MarketWatch
THE WALL STREET JOURNAL.

May 22, 2014, 5:00 a.m. EDT

Advice seekers retire with 79% more money

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A little help can make a world of difference.

If given a choice, would you prefer to reach retirement with 79% more money than the typical investor? Easy question, right?

Many retirement savers are given exactly this choice, yet only a third end up enjoying the extra cash. What's the difference? Prudent, high-quality advice that helped them avoid emotionally driven decisions.

Aon Hewitt, the global benefits consulting firm, studied hundreds of thousands of savers in selected companies it serviced from 2006 through 2012 — a period including the recent stock market collapse. Those who sought "help," broadly defined as using a target-date fund, a managed account or online retirement advice, did better.

Much better, in fact. A little more than one-third of retirement-plan participants, 34.4%, relied on some form of investing help and using that advice resulted in median annual returns that were 3.32% higher, net of fees.

The return difference implies a significant difference in outcomes — 79% more wealth at retirement for a 45-year-old who leaves work at 65, Aon found. In dollar terms, an investment of $10,000 would become $32,800 for the investor on his or her own and $58,700 for the person who used investment help.

Generally speaking, Aon found, younger savers used target-date funds to get that help (nearly half of the total sample used such funds). That's not a surprise, since many companies have made target-date funds automatic for new enrollees. To choose a different path would mean proactively leaving a target-date fund, and very few bother.

Enforcing discipline

You might be disposed at this point to guess that target-date funds did well by those who stayed in them, and you'd be right. Nevertheless, managed accounts, where the investor relied on a financial adviser to develop a risk-adjusted, personalized investment plan, earned 50 basis points (0.5%) more.

Importantly, this result also was net of fees. That is, they earned half of 1% more even after subtracting the cost of the adviser. Unsurprisingly, older savers with higher balances preferred an adviser over a target-date fund.

In part, advisers did better by using more refined approaches but also because an adviser is there to enforce discipline in tough markets. If you can literally ignore your target-date fund for years and through all markets and it's cheap enough, that's probably a good choice for you.

It's when the market tips into a swift decline that your theoretically stiff upper lip gets tested. A well-designed, risk-adjusted basket of low-cost index funds plus professional oversight gives you the best of both worlds — cheap *and* effective, especially in markets where you might be tempted to cash out of a target-date fund.

Bad things happen, and often we make them worse. Six in 10 investors on their own were taking on inappropriate levels of risk, Aon found. Investors over the age of 50 exhibited the widest variety of inappropriate risk-taking. Some were exposed to risks higher than that of a 100% stock portfolio, making them exceedingly vulnerable to a market decline when they could least afford it.

Volatile times

In practice, however, even target-date fund users take on unusual risks by being inconsistent. Many savers split up their portfolios, using target-date funds for some of the money and managed account strategies for the rest, Aon found.

That might feel like putting your eggs in different baskets. In fact, using a mix of styles signals confusion. It quickly becomes impossible to accurately judge risk, leading many to make poor decisions in volatile times.

As a result, a strong majority (61.8%) who used target-date funds for only part of their portfolio ended up inappropriately invested for their age, either exposed to too much risk late in their careers or too little risk when young. Their median annual returns were 2.44% lower, again net of fees.

If you invest completely on your own, your return without at least some kind of steady portfolio help could easily turn out to be dismal. You might have a portfolio that seems appropriate for your needs yet, underneath, is built to disappoint.

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