EPH
EXPAT PENSION HOLLAND

LIFE CYCLE INVESTMENT FUNDS

'AS GOOD AS IT SOUNDS?'

Life Cycle Funds in General

Life Cycle Funds are Investment Mix Funds that automatically reduce the risk as the owner ages. The central approach is the longer the investment horizon, the higher the acceptable risk.

The positive aspect of these funds is that thus you have no risk problem if you forget to pay attention to your portfolio. Which happens more often than you would imagine.

These funds are often used in the context of Pensions, Mortgages or Private Investments and can be advisable if implemented correctly.

Additional risk reduction is possible by not investing a large capital at once but to periodically invest smaller sums.

Life Cycle Funds are not suitable for 'investors' who like to prevent any kind of risk. For them there is only the savings account with its current 0% interest rate and 1,4% annual inflation.

Investments in General

Before we focus on the details of Life Cycle Funds, we will briefly focus on the essence of investments in general.

Step 1
The first step is to carefully find out what your Personal Risk Level amounts to. Feel free to use our form as enclosed on our site in which we determine your profile by asking many questions. It is advisable to never act beyond your Personal Risk Profile.

Step 2
Then you determine your Investment Horizon.

Step 3
The outcome of the previous steps provides automatically which kind of Investment Categories fit within your Profile and Investment Horizon.

In general we can differentiate 6 kind of categories:

1] Derivatives

- Extremely high risk which only aims at change in value and not to buy a certain object itself.
- For example Options/Warrants/Futures.
- Thus only for those with a Very Offensive risk profile and a high level of knowledge.

2] Equity/Stock

- High risk even though the exact amount of risk can be different due to the kind of sector and global location.
- Equity requires in general an investment horizon of at least **7 years**.
- For those with a (very) offensive risk profile, a slightly shorter period might be acceptable.

3] Real Estate

- Depending on the type of Real Estate, similar or slightly less risk than Equity.
- Thus requires an investment horizon of in general at least **5-7 year.**
- For those with a (very) offensive risk profile, a slightly shorter period might be acceptable.

4] High Yield Bonds

- As these kind of Bonds go for the higher return on investment and risk, they require in general an investment horizon of at least **5 years**.
- For those with a (very) offensive risk profile, a shorter period might be acceptable.

5] Solid Bonds

- As these kind of Bonds aim for a regular return on investment and risk, they require in general an investment horizon of at least **3 years**.
- For those with a (very) offensive risk profile, a shorter period might be acceptable.

6] Savings

- No real investment risk as long as not at a fixed term.

Step 4
Finally you have to decide:
- Do you prefer investments in Individual Objects or in Funds?
- Do you prefer to Selfinvest or use of a Broker?
- If you use Funds, do you prefer Active Funds that try to outperform the index, or Trackers that only follow the index but at lowest costs?

Step 5
- We advise to invest in Funds as the costs, risk spread and liquidity of the investment is often much better than in case of Individual Objects.
- We advise to Selfinvest as there are fine providers who couple low rates with high level and transparent information contribution.
- We are critical towards Active Funds and often wonder if the additional costs outweigh the 'extra' return on investment.
- In case investments are not pension related, we do not really advise to use mix funds as each investment category can have a different investment horizon.

As of now we will only focus on Life Cycle Funds.

Type of Life Cycle Funds

A] Pension/Investment Risk Profile
We often see that a client has a risk profile regarding Pensions which differs from the Investment related risk profile.

Which can be quite understandable.

One might feel for example that as Pensions are the bases and thus there might be more the need to go for safe. While regarding Investments there might be a quite different investment horizon and more flexibility and due to a possibly more complementary function a (slightly) more offensive profile.

Therefore we advise you to look into both risk profiles. They do not have to be different. But if they are, it is advisable to address this issue as Life Cycle Funds can be used within a Pension Plan but also outside of them in Private investments.

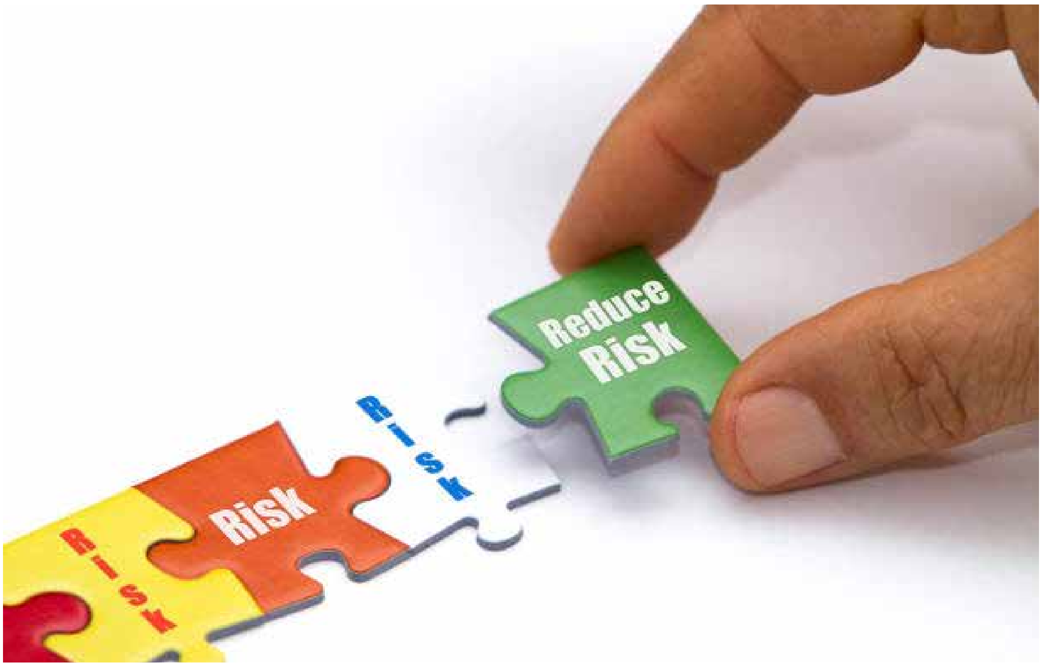
B] Risk Profile Related?

