

Protect Yourself from Identity Theft

I like to think I'm pretty scrupulous about avoiding identity theft. I try to shred anything that comes into my house with my name on it, I'm on my guard when conducting transactions online, and I ask questions before I give anyone personal information they may not need. (This is more of a privacy point than one about identity theft, but is anyone but me stunned at the number of people who blurt out their phone numbers when a random retail salesperson asks them for it?)

I recently attended an identity-theft seminar, however, and was surprised at how much I learned. That's because identity thieves are constantly evolving their practices. Just as soon as we consumers get up our guard against one type of identity theft, criminals seem to come up with a workaround.

For that reason, I'm devoting part of this month's issue to making sure you're staying one step ahead of the identity thieves. Not only are identity thieves using new methods that you need to be aware of, such as "skimming" and "pretexting," but identity theft has been spiking amid the faltering economy. Reported cases of identity theft increased to nearly 10 million in 2008, according to Javelin Strategy & Research, up 22% from 2007. Scammers steal personal information to rent apartments, open new credit cards, obtain health insurance or health care, establish utilities, or even obtain employment and loans. That fraud, in turn, exacts an enormous financial and emotional toll on those who are

scammed. On the plus side, the amount of dollars ripped off in each incident has dropped sharply, to roughly \$500 per incident, in part because consumers have become far more vigilant about staying alert for signs of identity theft and promptly reporting cases to authorities.

In the pages that follow, I've provided you with a comprehensive set of strategies for safeguarding your identity, whether you're at home, online, or out and about.

Track Your Statements

One of the best ways to be pre-emptive about identity theft is to scrutinize the transactions on your bank and credit card statements to ensure that they're in line with the transactions you've made. And if you identify a discrepancy, notify the financial institution immediately, first via phone call and then by certified mail, requesting a return receipt.

If you identify unauthorized charges on your credit card bill and notify your card company within 60 days of receiving the statement, your liability will be limited to \$50 per card. If you identify unauthorized transactions involving your debit or ATM card, time is of the essence. Your liability will be limited to \$50 if you notify your bank within two days of discovering the unauthorized transaction; if you notify the bank between two and 60 days of discovering the discrepancy, your liability jumps up to \$500. If it takes you more than 60 days to notify your bank of the unauthorized debits, you're on the hook for any losses in your account.

Note that if your ATM or debit card carries the Visa or Mastercard logo, and many of them do, your liability is in most cases limited to \$50 per card,

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regardless of how long it takes you to report the fraud to your bank. Still, for everyone's sake, it's best to report a problem as soon as you identify it.

In addition to combing your statements to make sure that all of your debits and credits are truly yours, I'd also recommend tracking the dates you receive your statements for the next month. That will give you an idea of when to expect them in future months. If you don't receive a credit card, bank, or other financial statement within two or three days of when you normally receive it, contact the bank or credit card company to let them know. Identity thieves have been known to steal financial statements out of the mail to obtain personal information, and if they've stolen your identity they may divert mail to another address. They may also steal newly issued credit or debit cards from the mail.

Reduce Your Reliance on Snail Mail

There's something comforting about receiving paper statements in the mail. For financial assets, that paperwork may seem like black-and-white, tangible proof that you truly own what you own.

That sense of security provided by paper is largely illusory, however. In fact, provided you've taken steps to secure your at-home network (more on this in a minute), conducting your financial transactions online is safer than using paper statements and checks. The reason is simple: When your financial transactions are passing from mailbox to the postal service back out to another mailbox, identity thieves have more opportunities to put their hands on your

personal information. And unless you shred everything that comes into your house, identity thieves can also sift through your trash in search of documents with your personal information and account numbers.

It's hard to eliminate snail mail from your life entirely, though, and some of you simply may not be ready to make the leap to online banking and bill-paying. Thus, it pays to take precautions when sending financial information through the mail. If you're receiving checks from your employer or a financial institution, use direct deposit rather than having checks mailed to your house. If you're ordering blank checks, arrange to pick them up at the bank rather than having them sent to your home. Always put your outgoing mail in a U.S. Postal Service mailbox rather than in your own home mailbox or the outgoing mailbox at your office. I also recommend that you skimp on putting extra identifying information like phone numbers and account numbers on your envelopes, even if the financial institution or utility asks you for it.

