STRATEGIES & IDEAS
FOR THE CHARLES
SCHWAB COMMUNITY
FALL 2020

OnInvesting

Fly Right

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3 Buy and sell the smart way
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This year has eclipsed even the Great Recession in terms of the personal and financial hardship so many families have had to endure. All of us have been impacted by COVID-19 in one way or another.

In these uncertain times, we at Schwab are here to support you in any way we can. That’s why we’ve been rolling out resources to help make sense of the current environment and keep your finances on track:

- If you’re looking for market commentary, schwab.com/insights now offers a curated selection of timely analyses from Schwab experts as well as time-honored investing strategies for when markets turn volatile.
- If you have questions about your account or how to use various Schwab services, our new schwab.com/FAQs provides quick answers.
- And, of course, you can reach us 24/7 at 800-435-4000 with any questions or concerns.

At the same time, we’ve taken a number of measures to safeguard the health and well-being of our employees so they can stay safe and care for their families while also continuing to serve you.

Although the current crisis is unprecedented, this is not our first downturn, nor is it likely to be our last. But that doesn’t make us any less optimistic about the future. We still believe in the power of investing—and look forward to helping you achieve your goals, come what may.

Sincerely,

Walt Bettinger
President & CEO
Schwab offers hundreds of ways to make an impact through socially responsible investing.

Socially responsible investing (SRI) helps you choose investments based on environmental, social, or ethical factors. Schwab’s research tools make it easy to choose from over 500 SRI mutual funds and over 80 SRI ETFs.

Plus, if you are looking for more personal guidance, you have the option to work with a Schwab Financial Consultant who can help you make the most of SRI at Schwab.

Learn more at schwab.com/SRI.

Investors should consider carefully information contained in the prospectus or, if available, the summary prospectus, including investment objectives, risks, charges, and expenses. Please read it carefully before investing.

Investing involves risk, including loss of principal.

Please note that there are certain requirements for working with a dedicated Financial Consultant.

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The Law of Averages

After months of fast drops and sudden rises in the market this year, investors may have all but forgotten 2019’s record runup of nearly 30%. But recency bias—or the tendency to believe something is more likely to happen again because it happened recently—highlights the need to look beyond the present when it comes to your long-term investments. “Those deep valleys don’t look quite so scary if you’re able to zoom out from the day-to-day and see the big picture,” says Mark Riepe, head of the Schwab Center for Financial Research.

The fact is, the S&P 500 returned an average of about 10.2% annually from its inception in 1926 through
2019 (see “The bigger picture,” below). In other words, even the market’s darkest days—including three Black Mondays (10/28/1929, 10/19/1987, and 08/24/2015) and numerous other market corrections—couldn’t knock the index off its long-term march upward.

If you have a hard time stomaching volatility, Mark’s advice is to limit how often you check your long-term accounts. “You shouldn’t focus on that money every single day,” Mark says. “At best, you’ll drive yourself crazy. At worst, you’ll be tempted to sell when markets turn against you.”

Of course, you shouldn’t completely ignore your investments, either. “Review your statements and adjust your holdings as necessary in order to maintain your target asset allocation—assuming your financial situation hasn’t fundamentally changed,” Mark says. “If it has, revisit your financial plan.”

As for external events, remember that, good or bad, this too shall pass. “Just as you shouldn’t make plans based on the good times lasting forever,” Mark says, “neither should you make plans assuming the bad times will last forever—because they won’t.”

The bigger picture
Despite nearly a century of extreme peaks and valleys, the S&P 500 has averaged an annual return of 10.2% since its inception.

Source: Schwab Center for Financial Research. Data from 1926 through 2019. Note: Annual returns from 1926 through 1970 are represented by the Ibbotson U.S. Large Stock Index, which comprised the same components as the S&P 500 and its predecessor indexes.

