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The Basics of Saving and Investing for Retirement

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By Nanci Hellmich

Figuring out the best investment strategy for your retirement savings can be challenging.

There's no one-size-fits-all strategy, either in choosing an investment plan or using a management style. Some people want to invest aggressively for potential growth, while others take a moderate approach. Some are conservative with their assets.

Some savers learn all they can about their companies' retirement plan options so they can take a hands-on approach to investing; others want to be less involved.

No matter which approach they take, most people benefit from learning more about their investment options. It's a good idea to develop a personal strategy, based on your age, life situation, risk tolerance, and other factors, says Brian Eichler, a senior team leader on CAPTRUST's Advice & Wellness team.

The Importance of Saving

Both retirement counselors emphasize that saving is key to financial wellness. "Saving is the driver," Eichler says. "I can build you a portfolio that might be a Ferrari, but if you don't put gas in the tank, it's not going anywhere."

He suggests retirement plan participants use CAPTRUST's [Total Retirement Planner calculator], as well as the other calculators on [captrustadvice.com], to figure out their saving and investing status.

When participants review their portfolios, many discover they need to pump up their savings. Eichler advises participants to work up to saving 10 to 15 percent of their gross incomes for retirement.

For some people, increasing their contributions to a retirement plan won't make a big difference in their paychecks. Eichler recently talked to a 40-year-old woman who was saving 6 percent of her gross income for retirement, and her company was matching 3 percent, totaling a 9 percent income allocation to her 401(k) plan.

He calculated that increasing her retirement contribution by 1 percent this year would reduce each paycheck by only $20. He encouraged her to consider having her company automatically increase her retirement deduction by 1 percent a year for the next few years until she reached a 15 percent contribution rate.

Eichler told her she was in a good position to increase her retirement savings because she had $25,000 in an emergency fund, which would cover several months of her expenses if she had a personal emergency.

One general rule of thumb: Keep enough money in an emergency fund to cover three to six months of income. This may prevent you from having to take a distribution from your retirement account before age 59 ½, because tax consequences and penalties may be imposed on early withdrawals.

How to Build Momentum

Ranson urges people to start saving as early as possible. It's better to begin with something small now than wait until you're 45 to get started.

She recently worked with a woman in her 30s who was paying off debt and was concerned that she'd never be able to retire because she wasn't saving. Ranson showed her that putting as little as 3 percent of her income into her company's retirement plan now could make a big difference in her nest egg at age 80.

"It's like a snowball. If you start on the top of the hill, it's going to get big by the time it gets to the bottom. But if you start in the middle, it won't grow as much," she says.

She suggests folks bump up their retirement contributions when they get a salary increase so that they don't feel as much of a pinch in their take-home pay.

Gauging Risk Tolerance

When it comes to allocating their retirement funds, many people aren't sure which investments are best for them. The advisors ask participants a series of questions to evaluate their risk tolerance—their comfort levels with the stock market's volatility. The advisors use the answers they receive to point out different investment options in participants' retirement plans.

All plans offer a selection of mutual funds, which allow people to own shares of stocks in many different companies, Eichler says.

If participants want to build their own portfolios, they typically can choose between actively managed mutual funds or passively managed, low-cost index funds, he says. In an actively managed fund, the fund managers pick stocks, bonds, or other securities. Index funds invest in securities that are included in an index, such as the S&P 500, an index of large U.S. companies.

Eichler encourages people to invest in a diversified portfolio with a mix of mutual fund investments across asset classes—large-cap stock funds, mid-cap stock funds, small-cap stock funds, international stock funds, a bond fund, and cash. Diversification means not putting all your assets in one place.

One option that many people consider is their retirement plans' target date funds, which are professionally managed funds designed to provide a diversified mix of stocks, bonds, and cash, he says.

The “target” in a target date fund is normally the year in which a person plans to retire or the year he or she turns 65. For instance, if you are going to retire in 2045, you’d invest in a 2045 target date fund.

The asset allocation in these funds adjusts over time to become more conservative as investors near retirement age. These funds are appealing to people who don’t want to take an active role in their retirement investment strategy, Ranson says.

Some investors are very risk-averse and want to avoid the ups and downs of the stock market, so they may put their money in capital preservation–oriented funds, which include money market accounts, stable value, or other low-risk investments. The downside is their money is not growing at a rate that meets or beats inflation, she says.

The Benefits of Roth Savings

Some participants are interested in Roth accounts, the experts say. Roths, whether 401(k), 403(b), or IRAs, are all designed to allow investors to grow their money on a tax-free basis.

Roths are funded with after-tax money, meaning the taxes are paid on the income when it is earned. Once the money is in the account, the compounded earnings are distributed tax-free later, as long as the investor meets certain requirements, Eichler says.

Finding the Best Fit

Overall, when choosing an investment strategy, people have to decide what works for them. “At the end of the day, we want to come up with a plan the investor feels comfortable with—one that is going to be the best fit for them,” Ranson says.

Eichler agrees. “You want to invest in a way that lets you sleep at night.”

His advice to participants: “If you have a question you’ve been wondering about, don’t keep wondering. Pick up the phone and call us.”

Have questions? Need help? Call the CAPTRUST Advice Desk at 800.967.9948, or schedule an appointment with a retirement counselor today.