Set Up a Secure Online Security System

As I noted, managing your financial transactions online can be safer than doing so via the mail. The essential ingredient, however, is an up-to-date security system for your home computer network, including anti-virus and anti-spyware software as well as firewalls. A good spam filter can also help ensure that you don't receive a lot of scam e-mails. Although these programs have gotten easier to use, they can still be cumbersome and require that you update them periodically. If you're not comfortable

To stop Windows from "remembering" your passwords:

- ① In Internet Explorer, click on the **Tools** menu from the top of your screen. Then click on **Internet Options** in the dropdown menu.
- ② Click on the **Content** tab. Click on the **Auto-Complete** button and the **AutoComplete Settings** screen appears.
- ③ Uncheck the box that says **User names and passwords on forms**, then click **OK**.

To password-protect Microsoft Excel and Word documents:

- ① With a Word or Excel document open, click on the **Tools** tab.
- ② Next click **Options** in the dropdown menu. Click on the **Security** tab and enter your password, then click **OK**.

Watch Out for These Common Types of Identity Theft

Dumpster Diving

WHAT IT IS_ Thieves steal personal information from garbage, recycling bins.

AVOID IT_ Shred account statements, bills, credit card solicitations.

Medical Identity Theft

WHAT IT IS_ Thieves steal your identity to obtain insurance, medical care in your name.

AVOID IT_ Safeguard your insurance card, review health-insurance claims carefully.

Phishing

WHAT IT IS_ Legitimate-looking e-mail or Web site asks you to supply personal information.

AVOID IT_ Never supply personal information when solicited via e-mail or online.

Pretexting

WHAT IT IS_ Scammer lies about identity in an effort to obtain your personal information.

AVOID IT_ Don't give out personal information unless you've initiated the contact.

Skimming

WHAT IT IS_ Applies to theft of credit or debit card numbers for fraudulent purposes.

AVOID IT_ Stay alert at point of sale; watch out for unusual devices attached to ATM machine, gas pump.

Pharming

WHAT IT IS_ Secretly directs you from a legitimate Web site to a scammer's site.

AVOID IT_ Look for padlock icon, "https" in the URL; keep security software up to date.

Shoulder Surfing

WHAT IT IS_ Thieves obtain PINs, account numbers by looking over your shoulder.

AVOID IT_ Shield ATM machine with your body, conceal credit card number from others in store line.

setting up these systems and doing what you need to do to keep them up to date, hiring a computer consultant to come into your home to do it for you can be well worth the money you'll spend.

Because you can't be sure about the quality of the security software on computer systems that aren't your own, be careful about accessing financial information when you're away from home. And never, ever log on to any of your financial accounts using a public or unsecured network.

Be Password-Savvy

Also be careful with the passwords you use, particularly on sites where you conduct transactions or provide personal financial information. Don't use obvious passwords, such as the name of your spouse or pet, or your birthday; that makes it easy for identity thieves to guess at yours. Also don't use the same password again and again. The hardest-to-hack passwords are gibberish or use a combination of numbers and letters.

Windows will ask you whether you want it to "remember" your passwords, and then it will populate the password field automatically. That makes it a lot easier to surf online, but be careful when using this

feature. Use it only when you're on sites that don't store sensitive information, such as your local newspaper's site, rather than on sites where you actually execute business transactions. You can also shut off the Windows feature that asks you whether you want it to remember your passwords. I've included details on how to change this feature on Page 2.

Using "password manager" software is another way to guard against phishing and other online scams. These programs store your user names and passwords and encrypt your information so it's not accessible to hackers; however, these programs may not be able to handle some of the more complicated password formats that some banks require.

If you manage your various user names and passwords on your own, perhaps by maintaining a Microsoft Word or Excel document on your computer, take care to ensure that document's safety. If your workstation doesn't require a password to log on, take the step of password-protecting your document. I've included details on how to password-protect Microsoft Word documents and Excel spreadsheets on Page 2.

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Shop Safely

In addition to keeping your home computer's security system up to date, you should take steps to help prevent fraud while shopping online. Make sure you have the latest version of your Internet browser, because newer versions often incorporate the latest in encryption technology. In addition, there are a couple of signals to look for to indicate that you're shopping safely. On any screen where the vendor requests that you input passwords, your name and address, credit card number, or any other identifying information, the URL in your browser window should read "https" rather than "http." In addition, you should see a small yellow padlock icon toward the bottom right corner of your screen. If you're not sure your information is adequately protected, call the company and tell it about your concerns.