See page 38 for important information. Please read the Schwab Intelligent Portfolios Solutions™ disclosure brochures for important information, pricing, and disclosures related to the Schwab Intelligent Portfolios and Schwab Intelligent Portfolios Premium programs. Schwab Intelligent Portfolios® and Schwab Intelligent Portfolios Premium™ are made available through Charles Schwab & Co., Inc. (“Schwab”), a dually registered investment advisor and broker dealer. Portfolio management services are provided by Charles Schwab Investment Advisory, Inc. (“CSIA”). Schwab and CSIA are subsidiaries of The Charles Schwab Corporation. Past performance is no guarantee of future results and the opinions presented cannot be viewed as an indicator of future performance. Investing involves risk, including loss of principal. Indexes are unmanaged, do not incur management fees, costs, and expenses, and cannot be invested in directly. For more information on indexes please see schwab.com/indexdefinitions. (0820-064K)
Tax Withholding in Retirement

How to help ensure you prepay enough taxes once you’re no longer working.

During your working years, you typically have one primary source of income: your paycheck. “In retirement, however, your income will likely be drawn from multiple sources—and the tax withholding rules for each may vary,” says Hayden Adams, CPA, CFP®, and director of tax planning at the Schwab Center for Financial Research.

Here’s how federal tax withholding generally works for some common sources of retirement income (state withholding may also apply):

- **Traditional, SEP, and SIMPLE IRAs**: Unless you specify otherwise, your plan’s custodian will withhold 10% on taxable distributions. Generally speaking, you can change or eliminate your withholding at any time by reaching out to your individual retirement account (IRA) custodian.

- **401(k), 403(b), and other qualified workplace retirement plans**: Plan providers typically withhold 20% on taxable distributions—unless the withdrawal is made to satisfy the annual required minimum distributions (RMDs) mandated by the IRS, which conform to IRA withholding rules.¹

- **Annuities and pensions**: Taxable periodic (e.g., weekly or monthly) payments from annuities and pensions are treated as wages using the IRS withholding tables in Publication 15 (see irs.gov/pub/irs-pdf/p15.pdf). You can set up or change your withholding by submitting Form W-4P to the payer.

- **Social Security**: Withholding isn’t required on Social Security payments, but a portion of your benefits may be taxable, depending on your income. Visit ssa.gov/planners/taxes.html to see how benefits are taxed. You can set up or change your withholding by submitting Form W-4V to the Social Security Administration.

- **Taxable bank or brokerage accounts**: In most instances, taxes are not withheld from capital gains, distributions, or other income generated from such accounts.² However, you may want to withhold more elsewhere or pay quarterly estimated taxes to help cover any tax liabilities produced by these assets.

If you’re unsure how much you should have withheld each year, you can use the IRS’ Tax Withholding Estimator (see irs.gov/individuals/tax-withholding-estimator) to calculate your overall tax obligation.

“That said, your estimated tax obligation is just that—an estimate—and will not account for any fluctuations in income throughout the year,” Hayden says. As a result, it’s wise to work with a tax professional. He or she may even recommend you make quarterly estimated tax payments in addition to the amounts already being withheld. “That way, you won’t end up underpaying the IRS throughout the year, which could result in penalties,” Hayden says.

¹Under the Coronavirus Aid, Relief, and Economic Security Act, RMDs have been waived for 2020. ²Certain taxpayers may be subject to backup withholding, which requires a payer to withhold tax from payments not otherwise subject to withholding. Learn more at irs.gov/taxtopics/tc307.

Learn how Schwab can help you generate income and make tax-smart withdrawals in retirement at schwab.com/retirementincome.
SRI and Your 401(k)

What to know before adding socially responsible investments to your retirement portfolio.

Only about 3% of 401(k) plans currently offer SRI funds— which use environmental, social, and governance (ESG) criteria to guide their investment decisions—but that figure may rise as investors push for funds that both align with their values and deliver competitive returns. Indeed, one survey found that 56% of plan participants prefer investing in socially responsible companies.2

“If investing with your values is important to you, SRI funds are a great way to go—provided they fit your goals,” says Michael Iachini, vice president and head of manager research at Charles Schwab Investment Advisory. “For example, retirement plans that offer SRI funds typically have only one option, and that option may or may not be the best fund for you.”

Growing good

In 2018, $11.6 trillion in assets were managed using ESG criteria in the U.S. alone—a 43% increase over 2016.

