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Time to Check Your Asset Allocation

Your mix of stocks, bonds, and cash should reflect your goals, time horizon, risk tolerance, and personal circumstances.

While periods of volatility are inevitable, investors may overreact during these times and undermine their long-term investment programs. Rather than succumb to knee-jerk reactions, individuals should review their asset allocation strategy and try to maintain a long-term perspective.

"As long as your asset mix of stocks, bonds, and cash appropriately reflects your financial goals, time horizon, risk tolerance, and personal circumstances, sticking with your investment plan could prove rewarding over longer periods," says Judith Ward, CFP®, a senior financial planner with T. Rowe Price. "Drastically reducing equity exposure for fear of incurring further short-term losses could result in having less money to fund long-term goals."

Diversification

Portfolios also should be diversified within each asset class. So an equity portfolio might include exposure to large- and small-cap stocks, growth- and value-oriented investments, and international equities. A bond portfolio might include international, high yield, and investment-grade corporate bonds as well as government debt.

Broad diversification across sectors provides exposure to those that are leading without being derailed by those that are lagging. Of course, diversification cannot assure a profit or protect against loss in a declining market.

In bond markets, fixed income securities traditionally have provided relative stability to help offset periods of equity declines. It has been almost 50 years since both the S&P 500 and 10-year Treasury bonds posted negative returns in the same calendar year.

Bonds typically offer greater return potential than cash and more stability than stocks, which is important for investors with nearer-term financial goals. However, investors with longer time horizons (at least five to 10 years) should continue to emphasize equities because they have outperformed other financial assets and provided a better hedge against inflation over the long term. Those approaching retirement might consider gradually reducing their equity exposure.

Over the past 25 years through 2018, the U.S. stock market has suffered through two historic bear markets (a 49% decline in 2000–2002 and a 57% fall in 2007–2009), as well as several corrections (declines of at least 10%). Yet, the market recovered to

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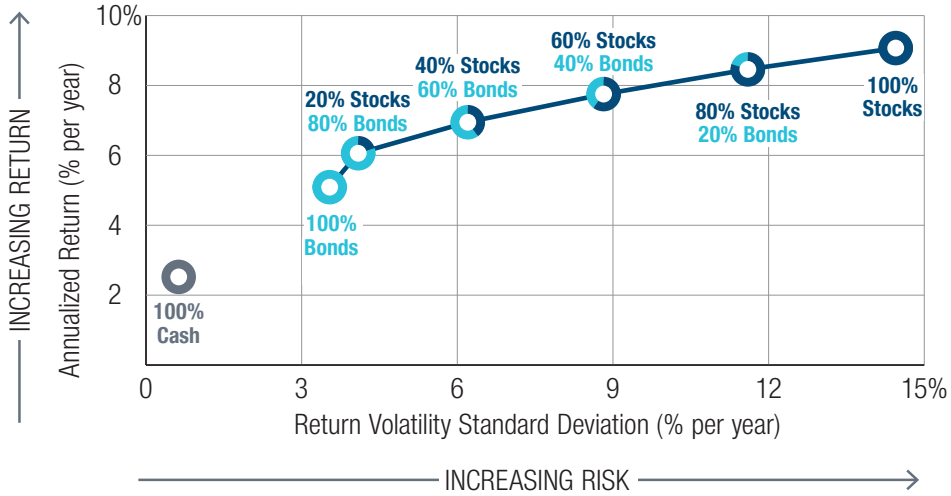
KEY POINTS

- Market volatility may be unsettling, but taking a long-term view can help.
- Keep in mind that U.S. stocks have provided positive returns over every rolling 20-year period since 1950.
- Broad portfolio diversification can help mitigate the risk of overexposure to any one area of the market.

Risks Versus Rewards of Asset Allocation

Greater risks and returns have gone hand in hand.



These hypothetical portfolios combine stocks and bonds to represent a range of potential risk/reward profiles. For each allocation model, historical data are shown to represent how the portfolios would have fared in the past. Figures include changes in principal value and reinvested dividends and assume the portfolios are rebalanced monthly. It is not possible to invest directly in an index. Chart is shown for illustrative purposes only and does not represent the performance of any specific security or T. Rowe Price product. Sources: Analysis provided by T. Rowe Price using Zephyr StyleADVISOR. Returns used in the analysis supplied by Morningstar. Stocks, S&P 500 Index; bonds, Bloomberg Barclays U.S. Aggregate Bond Index; cash, FTSE 3 Month US T-Bill Index. For the 25-year period ended 12/31/18. Bloomberg Index Services Limited. See Important Information.

reach new highs, showing an annualized return of 9.07% for the 25-year period ended December 31, 2018, compared with 5.09% for the Bloomberg Barclays U.S. Aggregate Bond Index. (See "Risks Versus Rewards of Asset Allocation.")

Stock returns can vary widely from year to year, and past performance cannot guarantee future results, but U.S. stocks (as measured by the S&P 500 Index) have provided positive returns over every rolling 20-year period since 1950 through 2018. During the 63 rolling 30-year periods since 1926, the market's worst performance was an annualized return of 8.5%.

Guidelines

During periods of market turbulence, Ward reminds investors that "what's happening in the headlines may not be what's happening in your accounts. Stick to fundamentals and focus on what you can control."

- Make sure your asset allocation is properly diversified and appropriate for your financial goals.
- Keep contributing to your retirement and college savings accounts. Investors with longer time horizons, in particular, can take advantage of investing during down markets.
- Rebalance on a regular basis to maintain your target portfolio diversification.
- Don't panic or try to time the markets.

"Regardless of the environment, investors should aim for a diversified portfolio that could provide reasonable returns over time," Ward says. "Looking beyond the short-term swings and adhering to your strategy may be the best bet to achieving your financial goals."

T. Rowe Price Asset Allocation Funds

You may choose to build your own portfolio of investments suited to meet your financial goals, or you may want to explore asset allocation funds, which offer a diverse portfolio through one fund. Depending on the goal for your assets, there are T. Rowe Price asset allocation funds to meet your needs. To learn more, visit **troweprice.com/assetallocation** or call **1-888-834-6586**.

Call 1-800-225-5132 to request a prospectus or summary prospectus; each includes investment objectives, risks, fees, expenses, and other information you should read and consider carefully before investing.

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