Once you make an online purchase, print out the confirmation and be sure you have the vendor's name, address, and phone number. Also be on high alert if a vendor you've never heard of has a price on an item that's far below the selling price everywhere else. You may indeed have found the deal of the century, but it could also be a red flag that the merchandise is counterfeit or the vendor isn't legitimate. Do a little more research before supplying your credit card number.

In addition, you're usually better off, from a security standpoint, using a credit card rather than a debit card when transacting online or in a store. As I mentioned above, debit card holders who don't report the problem within two days of discovering it could be on the hook for as much as \$500. On a more basic level, credit card holders whose accounts have been tampered with have an important lever that debit card holders do not have. If someone has made a fraudulent transaction on your credit card, you may simply refuse to pay the bill until the problem gets resolved. But if someone has taken money out of your account or made a purchase using your debit card, the onus is on you to get the money back.

If you're shopping in stores or dining out, you also need to take steps to protect your sensitive financial information. Guard your credit card number when

standing in line at a store, and make sure your credit card doesn't leave your sight for an extended period of time (though it's inevitable that restaurant servers take your credit card away from the table to process your transaction). Also be leery of hand-held card-processing machines, which can be devices to "skim"—meaning that the store employee makes a copy of your account number with an eye toward fraudulently using it later on.

Carry as few credit cards as you'll need, hold on to your receipts when you return home, and shred them. As an additional safeguard, write "Check ID" alongside your signature on the back of your credit card. You'll have to produce your driver's license each time you transact with that card, but the ID check will provide an additional safeguard that you're the only one who can use the card.

Don't Call Us, We'll Call You

Also be on high alert if someone saying they're from a bank, government agency, or law enforcement calls you and requests personal or financial information. These entities don't typically do this. Ask the caller to send you more information in writing, or, if you're concerned there's a problem with one of your accounts, look up the financial institution's phone number in your files or on the back of your credit card and place the call yourself. Don't use a phone number supplied by the person who called you, and don't assume the call is legitimate simply because your caller ID readout matches where the person says they're calling from. (Identity thieves can mock up their caller ID readouts.)

Also avoid making charitable donations over the phone. Instead, go to the charity's Web site or request that the information be sent to you in the mail.

Take Care with Health Care

Medical identity theft can take a number of different forms, and that's partly why it's a "growth" area of the identity-theft world. Criminals can pilfer your insurance information to obtain treatment or prescription drugs, or they may file fake claims to obtain payouts from insurers. Not only can this type

Ten Ways to Protect Yourself from Identity Theft Today

What You Can Do | Why You Should Do It

- 1 **Switch to online banking.** | Less personal information in the mail means thieves have fewer chances to obtain your information.
- 2 **Check your computer security: Spyware, firewalls, antivirus, and spam filters.** | Online transactions are only safe if your security system is up to date.
- 3 **Track the dates when you typically receive bills, statements.** | If a bill or statement hasn't arrived, you can alert the issuer promptly.
- 4 **Use direct deposit for checks.** | Identity thieves target mailed items that look like checks.
- 5 **Turn off the "Remember Your Password" feature in Windows.** | Makes it harder for identity thieves to click through for your personal information.
- 6 **Password-protect sensitive documents.** | Protects you in case someone improperly gains access to your computer.
- 7 **Use credit rather than debit when shopping.** | Consumer protections are generally greater for credit cards than debit.
- 8 **Write "Check ID" on the back of credit card.** | Vendor will have to ask for photo ID before accepting your card.
- 9 **Scrutinize health-care statements.** | Medical identity thieves can masquerade as you, obtain treatment or insurance.
- 10 **Carry a copy of your Medicare card.** | Original cards carry your Social Security number; you can black it out on copy.

of fraudulent activity muck up your finances and credit report, but if a criminal's medical history is commingled with your own, there's a chance you could receive the wrong type of medical treatment.

All of that makes it essential that you safeguard your health-care records and insurance information as closely as you guard other personal financial information. As with your credit and debit cards, keep close tabs on your insurance card at all times. In addition, review your health-care transaction statements as closely as you scrutinize your credit card and bank statements. If you spot anything out of the ordinary, notify your health-care provider and insurance company as soon as possible. As with financial statements, receiving claims and other medical information online is preferable to having these statements pass through the mail.