<table>
<thead>
<tr>
<th>Year</th>
<th>Assets under management</th>
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<tr>
<td>2016</td>
<td>$8.1 trillion</td>
</tr>
<tr>
<td>2018</td>
<td>$11.6 trillion</td>
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Here are four questions to consider when selecting SRI funds for your retirement portfolio.

1. What’s its focus? Some funds broadly integrate ESG criteria into their investing practices or focus on companies that aim to solve specific environmental or social issues, whereas others exclude certain kinds of companies—such as those that sell tobacco products.

2. Does it have a solid track record? “Generally speaking, you want to see a track record of at least three years to ensure the fund’s strategy is sound and not just a flash in the pan,” Michael says.

3. Is it diversified? Because SRI funds tend to focus on a narrower slice of the market, they may offer less diversification than, say, a broad-based index mutual fund or exchange-traded fund (ETF). For example, the VanEck Vectors Environmental Services ETF—which invests at least 80% of its assets in the stocks of companies involved in the environmental services industry—allocates a whopping 41.67% to its top five holdings.3 “At such high concentrations, a single stock could have undue influence on the performance of your portfolio,” Michael cautions. “If that concerns you, look for funds with lower allocations to any one company.”

4. What’s its annual fee? Every dollar you pay in fees is one you can’t invest for future growth—and that’s doubly important when it comes to your retirement savings. “Some SRI funds charge astronomical fees while others are more on par with low-cost index funds,” Michael says. “Be sure you know what you’re paying before you invest.”

If your workplace retirement plan offers limited SRI choices—or none at all—consider investing through an individual retirement account, which typically provides access to the same investment options as a traditional brokerage account.

To research SRI mutual funds for your portfolio, log in to schwab.com/fundscreener and select Socially Conscious under the Basic Criteria dropdown. To research SRI ETFs, log in to schwab.com/ETFscreener and select Socially Conscious under the Portfolio dropdown.


See page 38 for important information.

◆ Investors should consider carefully information contained in the prospectus, or if available, the summary prospectus, including investment objectives, risks, charges, and expenses. You can obtain a prospectus by calling Schwab at 800-435-4000. Please read it carefully before investing.◆ The information provided here is for general informational purposes only and should not be considered an individualized recommendation or personalized investment advice. The investment strategies mentioned here may not be suitable for everyone. Each investor needs to review an investment strategy for his or her own particular situation before making any investment decision.◆ Investing involves risk, including loss of principal.◆ Socially screened funds exclude certain investments and therefore may not be able to take advantage of the same opportunities or market trends as funds that do not use social screens.(0520-0PUR)
Shopping for Bonds

You comparison shop for most everything else—so why not for bonds?

Would you ever buy a car—or even a new pair of shoes—without looking for the best deal? Probably not. So why don’t more investors comparison shop for bonds?

“Many investors simply don’t realize different firms charge different prices for the exact same bond,” says Kathy Jones, senior vice president and chief fixed income strategist at the Schwab Center for Financial Research.

The problem stems from the fact that bonds don’t trade on centralized markets like stocks, which makes their true cost difficult, if not impossible, to ascertain. Instead, most are purchased “over the counter” through a brokerage firm that buys a bond on your behalf—and tacks on a fee, or markup, that can range from a fraction of a percent to several percentage points, depending on factors such as bond liquidity and the firm executing the trade.

“All too many brokerages not only charge far too much but also conceal such costs from investors,” Kathy says. So, before you buy your next bond, ask your broker these important questions—and be sure you’re satisfied with the answers.

1. **What’s the market price?** This will reflect the actual price it costs your broker to buy a bond from another dealer (which may include fees paid to the dealer).

2. **What’s the markup?** Markups refer to the difference between the market price of a bond and the price a broker-dealer charges to sell it. Markups are generally wrapped into the price—and may or may not be disclosed. (For more on Schwab’s fixed income pricing, visit schwab.com/fixed-income-pricing.)

3. **Are there additional fees?** In addition to markups, brokers may charge miscellaneous fees to cover administrative services, clearing fees, overhead, etc.—which, as with the markup, they may or may not be required to disclose.

4. **What’s the accrued interest?** When you buy a bond between coupon payment dates, you’ll owe the seller any accrued interest since the last payment date. This cost has nothing to do with your broker but does factor into the total cost.

