build a portfolio that serves your retirement needs.

Remember these key takeaways:

1. Start early and contribute consistently to harness the power of compound growth
2. Diversify across asset classes to manage risk while pursuing returns
3. Keep costs low through index funds and careful investment selection
4. Match your investments to your time horizon, taking more risk when retirement is distant
5. Create a written plan and stick to it through market cycles
6. Rebalance periodically to maintain your target asset allocation
7. Adjust your strategy as you age, gradually focusing more on income and preservation

Your specific investment approach will depend on your personal circumstances, but the principles outlined in this guide apply universally. Whether you choose a simple target-date fund or build a custom portfolio, understanding these fundamentals will help you make informed decisions.

The ultimate goal isn't to beat the market or impress others with sophisticated strategies — it's to build sufficient resources to fund the retirement lifestyle you desire. By focusing on what matters most and avoiding common pitfalls, you can join the ranks of successful retirement investors who achieve financial security and peace of mind.

# Your next steps

Knowledge is only valuable when put into action. Now that you understand the basics of retirement investing, it's time to take concrete steps toward securing your financial future.

## **Start today, not tomorrow**

The power of compound interest means that even small actions taken today can have tremendous impact on your retirement security. Don't wait for the "perfect time" to begin — the best time to start is now.

## **Schedule your retirement check-up**

If you already have retirement accounts, set aside 60 minutes this week to review your current investments, contribution rates, and allocation strategy. Are they aligned with what you've learned in this guide?

## **Boost your contributions**

Consider increasing your retirement contributions by just 1–2% of your income. You likely won't notice the difference in your paycheck, but over decades this small change can significantly enhance your retirement lifestyle.

## **Speak with a professional**

A qualified financial advisor from Farther can help you create a personalized retirement plan tailored to your unique situation and goals. Many offer complimentary initial consultations to discuss your needs.

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