Also be careful with Medicare cards, which include Social Security numbers. One idea is to make a copy of your card, then use black marker on the copy to cover up the last four digits of your Social Security number. If you're a new patient, health-care providers may still require that you bring your original card to the office so they can make a photocopy, but after that your safer copy should be sufficient.

Mind the Home Front

Also take care when storing sensitive documents in your house. Even if you don't have a lot of people coming and going in your home, I recommend a locking file cabinet to hold any paperwork that includes your account numbers or Social Security numbers. And if you keep a master directory with your financial account numbers, by all means keep that under lock and key—either at home, in a safety-deposit box, or in a password-protected electronic version. Identity-theft experts also say you only court problems by carrying your Social Security card in your wallet; your safety-deposit box is the best place for it.

Finally, be careful about what you throw away. Good old-fashioned dumpster diving is still a popular form of identity theft; by putting all of our paper recyclables together and on the curb, many of us make it even easier for identity thieves to sort through our paperwork. That's not to suggest you shouldn't recycle but rather that you should invest in a good-quality cross-cut shredder and make liberal use of it. ■■

How to Conduct a Midyear Portfolio Review

Investment Insights | Christine Benz

Because it's possible to shoot yourself in the foot with overzealous monitoring and trading, I'm a big proponent of conducting a systematic portfolio review just a few times a year. The purpose of this portfolio checkup is not necessarily to take action but rather to troubleshoot problem spots and identify changes you may want to make as part of your rebalancing program. Here are the steps to follow as you conduct your midyear checkup.

Step 1: See the big picture.

If you're like most people, you have more than one investment-service provider, and sifting through multiple statements can be a cumbersome process. In addition, looking at your holdings in separate silos can lead to a trap that behavioral-finance experts call "compartmentalization" or "mental accounting." Those terms simply mean that investors might treat different pools of money differently based on where they hold the assets and how they got the money. For example, investors might take a more frivolous attitude toward money they won than they would toward assets they saved.

To help conduct an efficient review of your portfolio that aggregates all of your holdings, I'd recommend using an online portfolio tool; Morningstar.com's is called Portfolio Manager. There are several ways to enter your portfolio into Morningstar.com's Portfolio Manager, but the simplest is to use Morningstar's Instant X-Ray tool, found on the Tools cover page of the Web site. Simply gather up all of your holdings' tickers and the amount you have in each stock or fund, and then enter this data into the tool.

You may hit a snag, though, if you own securities that don't have tickers and therefore won't fit into Instant X-Ray. For example, Morningstar's portfolio tools don't accommodate individual bond holdings, guaranteed investment contracts, and stable-value funds (found in defined-contribution plans like

401(k) plans) and collective investment trusts or separately managed accounts.

There aren't perfect mutual fund proxies for individual bond holdings. But if you know the maturity and credit quality of a bond you own, you can use a bond index mutual fund or exchange-traded fund that occupies the same square of the Morningstar Style Box to approximate your portfolio's exposure.

Guaranteed investment contracts and stable-value funds are more tricky because there's no close analog in the mutual fund or exchange-traded fund realm. These funds invest in short-term, usually high-quality bonds and then buy an insurance "wrapper" to guarantee the principal and accumulated interest even if the bonds decline in value. Thus, they usually yield a few percentage points more than money market funds with only slightly more volatility. (Recent trouble in two large stable-value funds makes clear that these investments may not be as risk-free as some stable-value proponents had argued in the past, however.) As with individual-bond holdings, there are no perfect proxies for stable-value funds, though a short-term bond index fund such as **Vanguard Short-Term Bond Index** VBISX is as close as you're apt to come.

Company retirement plans are increasingly offering non-mutual fund investments such as separately managed accounts and collective investment trusts in

their menu of choices. Such funds aren't necessarily worse than mutual funds, and in fact may be quite strong and inexpensive, but they don't have to provide the same level of disclosure that mutual funds do. If you're able to find out who's running the fund, you may be able to do a little bit of sleuthing to identify a mutual fund that's a near-clone of the investment in your plan—for example, if you find out that a firm like Dodge & Cox is running a fund called "Core Stock" for your company, it's a good bet that fund is nearly identical to **Dodge & Cox Stock** DODGX. Use any other information you have—such as manager names, return histories, or top 10 holdings—to corroborate that the mutual fund is a good proxy for the investment in your plan.