5. **What’s the overall cost?** This will include all of the above: the market price, plus any markup, additional fees, and accrued interest.

“Be wary of firms that fail to give you direct answers about their fees,” Kathy says. “They’re probably being opaque for a reason.”

Indeed, even seemingly small differences in markups can mean giving up hundreds, if not thousands, of dollars in total returns over time. And with prices and yields fluctuating to the degree they have recently, it pays to shop around.

See page 38 for important information. ♦ Fixed income securities are subject to increased loss of principal during periods of rising interest rates. Fixed income investments are subject to various other risks, including changes in credit quality, market valuations, liquidity, prepayments, early redemption, corporate events, tax ramifications, and other factors. Lower-rated securities are subject to greater credit risk, default risk, and liquidity risk. ♦ In the bond market, there is no centralized exchange or quotation service for most fixed income securities. Prices in the secondary market generally reflect activity by market participants or dealers linked to various trading systems. Bonds available through Schwab may be available through other dealers at superior or inferior prices compared to those available at Schwab. All prices are subject to change without prior notice.

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<td>$100,000+</td>
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</table>
Dear Reader,

I’m glad you raised this question because it touches on a widely misunderstood component of the Social Security system: family benefits. Unlike survivor benefits—which are paid to eligible beneficiaries upon your passing—family benefits are paid to eligible family members during your lifetime. Even

Social Security for Families

The benefit begins with you—but it doesn’t end there.

Q

Dear Carrie,

I’m 62, my wife is 53, and we have 14-year-old twins. My income has dropped precipitously, and I’m looking for a way to fill in the gap. Could applying now for Social Security benefits make sense?

A

Dear Reader,

I’m glad you raised this question because it touches on a widely misunderstood component of the Social Security system: family benefits. Unlike survivor benefits—which are paid to eligible beneficiaries upon your passing—family benefits are paid to eligible family members during your lifetime. Even
better, family benefits don’t eat into your benefit; on the contrary, they can significantly boost your family’s total payout.

While it generally makes the most sense to delay claiming Social Security benefits if you can afford to wait and are in good health, family benefits can make claiming early an attractive option. That said, the rules regarding family benefits are complex—but understanding the basics can help you and your family capture all available benefits.

Who’s eligible—and when

First things first: You have to file for your own benefit before your family members can collect against it. From there, your family members can collect against your Primary Insurance Amount (PIA)—or what your Social Security benefit would be at full retirement age (between 66 and 67 for today’s retirees)—provided they fall into one of three categories:

- **Spouses age 62 or older**, who can collect from 52.5% to 50% of your PIA based on when they file (see “Patience pays,” above right).

- **Spouses of any age**, who can collect 50% of your PIA, provided you’ve been married at least one year and have a child under the age of 16 (or a child of any age in your care who was disabled before age 22).

- **Children**—including adopted, biological, and stepchildren, as well as grandchildren for whom you’re the legal guardian—who can collect 50% of either parent’s PIA, provided they’re unmarried and:
  - Younger than 18.
  - Younger than 19 and a full-time K–12 student.
  - Any age, if disabled before age 22.

So, assuming you filed for Social Security at age 62, your spouse at age 55 would be eligible to receive 50% of your PIA until your twins turn 16. At that point, her benefit would stop.

If your wife is eligible for her own Social Security benefit and waits until her full retirement age, she would receive either 100% of her benefit or 50% of yours—whichever is larger. If she claims either her or your Social Security benefit before her full retirement age, her benefit would be reduced accordingly (again, see “Patience pays,” above).

Maximum family benefit

While the numbers may look good so far, there’s a limit on the total benefit your family can collect. This family maximum benefit is between 150% and 188% of the primary earner’s PIA (the Social Security Administration uses a complex formula to determine the final amount).

If the sum of your benefit and your family’s benefits exceeds this amount, their payments—though not yours—would be uniformly reduced to meet the cap. For example, if the benefit for your wife and your twins exceeds the maximum by $1,200, each of their monthly payments would be cut by $400, while yours would remain the same.