The central focus of Life Cycle Funds is to automatically reduce risk as the owner ages. **But *what* risk?**

As each person can have a different risk profile it is obvious that it makes a big difference if a Life Cycle Fund offers the choice between several risk profiles as this increases the tailor-made outcome.

In case such a choice is not available, you would assume that the fund will use an Average or Neutral risk profile. If that happens to also be your risk profile, than such a fund might be considered.

In case you have a risk profile that differs substantially and for example is Very Defensive or Very Offensive, then we advise you to question if that fund is most optimal for you.



C] Type of Mix Fund

Of course it is highly relevant to know what kind of Investment Categories Life Cycle Funds offer as they might be within or beyond your risk profile. Please combine this with the investment horizon aspects.

D] Active or Passive Funds

The difference between Active/Vision Funds versus Passive/Index Tracker (ETF) Funds regarding Sector and Location is often not so much the return on investment but the height of the costs.

As Life Cycle Funds are often used for quite a long period, a substantial annual difference in costs can have a huge impact in the long run.

Risk Reduction with Age

A] Standard Risk Reduction

One of the most relevant aspects of Life Cycle Funds is if they indeed reduce in the most optimal manner risk as age increases.

A standard example is the following fund:

First Phase: 2017-2037

A fixed spread of:

- Equity 90%
- Bonds 10%

Second Phase: 2037-2062

Increasingly a shift towards lower risk and at the end:

- Equity 50%
- Bonds 40%
- Cash 10%

Third Phase: 2062-2069

Increasingly a shift towards lower risk and at the end:

- Equity 30%
- Bonds 50%
- Cash 20%

B] Difference in Risk Reduction

This is best explained with an example. While comparing Life Cycle Funds risk reduction, we have seen that regarding a neutral risk profile, funds had the following different implementation:

	Start Risk Reduction	**Equity Age 60**	**Equity Age 65**
Fund A	Age 50	23%	5%
Fund B	Age 53	33%	12%
Fund C	Age 55	50%	35%

C] Conclusion

The fact that a Life Cycle Fund promises to provide optimal risk reduction fitting to your risk profile, does not automatically result in the best implementation.

Sometimes we see funds that according to our client protective stance, keep the risk level too high for too long and too near retirement age.

Costs of Life Cycle Funds

A] Regular Costs

- Costs related to opening and having an account. (Often none.) : Paid directly by investor
- One time transaction costs: As of 0,15% : Paid directly by investor
- Annual management costs: As of 0,2% : Paid directly by investor
- Fund costs: processed into the capital of the fund : Not paid directly by investor

B] Not Regular Costs

We often see that insurance companies offer the possibility to reduce the risk of value decrease by a sudden drop of the market. This by using financial derivatives to thus create a minimum value.

We are highly critical towards these kind of additional clauses. Often they are just too expensive. If you need more safety, would it not be better to change your investment categories and thus even get a higher net return on investment at lower costs?

C] Deviant Cost Levels

The longer you are paying a too high cost level, the higher the negative impact thereof due to the substantial impact of compounded return on investments.

In order to prevent this, we advise you to be especially allert towards Active/Vision Funds and Broker related activities.

You would not be the first investor paying not the usual 0,3% - 0,5% annual direct costs but instead 2% - 2,5%.

Conclusion

Within a Pension Plan or within a Private Investment, it can be fine to use a Life Cycle Fund.

But only if the investment and risk reduction with age is perfect and combined with the lowest costs possible.

We advise you to consider them if you appreciate their approach, but remain highly critical.

Feel free to ask for our advice as we gladly provide extensive aftercare to our clients.

International experience and Network

We have more than 20 years of experience in international expat and collective pension consultancy. Thus we have an elaborate international network. If so desired, we can advise and act swiftly in international matters.

Contact

For further information please contact pension jurist/consultant Patrick Donders:

Tel: +31 (0)6 26014112
E-mail: info@expatpensionholland.nl
Site: www.expatpensionholland.nl

AFM license number 12043181

EPH
EXPAT PENSION HOLLAND