Once you've entered all of your holdings (or proxies for them) into the Instant X-Ray tool, click "Show Instant X-Ray," then "Save Instant X-Ray Holdings as a Portfolio" (in the top right corner of the X-Ray page). You'll be asked to save your portfolio as either a "Watch List Portfolio" or a "Transaction Portfolio." The former will be adequate if you trade infrequently or want to create a one-time snapshot of how your portfolio looks now; the latter style is the better bet if you want to be able to edit your portfolio on an ongoing basis.

I recommend rebalancing only if your allocation to an asset class has veered at least 5 percentage points from your targets. If you rebalanced back to your target allocations at year-end or in early 2009, there's probably no need to make changes now. But those who haven't rebalanced recently are apt to find their portfolios light on stocks relative to their targets. If that's the case, you can undertake rebalancing now or wait until later in the year to restore your asset allocation to its target level. (Because the market has bounced significantly from its early March lows, rebalancing back into stocks doesn't seem as urgent as it did at the outset of this year; the market has done some of that work for you.) The December 2008 issue of *PracticalFinance* included advice on how to rebalance: <http://finance.morningstar.com/Download.aspx>.

Step 3: Revisit your cash stake.

In addition to checking up on your stock/bond/cash mix, also take note of how much you have in cash in dollars and cents. There are no one-size-fits-all requirements, but most retirees and those who are within a few years of retirement should aim to hold at least three years' worth of living expenses in highly liquid investments like CDs, money market accounts, and checking and savings accounts. If you build such a cash cushion and periodically replenish it, you won't have to disrupt your longer-term investments to raise cash for living expenses. (If you're retired and are drawing on a pension as well as Social Security, holding three years' worth of living expenses in cash is probably overkill. If you're not currently taking withdrawals from your portfolio to cover living expenses, holding one to two years' worth of living expenses is probably sufficient.)

Those who have 10 or more years until retirement should have at least six months'—and preferably one year's—worth of living expenses in cash or cashlike investments.

To check up on your portfolio's liquidity, look at the dollar amount you have invested explicitly in these types of assets rather than the cash position generated by Instant X-Ray. X-Ray's cash statistic might be useful from the standpoint of asset-allocation monitoring, but it encompasses straight cash

“Rebalancing back into stocks doesn't seem as urgent as it did at the outset of this year; the market has done some of that work for you.”

Step 2: Check on your asset allocation.

Once you've saved your portfolio, click on the X-Ray tab. Focus on your asset allocation, a pie chart depicting how much you have in stocks (both foreign and U.S.), bonds, cash, and other (usually hybrid securities like convertible bonds and preferred stock). From there, you can compare your current asset allocation with your target allocations.

If you don't have a target asset allocation and would like help arriving at one, refer to the August issue of *PracticalFinance*: <http://finance.morningstar.com/Newsletter.aspx>.

holdings like CDs as well as any residual cash in stock and bond mutual funds that you own. Thus, it may not provide a true depiction of the liquid investments you could tap in a pinch.

If it turns out you're light on cash or cashlike instruments relative to where you should be, Step 6, below, discusses what to look for when deciding what to sell.

Step 4: Investigate style, sector, and individual-stock positions.

Once you've assessed your portfolio's asset allocation and cash stakes, turn your attention to how your stock and bond holdings are positioned by investment style and sector. Within Instant X-Ray, you can see stock and bond Morningstar Style Boxes (two nine-square grids in the upper right corner of the X-Ray page) that depict the investment styles of your holdings. While you shouldn't expect to see an even distribution of holdings in each of the nine squares—and most diversified equity indexes will hold the bulk of their assets in the top row of the style box—you do want to take note if the majority of your holdings are huddled in one or two regions of the style box. You also want to pay attention to where the big holes are;

if you're planning to add new holdings, you can concentrate your research efforts there.

Instant X-Ray also shows you how your stock holdings are dispersed across various market sectors, as well as how that positioning compares with the S&P 500 Index's sector weightings. As with style-box positioning, you shouldn't get too worked up about some divergences, but you do want to take note of very big bets—sectors where your weighting is more than twice that of the index, for example. If you need help interpreting whether your portfolio's style and sector bets are notable, click "X-Ray Interpreter" at the top of the X-Ray page for a written explanation of what's notable about your portfolio's current positioning.