Next steps

As you can see, the family benefit rules within Social Security are complex but worth understanding. Your Social Security statement, available at ssa.gov/myaccount/statement.html, can tell you how much you and your family would receive, or you can call the Social Security Administration at 800-772-1213. You can also call 800-355-2162 to talk to a Schwab financial consultant about how Social Security fits into your financial plan.

What about ex-spouses?

An ex-spouse who was married to you for at least 10 years, is 62 or older, and is currently unmarried is also eligible to collect up to 50% of what your Social Security benefit would be at full retirement age. Rest assured, however, that your ex-spouse’s payouts have absolutely no impact on your—or your family’s—benefits.

Carrie Schwab-Pomerantz (@carrieschwab), CFP®, is president of Charles Schwab Foundation and senior vice president of Schwab Community Services at Charles Schwab & Co., Inc.

See page 38 for important information.

The information provided here is for general informational purposes only and should not be considered an individualized recommendation or personalized investment advice. The investment strategies mentioned here may not be suitable for everyone. Each investor needs to review an investment strategy for his or her own particular situation before making any investment decision.

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You’ll Be Back
What investors can do to rebuild their finances.
By Rob Williams

The market sell-off triggered by COVID-19 may have shaken your confidence and taken at least a near-term toll on your finances. But times of uncertainty are also an opportunity to reevaluate your priorities.

In fact, research has shown that specific events—the start of a new year, for example, or the conclusion of a crisis—can be a powerful catalyst for change.\(^1\)

If you’re ready to make a fresh start with your finances, here are five steps to get the ball rolling.

**Step 1: Take stock**
You can’t make meaningful financial change unless you know where you stand:

- **Calculate your net worth**: Make a list of all your assets and subtract your debts (or use a wealth-tracking app). This is the benchmark against which you can measure future progress. And don’t panic if your net worth declines during tough market periods—what’s important is the long-term trend.
- **See where your money is going**: After calculating your after-tax income, list your current expenses and decide which are essential (such as housing and retirement savings) and which are nonessential (such as subscription services and ordering takeout). If you have a big expense coming up—like college tuition or a roof repair—sock away that money in a separate savings account so you’re less likely to tap it for other expenses.

**Step 2: Shore up your savings**
Once you have a big-picture view of your finances, you should then make sure your savings are on track:

- **Prioritize retirement**: A rule of thumb is to save 10% to 15% of your pretax income, including any matching contributions from your employer, starting in your 20s. If you started saving later than that, add 10% for every decade you delayed. And if your current budget won’t support your target savings rate, free up some cash by eliminating nonessential expenses.
- **Account for emergencies**: Establish an emergency fund with three to six months’ worth of essential living expenses in a highly liquid checking, savings, or money market account.
to help cover unexpected expenses without having to sell more-volatile investments.

Step 3: Manage your debt
For many people, some level of debt is a practical necessity—especially when purchasing pricey assets such as a car or home. Here’s how to manage it effectively:

- **Eliminate high-cost debt:** The cost of credit card debt adds up quickly if you carry a balance, so focus on bringing that down to zero—and keeping it that way.
- **Consolidate balances:** If you own your home, consider establishing a home equity line of credit (HELOC) to consolidate other types of debt at a potentially lower interest rate. A HELOC can also serve as backup emergency savings.
- **Watch your total debt load:** Don’t confuse what you can borrow with what you should borrow. Try to follow the 28/36 rule: Ideally, no more than 28% of your pretax income should go toward your mortgage, and no more than 36% of your pretax income should go toward all debt.

Step 4: Optimize your portfolio
Create an investment plan that will help you stay disciplined in all kinds of markets:

- **Focus on your overall investment mix:** Have a targeted asset allocation that’s in sync with your long-term goals, risk tolerance, and time frame. The longer your time horizon, the more opportunity you’ll have to ride out a down market. (For more, see “Reassessing Risk,” page 22.)
- **Diversify across and within asset classes:** Diversification helps reduce volatility risk by spreading your wealth across myriad assets. Mutual funds and exchange-traded funds (ETFs) offer a diversified basket of securities in just about any asset class.
- **Consider taxes:** Place relatively tax-efficient investments (such as ETFs, index funds, and municipal bonds) in your taxable brokerage accounts, and relatively tax-inefficient investments (such as actively managed mutual funds and real estate investment trusts, or REITs) in your tax-advantaged retirement accounts.
- **Review and rebalance as needed:** Market ups and downs can have a significant impact on the balance of stocks, bonds, and other assets in your portfolio. Check your holdings at least quarterly and rebalance as needed to ensure you’re still investing according to your goals and timeline.

