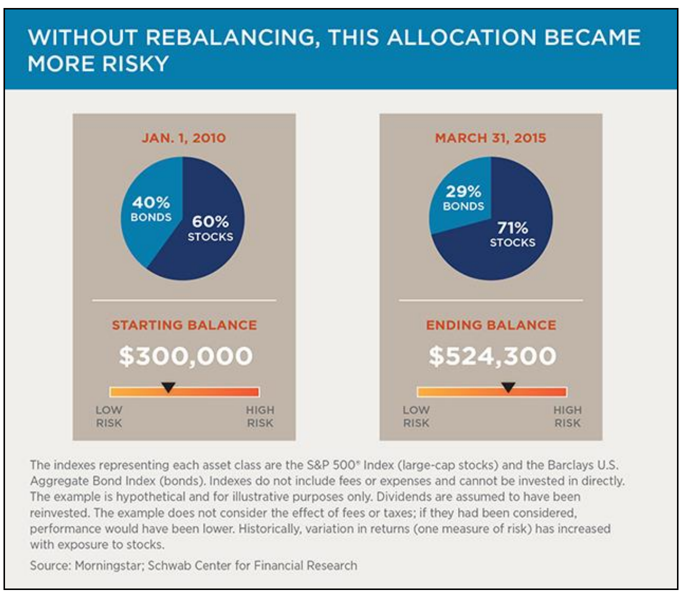
Financial Literacy Series

Taking Control of Your Financial Future

The Importance of Portfolio Rebalancing

When you invest in a portfolio, you decide how much risk you want to take by determining your asset allocation. Your portfolio asset allocation is simply the percentage of stocks and bonds you have in your portfolio. If you are younger, your asset allocation might be heavier weighted to stocks with an asset allocation of 85% stocks and 15% bonds. Since time is on your side, your risk tolerance is greater and you can afford to take on more stock exposure. As you get older, your risk tolerance might change moving you into an allocation that includes less stock and more bonds.

So what is rebalancing and why is it important? When you determined your asset allocation, you built it on your ability to take on risk. As the stock market changes, so does your portfolio asset allocation and leaving it alone could land you in a situation where you have taken on too much risk. Rebalancing is the discipline of selling some of the assets that have gone up in the portfolio in order to maintain the original asset allocation of the portfolio.



The example on the left shows a hypothetical couple who started out with a $300,000 portfolio in 2010. Their original allocation of 60% stocks and 40% bonds has delivered hefty gains since they set it five years ago. When the stock market started to rebound their portfolio grew to $524,300.

By 2015, the equity part of their portfolio grew to about 71% of their allocation, and bonds a mere 29% (a roughly 70/30 split).

By not rebalancing, this couple increased the risk in their portfolio. Rebalancing helps to mitigate that risk by bringing the portfolio back in line with the original asset allocation.

In addition to managing the risk in your portfolio, rebalancing establishes a discipline that sells securities when they are high and buys securities when they are low. The LeTort Trust Managed Portfolios are automatically rebalanced on a quarterly basis to keep your asset allocation consistent as the market changes.

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3130 Morningside Dr. Camp Hill, PA 17011 | 717.761.7626 www.letorttrust.com

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