Finally, click "Stock Intersection," also along the top of the main X-Ray page, to see whether your portfolio is disproportionately skewed toward one or two individual stock holdings. This is a good way to tell whether company stock is hogging a disproportionate share of your portfolio. (As a general rule of thumb, company stock should take up less than 10% of your total holdings.)

Step 5: Examine performance.

It's a big mistake to focus too much attention on

Unhappy with Your Fund? Consider These Trades

World Stock

Janus Worldwide
JAWWX

**T.Rowe Price Global
Stock** PRGSX

+

Janus fund has a new manager, but most investors hold it at a loss.

Intermediate Bond

**Western Asset Core
Bond** WATFX

Harbor Bond HABDX

+

Western may be on the mend, but recent struggles highlight risks here.

Mid-Cap Value

**Hotchkis and Wiley
Mid-Cap Val** HWMIX

**Artisan Mid Cap
Value** ARTQX

+

Risks of H&W's contrarian approach came home to roost in 2008.

Short-Term Bond

**Fidelity Short-Term
Bond** FSHBX

**Vanguard Short-Term
Bond Index** VBISX

+

We like Fidelity fund's new manager, but bond group undergoing changes.

Muni National

**Oppenheimer Rochester
National Muni** ORNAX

**Fidelity Municipal
Income** FHIGX

+

Oppenheimer Rochester fund has always been risky risky risky.

short-term performance, but your quarterly or semiannual portfolio review should include a quick assessment of which of your holdings are providing the biggest boost to or drag on your portfolio's overall return. It's fine to glance at year-to-date performance, but focus most of your attention on the longer-term numbers—each holding's return over the past three and five years relative to that of other offerings within that same category. Also take note of absolute returns. Which of your holdings have contributed the most—or detracted the most—from your portfolio's bottom line?

Investments that have underperformed their peer groups or have generated weak absolute returns shouldn't automatically go on your sell list, however. In fact, that can be a recipe for disastrous investment returns, as funds that have been in a performance slump may in fact be poised to deliver strong returns in the future. But if you have an investment that both underperformed during the bear market and hasn't snapped back over the past few months, you'll want to be sure to check up on whether there have been any substantive changes that have undermined that holding's attractiveness.

Step 6: Review the fundamentals.

Once you've checked out your aggregate portfolio's positioning and performance, it's time to conduct a quick checkup on each of your individual holdings. At the bottom of the Instant X-Ray page, you'll see links for each of your funds or stocks; click the links to see a detailed report with data and analysis for each. Morningstar's Analyst Reports—free to Morningstar.com Premium Members—are a quick and easy way to get a handle on the key issues at most prominent mutual funds, exchange-traded funds, and publicly traded companies; our analysts will also tell you whether they think a security is worth owning or not.

If you'd like to conduct your own research on your holdings, you'll need to drill down into the data. For funds, take note of any manager changes or upheaval at the fund-company level. Also pay attention to whether a fund's investment style has changed appreciably since you purchased it: Has a once-high-quality bond fund begun buying junky credits? Don't

be alarmed if your fund has shifted style boxes, as that's a frequent outcome if a manager is using a truly active approach. More concerning are signs of true strategy shift—for example, if a once fully invested mutual fund now holds a sizable cash position.

If you own individual stocks, you already know that you'll need to exercise more hands-on oversight than is the case with mutual funds. As you assess individual stocks, take note of price multiples and profitability trends; Premium Members can also see Morningstar Ratings, moat assignments, and fair value estimates for all stocks covered by our analysts.

Step 7: Plan your next move.

After you've reviewed your portfolio's current status, it's time to plan your next move. It's not likely that you'll uncover a portfolio problem you need to address right away, but you should make sure to schedule a time to rebalance your portfolio. Conventional financial-planning wisdom holds that the best time to rebalance is at year-end, with an eye toward harvesting any losses to offset capital gains elsewhere in your portfolio. But if you'll have more time to focus at some other time of the year—say, earlier in the fourth quarter—by all means do so. ■■■

Hitting a Pothole on the Road to Retirement

Portfolio Makeover | Christine Benz

Less than a year ago, Frank and Angela Greco (not their real names) thought they were cruising into the next great phase of their lives.