Step 5: Protect your assets, dependents, and estate
Your estate plan is a way for you to support the people and things you care about most. Enlist a lawyer or estate-planning attorney to help you:

- **Update your will and beneficiaries:** A will is crucial to providing for your dependents’ support and care. And reviewing beneficiaries ensures that the proceeds from annuities, life insurance policies, retirement accounts, and other

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Dream Date
How to choose the right target-date fund for you.
By Michael Iachini

Target-date funds have become a staple of many 401(k) and individual retirement accounts (IRAs). According to BrightScope, 21% of all assets in 401(k) plans were in target-date funds in 2016—up from 3% just a decade earlier. More broadly, total assets under management in target-date funds increased from roughly $7 billion in 2000 to nearly $1.4 trillion in 2018.1

The appeal is understandable. Target-date, or age-based, funds offer an all-in-one mix of stocks, bonds, and cash that grows steadily more conservative over time, with some funds reaching their most conservative mix at their target date. More broadly, total assets under management in target-date funds increased from

Look under the hood
Despite their relative simplicity, target-date funds can vary widely in their asset allocation, management approach, and more. When comparing funds, pay particular attention to:

- Fees: All target-date funds generally involve some degree of human judgment in the selection of investments, but some are more actively managed than others. Those made up primarily of index funds, for example, may offer net expense ratios as low as fractions of a percentage point. Actively managed funds, which have professionals making more judgment calls about which assets to include, can have net expense ratios above 2%. Data from Morningstar shows that lower-fee funds have proven more popular in recent years. However, actively managed funds may be more responsive to market fluctuations.2

- Glide path: This is the term for how a fund’s asset allocations change over time. For example, some target-date funds move heavily into bonds and cash before the fund’s target date, while others continue to hold sizable allocations well after that date (see “Is ‘to’ or ‘through’ right for you?” above right). Different funds may also have different allocation models. For example, the stock allocations among the half-dozen largest funds with a target date in 2020 range from 33% to 55%, according to Morningstar.3

- Holdings: While some funds stick to a basic mix of stocks, bonds, and cash, others incorporate investments like commodities and real estate investment trusts (REITs). In general, broader is better. That’s because the more asset types you have, the less likely they’ll all move in the same direction at the same time, which can help mitigate your losses during a downturn. That said, Schwab recommends that even the most aggressive investor’s portfolio contain a total of no more than 10% commodities REITs, and other so-called real assets.

Is “to” or “through” right for you?
All target-date funds grow more conservative over time. However, “to” funds reach their most conservative allocation at their target date, while “through” funds continue to adjust their allocations well beyond that date.

The examples are hypothetical and for illustrative purposes only.

- To review a fund’s glide path, log in to schwab.com/research-tools, input its ticker symbol, and click the Fund Facts & Fees tab.

- To review a fund’s glide path, log in to schwab.com/research-tools/download, input its ticker symbol, and click the Prospectus link.

- To review a fund’s holdings, log in to schwab.com/research-tools, input its ticker symbol, and click the Portfolio and Holdings tab.

“Core and explore”
Alternatively, if you prefer to keep a hand in overseeing your investments, consider a so-called core-and-explore approach, in which most of your retirement portfolio remains in a target-date fund, with a portion left over for other investments you can manage yourself. If you decide to pursue this approach, take a holistic view of all your investments to ensure they’re complementary and collectively in line with your target asset allocation.

- For example, target-date funds offer a simple, one-stop solution for many retirees. Simple, however, doesn’t always mean easy. You’ll still need to do your homework to find the right fund for you—and to stay on top of your overall progress toward your goals.4


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See how Schwab Target Date Funds work hard for your retirement at schwab.com/targetfunds.

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want to sell your winners prematurely, it might make more sense to generate the necessary income by selling your losers—which may allow you to offset up to $3,000 a year in ordinary income in the process.

