Reallocate Your Portfolio Before The Next Wave Hits

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Bob Weir, CFA: Director of Research

Reallocate Your Portfolio Before The Next Wave Hits

By Jim Pearce (bio at end)
July 13, 2018

Yesterday, I addressed a reader's question regarding the apparent absence of inflation despite central banker intervention that has pumped trillions of dollars into the global economy. I surmised that inflation has occurred as a result, but primarily in the form of share price appreciation in large-cap stocks that have been buying back their own shares, and not as much in the cost of products tracked by the Consumer Price Index.

Today, I will address a separate, but in my opinion, related question since I expect inflation to migrate out of stocks and into the overall economy as global trade tensions heat up. If enough companies either cut back on their stock repurchase plans or discontinue them all together in response to declining sales from overseas, that may trigger a stock market correction.

Here is the reader question for today: (BW: a 401(k) is similar to a Canadian RRSP)

> "How many times do you recommend a person change his asset allocations in a 401(k)? I heard in the past people say pick it and forget it. I think it is important to constantly stay up-to-date on what is going on and how the market looks to be shaping up!"

As a long-time financial planner, I do not buy into the conventional wisdom that you should only review the asset allocation of your retirement account on a rote schedule, such as annually. That approach may be worse than not doing it at all since it encourages reactive behavior that can lead to poor decisions.

Too many investors make the mistake of reviewing the past one-year and five-year performance figures and emphasize the funds with the best track records. That is sometimes referred to as "rear-view mirror" investing, and often results in a portfolio being concentrated in investments that have become over-valued and likely to under-perform in the future.

For that reason, I prefer a proactive approach that makes adjustments based on the relative value (and potential risk) of the investment choices available. If you believe, as I do, that high-multiple growth stocks are at greater risk of rising inflation than low-multiple value stocks, this determination should drive the asset allocation process more than long-term historical performance figures.

Also, if you think inflation is likely to rise soon, shifting money into investments that should benefit from inflation is a good idea, even if their recent track record is relatively poor.

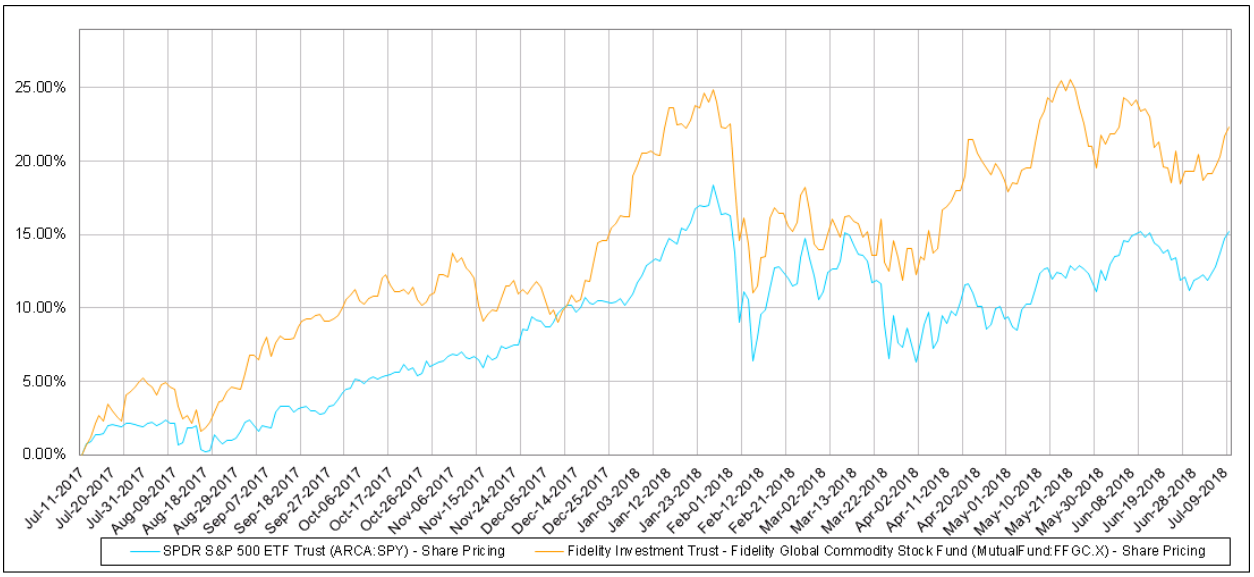
For example, the WisdomTree Continuous Commodity ETF (GCC) has performed horribly over the past five years, losing more than a quarter of its value while the tech-heavy Invesco QQQ Trust (QQQ) has more than doubled in value.

However, if inflation does pick up soon, the direction of each fund could quickly reverse. The problem for most investors is that it is difficult to make that adjustment until after the likelihood of its occurrence has already been proven. By then, much of the value of making such an exchange has already been realized.

That is why I have already made that adjustment to the asset allocation model I use in *Personal Finance*.

If you fear the opportunity cost of making such a move prematurely may be greater than the benefit of avoiding a potential loss later, there may not be as much risk as you think.

For example, over the past 12 months, the **Fidelity Global Commodity Stock** (FFGCX) fund that I use for that purpose in my Maximum Income Portfolio has gained 22% while the **SPDR S&P 500 ETF** (SPY) is up 15% (including dividends).



With 35% of my current asset allocation in Inflation Hedges, this portion of my portfolio is actually making the biggest contribution to my overall return, while providing protection against rising interest rates that inevitably accompany higher inflation.

Point being, don't wait until after rising inflation has already eaten into your hard-earned gains. More importantly, don't put even more money into over-priced asset classes the next time you get around to rebalancing your portfolio.

The time to reallocate your retirement account is now, as investors face a major market shift.

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About the Analyst

Jim Pearce
Bio | **Archive**

Jim Pearce is the Chief Investment Strategist of *Personal Finance*, our flagship publication. He is also the Director of Research at Investing Daily, overseeing the work of our entire analyst team. He began his career as a stockbroker in 1983 and over the years has managed client investment portfolios for major banks, brokerage firms and investment advisors. Jim has a BA in Business Management from The College of William & Mary, and a CFP from the College for Financial Planning.