Frank, 57, was employed in a sales role in the financial-services industry, while Angela, 52, had recently returned to work full-time in an administrative position at an insurance company. With all three of their children grown, out of the house, and through college, the couple was starting to dream about their next steps: retirement in less than a decade, hopes for weddings and grandchildren, and finally taking the trips they had deferred while they were raising their kids and paying for school.

Less than one year and one bear market later, this couple has seen their dreams upended. Not only has their investment portfolio taken a hit, but Frank's company was shaken badly during the mortgage crisis and subsequent market meltdown. His former employer was acquired by a larger firm late last year, and Frank's position was eliminated along with thousands of others at his company. With it went Frank's low-six-figure paycheck, as well as the couple's sanguine attitude about the future.

The Grecos have reacted quickly to make the best of a bad situation. Angela is still employed full-time and has secured health-care insurance, once covered by Frank's company, through her employer. Frank negotiated a solid buyout package, amounting to one year's worth of salary, from his former company. He has also started a computer-consulting business.

His young business hasn't come close to supplanting the paychecks he earned from his former employer, though, and he and Angela are getting nervous about what the future holds. Angela's salary barely covers the Grecos' mortgage and property taxes, so the couple has been dipping into the proceeds from Frank's

buyout package to pay for additional living expenses. Also, the couple would like advice on stabilizing their investment portfolio. Although they've recouped some lost ground over the past month and a half, their portfolio is currently worth \$800,000, down from \$1.2 million in late 2007.

The Before Portfolio

Taken together, the Grecos' portfolio has 50% in stocks and stock funds, another 25% in bonds, and the remainder in cash. Frank's 401(k) portfolio, the largest portion of the couple's assets, features a number of solid offerings from the American Funds group. Unfortunately, Frank also held a large position in the stock of his former employer in his 401(k) plan. He sold his shares in late 2008, but only after the stock had taken a drubbing. Angela's 401(k) plan, while a relatively small portion of their overall portfolio, is solid, featuring a stake in **T. Rowe Price Blue Chip Growth** TRBCX as well as a smaller stake in **T. Rowe Price Spectrum Income** RPSIX.

Frank has wisely used his IRA to shelter the bulk of their fixed-income investments, whose taxable income distributions make them a good fit within the IRA wrapper. Frank's IRA also holds a handful of income-producing stocks and smaller positions in a global-stock fund and a commodity exchange-traded fund.

The pair also has another large asset: their house, which they estimate is worth \$600,000, even in the currently depressed real estate market. They purchased their five-bedroom home in a major metropolitan area in 1996, and roughly \$125,000 remains on their mortgage. Their payments on the house, including mortgage, taxes, and insurance, amount to \$2,600 per month.

The After Portfolio

I consider the Grecos' asset allocation to be pretty reasonable for this couple. The couple's cash should cover their needs for additional income for the next few years. That means they don't have an imminent need to move additional assets into fixed-income securities, and sticking with their current asset

Adjusting to a New Reality

Frank and Angela's Portfolio: Before

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
T. Rowe Price Blue Chip Growth TRBCX	★★★★	LG	22,309	0.71
T. Rowe Price Growth Stock PRGFX	★★★★	LG	12,115	0.71
T. Rowe Price Spectrum Income RPSIX	★★★★	MU	59,248	0.70
American Funds Investment Co of Am AIVSX	★★★★	LV	174,526	0.57
American Funds Capital Income Build CAIBX	★★★	IH	169,843	0.55
American Funds EuroPacific Growth AEPGX	★★★★★	FB	96,342	0.74
American Funds High Income AHITX	★★★	LG	9,210	0.67
Loomis Sayles Bond LSBRX	★★★★	MU	93,500	0.94
ExxonMobil XOM	★★★★★	Energy	6,588	N/A
Kraft KFT	★★★★★	Consumer	11,235	N/A
Fidelity Worldwide FWWFX	★★★★	WS	23,500	1.19
iPath Dow Jones-AIG Commodity Index DJP	N/A	NR	35,000	0.75
Pfizer PFE	★★★★★	Drugs	21,090	—
Cash	N/A	N/A	115,900	N/A
Total			850,406	

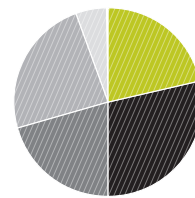
Super Sector Weighting (%)

Information	24.25
Service	32.99
Manufacturing	42.77

Top Three Sectors (%)

Consumer Svs	15.42
Health Care	14.58
Telecom	10.94

Asset Allocation (%)