* The investment no longer fits your strategy

Regardless of whether an investment has lost or gained value, you should never keep it if it no longer fits your strategy (see “Investing Mindfully,” page 26). That said, it can be hard to let go of an investment that’s lost value thanks to the break-even fallacy, or our instinct to wait to sell an investment until it rebounds to our purchase price.

But holding on to the investment in hopes of a turnaround could further erode your returns, whereas taking the loss could allow you to get your portfolio back on track more quickly—and potentially offset capital gains and/or ordinary income.

Using a tax loss to get a tax break

A hypothetical investor who realized $10,000 in short-term capital gains and $15,000 in capital losses could use tax-loss harvesting to cut down her tax bill—this year and in future years.

**Taxes that could have been owed without tax-loss harvesting**

| Source: Schwab Center for Financial Research. Assumes a 32% combined federal/state marginal income tax bracket, with short-term capital gains taxed at ordinary income tax rates. The example is hypothetical and provided for illustrative purposes only. It is not intended to represent a specific investment product and the example does not reflect the effects of fees. |

<table>
<thead>
<tr>
<th>Capital gains</th>
<th>Ordinary income</th>
</tr>
</thead>
<tbody>
<tr>
<td>$3,200</td>
<td>$960</td>
</tr>
</tbody>
</table>

$3,200 ($10,000 x 32%) + $960 ($3,000 x 32%) = $4,160

**Other considerations**

If you’ve decided to sell some losers, it’s important to understand a few of the applicable tax rules before you take action:

**Short- vs. long-term capital gains:** Short-term capital gains are taxed at ordinary federal income tax rates, which for many taxpayers are higher than the long-term capital gains rates of 0%, 15%, or 20%, depending on your income level.

Note that any losses must first be applied to gains of the same type (i.e., long- or short-term gains) before they can be applied to gains of a different type. For example, if you have short- and long-term gains, you must use any long-term losses to offset your long-term gains first; then you can use any remaining long-term losses to offset your short-term gains.

**Wash-sale rule:** If you plan to take a loss and reinvest the proceeds, be mindful of the wash-sale rule, which stipulates you can’t use the losses to offset gains if you purchase the same or a “substantially identical” investment within 30 days before or after the sale. Unfortunately, there’s no clear guidance on what constitutes a substantially identical investment. Stocks are fairly straightforward, but for exchange-traded funds and mutual funds, it’s best to err on the side of caution by selecting a fund that tracks a different benchmark or has a markedly different investment mix.

A financial planner or qualified tax advisor can help you make the most of any investment losses—without running afoul of the IRS. ■

Read more insights about tax-loss harvesting and other tax strategies at schwab.com/taxes.
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Is the recent episode of extreme volatility unprecedented?

Joe: “We’ve certainly seen bouts of heightened turbulence before, but nothing like this. If you were trading on traditional fundamentals, those were all but meaningless once the crash began. In fact, it forced fundamental traders to turn to nonfinancial data for information, focusing on things like science, sentiment, and the stimulus.”

What’s the big lesson traders should take away from this episode?

Kevin: “We went 11 years without any real tests or market shocks, which may have lulled some traders into a false sense of security. This is a chance to remind ourselves of complacency risk. It’s the nature of the game: You’re going to go through periods when you’re absolutely crushing it—but there’s always the chance you’re the one who’s going to get crushed.”

Joe: “You also need to determine what percentage of your portfolio you’ve really comfortably trading. I’ve always looked at it this way: I don’t want to enter a trade unless I’m willing to lose that money. That doesn’t mean I’d be happy about losing it, but if I can handle the loss both financially and mentally, it helps keep me focused on the trade itself, rather than fear or greed.”

Did anyone succeed during the recent downturn?

Lee: “There were several periods during which the market was up a few hundred points for a couple days, then down several hundred points, then up again. So, to a certain extent, the traders who found the most success were those comfortable trading momentum—that is, trading the short-term trend to capture gains quickly.”

What can traders do to manage risk moving forward?

Joe: “It doesn’t matter whether you’re trading stocks, futures, options, whatever—just go smaller. Correct position sizing becomes that much more important when the swings are bigger. I also believe in ‘going home flat’ when the market is choppy—that is, not having a position open overnight, because that’s when things can go sideways for you. Take as much of that risk off the table at the end of the day as you can.”

