

FUND TRACK

# Shopping at 'Target,' Mutual-Fund Style, For Retirement

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Simplicity isn't a word that most people associate with investing.

That goes a long way toward explaining the rising popularity of mutual funds designed to provide one-stop shopping for retirement investing.

The funds, known as "target date" or "lifecycle" funds, simply require investors to pick one that comes closest to their expected retirement date and let professional money managers do the rest. The managers promise a ready-made portfolio of stock and bond funds that gradually becomes more conservative as the investor gets closer to retirement.

But a peek under the hood of these funds, which held \$40 billion in assets at the end of November, shows that they differ substantially in investment strategy, asset mix, fees and performance. Among funds targeted for the year 2030, for example, T. Rowe Price Group Inc. was the performance leader with a 14.2% gain last year, while Fidelity Investments' no-load version of its 2030 fund lagged with a return of 10.5%, according to fund tracker Morningstar Inc.

Target-date funds "can be significantly different," says Kerry O'Boyle, a fund analyst at Morningstar.

The funds are the latest incarnation of those intended to provide investors with instant asset allocation between stocks and bonds. The earliest were balanced funds, which typically put 60% of assets in stocks and 40% in bonds. In the early 1990s, fund companies began to roll out offerings in which investors could choose a preset mix of funds to match their risk tolerance, whether it be "aggressive" or "conservative."

Some see target-date funds as a better mousetrap. "Everybody can grasp the concept of 'I hope to retire in 30 years,'" says Michael Francis, a retirement-plan consultant based in Hartland, Wis. "Risk tolerance is kind of a fluffy concept. You ask people 'What's your risk tolerance?' and their answer is usually 'I don't know.'"

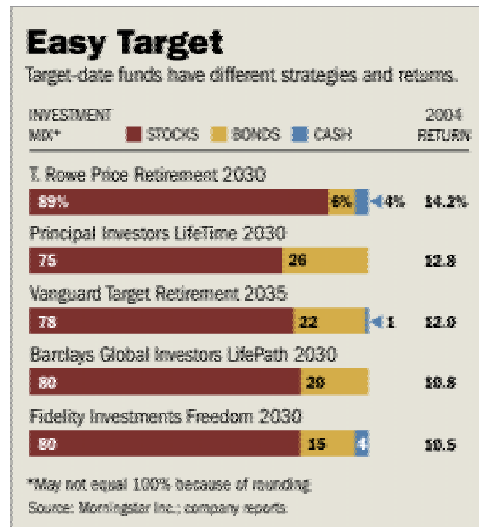
More than a dozen fund firms offer target-date funds and they are growing fast. In the first 11 months of 2004, investors put \$13 billion of new money into target-date funds, double the pace of 2003, according to Financial Research Corp. Five years ago, the funds had just \$6.7 billion in assets.

The funds are attracting investors rolling money out of 401(k) plans and into individual retirement accounts as well as investors in 401(k) plans themselves. Employers are increasingly making target-date funds the default option in 401(k) plans. At the end of November, 632 such

plans designated Fidelity's target-date funds, called Freedom Funds, as the default option, more than double the number just two years ago. Fidelity now has more than \$28 billion under management in all of its Freedom Funds.

Even the federal government's Thrift Savings Plan, which has been touted as a model for proposed Social Security private-investment accounts, is planning to add target-date funds this year.

"There is a significant group of people that just don't want to make these decisions," says David Cvengros, an executive with Barclays Global Investors, which rolled out its target-date fund of funds in 1994. (Barclays says its offerings were the first of the kind.)



The general principle is that the longer the time until retirement, the greater the percentage of assets that will be invested in stocks, and the fund's bond holdings grow as retirement draws near.

The allocation, however, varies from fund to fund. For investors expecting to retire in 2030, Vanguard Group's fund provides a blend of 80% stock funds and 20% bond funds. The 2030 fund run by T. Rowe Price, however, intends to hold 90% stocks, based on the firm's research suggesting that investors need to rack up higher returns to amass the sums of money needed for retirement at a time when people are living longer.

Some lifecycle funds are designed to provide income and stability for people already in retirement, and the variations among these are even greater. Vanguard's version holds 20% in stock funds, 75% in bond funds and 5% in a money-market fund; Putnam Investments' fund is a mix of 25% stock funds, 45% bond funds and 30% in a money-market fund.

T. Rowe Price, meanwhile, offers a fund for retirees with 40% in stocks, 30% in bonds and 30% in short-term bond and money-market funds. Retirees can also hold on to T. Rowe Price target-date funds, which continue to shift toward a more conservative mix for 30 years after retirement, eventually reaching 20% in short-term bond

and money-market funds, 60% in other bond funds and 20% in stock funds.

There are considerable differences in the underlying investments as well. Vanguard's target-date funds hold just four or five of its broadest-based index funds, as a way to keep costs to investors low and avoid the risk that comes with having active management of a fund, says Catherine Gordon, director of Vanguard's investment counseling and research group. "It significantly reduces the risk that someone runs into bad luck," she says.

But Fidelity's 2030 fund holds 18 actively managed Fidelity funds, seven of which are large-cap funds and five of which focus on international stocks. Barclays takes a middle road, investing its funds in "enhanced index" funds, where portfolio managers make bets on individual stocks in an index in an effort to slightly exceed the index's performance. Wells Fargo Funds, meanwhile, takes the unusual approach of investing in individual stocks and bonds, rather than its funds.

Some fund companies also levy an additional charge to investors, on top of fees they collect for running the underlying funds. Putnam charges investors an extra 0.05% of assets and Fidelity adds 0.08%. That money can add up. In the 12 months ended March 31, Fidelity collected \$15.3 million for the asset-allocation services provided for its 10 target-date funds.

Fidelity says the added fee is justified by the additional work the Freedom Funds portfolio manager does, making the target-asset allocations called for by the firm's model and adjusting the mix based on his view of the market. "That's the greatest added value we provide," says John Sweeney, a senior vice president of mutual-fund product development at Fidelity. Putnam, meanwhile, says the additional fee covers the costs of running the target-date fund as well as portfolio management.

However, many others, such as American Century Investments, Vanguard and T. Rowe Price, don't charge an additional fee.