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HOW MILLENNIAL INVESTORS CAN AVOID SABOTAGING THEIR RETIREMENT

Investing for retirement isn't something 20- and 30-somethings can afford to get wrong.

By: Rebecca Lake - February 28, 2017

When it comes to saving and investing for retirement, millennials are a mixed bag.

According to Wells Fargo's 2016 Millennial Study, 41 percent of young adults still aren't saving for their later years. Research from Fidelity shows that millennials who are saving are increasing their savings rate steadily but they're only setting aside roughly half of the 15 percent of income that's recommended for a secure retirement.

Millennials have an edge over older savers where retirement is concerned since time is on their side, but they may not always capitalize on this advantage. Avoiding certain stumbling blocks can help younger savers protect their financial futures.

Don't fall into the cash trap. A BlackRock Investor Pulse Survey revealed that millennials have the highest cash allocation of any generation, at 70 percent. That reliance on cash could have a major impact on their financial security in retirement, says Angela Coleman, a fiduciary investment advisor at Unified Trust Co. in Lexington, Kentucky.

"Consider this: a 25-year-old earning $35,000 a year, saving 10 percent annually for 40 years and earning an average rate of return will have $280,000 more in retirement than the individual who decides to sit on a cash nest egg," Coleman says.

In that context, it's relatively easy to see what a preference for cash may be costing millennials. Mike Serio, regional chief investment officer for Wells Fargo Private Bank in Denver, says young adults must consider the broader financial picture when allocating assets.

"Risky asset returns in the short term are difficult to predict, but over longer periods of time they become much more predictable," Serio says. He says millennials should be willing to embrace more aggressive choices when time is working in their favor.

Millennials who prefer cash over stocks or bonds also miss out on the power of dollar-cost averaging, says Patrick Lynch, owner of Denver-based Patrick Lynch Financial.

"Normal market cycles indicate historically that even missing a few days can cut an investor's achievable rate of return in half," Lynch says.

His advice to younger investors who may be reluctant to play the market?

"Get in and stay in," Lynch says, and remember that investing for retirement is a marathon, not a sprint.

Be realistic about your risk tolerance. Understanding your individual risk tolerance is critical for younger investors, says Paul Springmeyer, a portfolio manager with The Private Client Reserve of U.S. Bank in Minneapolis, Minnesota.

"The reason it's particularly important for young investors to be conscious of the relationship between risk and reward is that they have a considerably longer investment horizon," Springmeyer says. That in turn means that millennials have a much longer runway to create wealth.

Kyle Winkfield, managing partner of O'Dell, Winkfield, Roseman & Shipp, a financial planner in the District of Columbia, says understanding risk tolerance begins with understanding what your purpose is for saving and investing.

"It's important to decide how much money one is willing to lose, but more importantly, to find an investment philosophy that aligns with one's values and goals," Winkfield says.

Serio says younger investors also need to consider the emotional component when making investment choices and how that could inadvertently expose them to more risk.

"Given their age, millennials will be in the markets for a significant amount of time," Serio says, and it's likely that they'll experience rough spots. Young investors need to know that they worst they can do during periods of increased volatility is panic and let emotions take over.

Diversify the right way. Portfolio diversification is important at any age but younger investors need to tread carefully when venturing into the market for the first time.

Cary Guffey, a financial advisor with PNC Investments in Birmingham, Alabama, says millennials should consider mutual funds and exchange-traded funds for broad diversification with relatively low investment minimums.

"When you pick one stock, you may be hitching your cart to one horse," Guffey says. "If it turns out it runs fast, you may do well but if it pulls up lame, your account may underperform. With a fund or ETF, you have a team of horses so if any one part isn't working, you still have the rest of the team to rely on."

Dana Anspach, founder and CEO of Sensible Money, a financial planner in Scottsdale, Arizona, points to target-date funds as another option for millennials seeking increased diversification.

"Choosing aggressive investments makes sense if you have a long time to let your investments work," Anspach says. If you're not sure how to balance asset allocation, target date funds can do the work for you.

Millennials who are considering individual stocks should stick with what they know, says Brandon Moss, vice president wealth adviser management at United Capital in the Dallas area.

"People always ask questions like, "should I buy Apple (ticker: AAPL) or Google?"," Moss says. "Check your pocket or purse; if you pull out an iPhone, consider Apple. If you pull out an Android or Pixel Phone, maybe consider Google (GOOG, GOOGL)."

In other words, young investors may find it easier start with the brands they associate with and the services they appreciate. Moss does offer a word of caution for newbie stock investors, however.

"If you don't understand it, don't buy it," Moss says. "As cool as something may sound, if you can't figure out how they make money or how people use it, steer clear."

Put your employer's retirement plan to work. Transamerica's 17th annual retirement survey found that 72 percent of millennials are saving in their employer's plan. While that's encouraging, it still leaves a sizable number of young adults who aren't leveraging the power of a 401(k) or similar plan.

Marc Labadie, partner at CR Myers & Associates in Southfield, Michigan, says not contributing anything to an employer's plan is the biggest mistake millennials can make

"If they have access to a Roth 401(k), that's a great place to start," Labadie says. Millennials can create tax-free retirement money using these accounts.

Labadie acknowledges that not contributing enough to get the company match is another pitfall millennials should avoid. A 2015 Financial Engines report shows that missing the employer match could cost savers nearly $43,000 over a 20-year period.

Using your 401(k) as a piggy bank is another no-no for millennials, says Wayne Bland, a principal with Charlotte-based Metro Retirement Plan Advisors.

"While most 401(k)s have a loan provision, taking a loan from your retirement account should be a last resort," Bland says.

Millennials who borrow from their 401(k) should make every effort to pay it back as quickly as possible, Bland says. "Paying the loan back early puts those retirement savings back to work for you sooner."

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