- Cash 21.49
- U.S. Stock 28.70
- Foreign Stock 20.45
- Bonds 23.92
- Other 5.45

Equity Style (%)

Value	Blend	Growth	
35	30	27	Large
4	2	2	Medium
0	0	0	Small

0-10 11-25 26-50 51-100

Frank and Angela's Portfolio: After

Fund Name	Star Rating	Category/ Industry	Holding Value (\$)	Expense Ratio (%)
T. Rowe Price Blue Chip Growth TRBCX	★★★★	LG	34,424	0.71
T. Rowe Price Spectrum Income RPSIX	★★★★	MU	59,248	0.70
Harbor Bond HABDX	★★★★★	CI	100,000	0.55
Vanguard Total Bond Market Index VBMFX	★★★★	CI	75,000	0.20
Vanguard High-Yield Corporate VVHGX	★★★★	HY	25,000	0.27
Vanguard Total Stock Market Index VTSMX	★★★	LB	109,601	0.16
Vanguard Equity-Income VEIPX	★★★★	LV	100,000	0.30
Dodge & Cox International DODFX	N/A		100,000	—
Loomis Sayles Bond LSBRX	★★★★	MU	32,320	0.94
Royce Total Return RYTRX	★★★★	SV	25,000	1.12
ExxonMobil XOM	★★★★★	Energy	6,588	N/A
Kraft KFT	★★★★★	Consumer	11,235	N/A
iPath Dow Jones-AIG Commodity Index DJP	N/A	NR	35,000	0.75
Pfizer PFE	★★★★★	Drugs	21,090	N/A
Cash	N/A	N/A	115,900	N/A
Total			850,406	

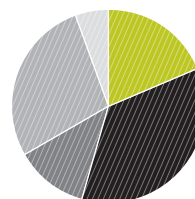
Super Sector Weighting (%)

Information	16.66
Service	42.65
Manufacturing	40.69

Top Three Sectors (%)

Health Care	16.89
Financial Svcs	15.56
Industrial Matls	13.06

Asset Allocation (%)



- Cash 18.69
- U.S. Stock 35.79
- Foreign Stock 12.20
- Bonds 27.85
- Other 5.46

Equity Style (%)

Value	Blend	Growth	
33	25	19	Large
7	5	5	Medium
2	2	1	Small

0-10 11-25 26-50 51-100

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If you're interested in seeing your portfolio featured in our Portfolio Makeover section, please e-mail me at christine_benz@morningstar.com. Rest assured that we will protect your privacy by using a pseudonym and withholding any other identifying details. Please include the following information: your fund, stock, and bond holdings, as well as the percentage or dollar value you have allocated to each, your age, a brief outline of your life experience, including your family situation and career background, details on the financial goals you would like to achieve, and your assessment of your risk tolerance.

Categories

CI Intermediate Bond	LV Large Value
FB Foreign Large Blend	MU Multisector
HY High-Yield Bond	NR Natural Resources
IH World Allocation	SV Small Value
LG Large Growth	WS World Stock

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Hitting a Pothole on the Road to Retirement
Continued from Page 10

allocation will also give their equity portfolio a chance to rebound following the bear market.

I'm usually hesitant to recommend that someone leave their 401(k) assets in their old plan, largely because many 401(k) plans charge participants additional administrative costs above and beyond what the individual funds charge; rolling over 401(k) assets to an IRA also affords far more choices than are typically available with a 401(k). In Frank's case, my major hesitation is that his 401(k) plan doesn't include as many fixed-income choices as I'd like to see.

I would also suggest adjustments to Frank's IRA portfolio. **Loomis Sayles Bond** LSBRX, while a solid fund, is too aggressive to serve as a core fixed-income holding; I would recommend reducing it and deploying

some of those assets into a wide-ranging, high-quality fund such as **Harbor Bond** HABDX.

I would also suggest that the Grecos give serious consideration to downsizing, and they say they have begun to do so. They note that they have been looking at condos and townhouses in their community and have found a few they like in the \$300,000 range. Were they to sell their home for \$600,000, they could purchase a smaller home outright, bank some cash, and get rid of their largest monthly outlay. (They would still have to pay real estate taxes and an assessment fee, but those two items would cost less than \$1,000 a month.) Not only does this step make financial sense, but it would also provide this couple with some much-needed peace of mind. ■■

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