Lee: “If your old trading style was one in which you sold right at the top and bought right at the bottom, it means you’re prepared to act when the market settles down a bit.”

Joe: “Cash is, in fact, a position. And with market volatility unprecedented, that means you need to be prepared to act when the market settles down a bit. A trading plan is always necessary, but it’s even more so during a down period like we’ve had this year.”

Kevin: “A trading plan is always important, but it’s even more so during a down period like we’ve had this year. In addition to rightsizing your trades and establishing your exit points, you have to look objectively at your winners and losers. Dig into your results and find out where your profits and losses are coming from. If the profits aren’t there, that should encourage you to step back and reassess your plan.”

Does it ever make sense to just sit it out?

Lee: “Absolutely. For traders, it’s never a good idea to just stay in cash until the market settles down a bit.”

Kevin: “Cash is, in fact, a position. And it means you’re prepared to act when you do find an interesting opportunity in line with your risk tolerance. Under no circumstances do you need to be trading all the time.”

How do you regain confidence after something like this?

Joe: “No matter how strong a stomach you have, when you see your investments drop 30% in a matter of weeks, it’s tough to deal with. Nobody is that cold-blooded. Part of the challenge is determining your degree of fortitude ahead of time. Whether you’re a trader or a long-term investor, it’s all about knowing how much risk you’re truly comfortable with.” (For more, see “Reassessing Risk,” page 22.)

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Investing Mindfully
How to tune out the noise and make more purposeful investment decisions.
Despite every intention of making rational, reasoned decisions—especially when it comes to our finances—we sometimes allow emotions to get the better of us.

Worse, we have a tendency to rationalize away any resulting mistakes, which over time only compounds the initial error.

Noel Prize-winning psychologist Daniel Kahneman has done extensive research into how we can make more deliberate and logical decisions when our emotions are running high. His conclusion? Slow down. The more time you take, Kahneman’s research suggests, the less likely it is that emotion will cloud your decision-making.

In practical terms, that means taking a beat and really thinking through why you want to buy an investment. Does the asset support your goals or are you merely chasing a hot stock or market? The same holds true when you want to sell. Does the investment no longer fit your strategy—or is it driving your decision? Here’s how to know whether you’re selling or buying stocks, bonds, and funds for the right reasons.

**Stocks**

**If you’re willing to buy or sell at any price, that’s a tipoff you’re not thinking rationally,” says Kahneman.**

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**Bonds**

Because bonds are relatively stable, investors are less likely to dump them in a fit of panic selling. On the contrary, bond investors should be wary of panic buying. Consider reevaluating your next bond purchase if:

- You’re buying risky bonds in an effort to boost yields: With 10-year U.S. Treasury bonds yielding less than 1%, it’s hard to ignore high-yield bonds paying 7% or more. But letting your desire for higher yields dictate your investment strategy is the exact type of emotional decision-making you want to avoid. “High-yield bonds have a much higher default risk than their investment-grade counterparts, so if you wouldn’t normally include them in your portfolio, I wouldn’t add them now,” says Collin Martin, director of fixed income at the Schwab Center for Financial Research. “Plus, we’re likely to see more defaults in the months ahead as the economy works to recover from COVID-19.”

- You’re watching deteriorating fundamentals, which often indicate trouble. “You should ditch a stock as soon as it fails to live up to your reasons for buying it in the first place,” says Steve. However, if the stock’s price is falling but its fundamentals remain strong, it could be a well-positioned for a rebound. “Don’t let fear trick you into parting ways with a worthy investment,” he adds.

- You’re reevaluating your overall portfolio. “You should be reevaluating your overall portfolio. You should be reevaluating your overall portfolio. You should be reevaluating your overall portfolio.”

**Funds**

**It can be tempting to get into or out of ETFs and mutual funds whenever there’s a big market swing,” says Steve.**

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Unless you’re an active trader, you should avoid basing your investment decisions on market trends.

Most investors know that trying to time the market is contrary to achieving their long-term goals, but knowing that to be true doesn’t necessarily keep you from making emotional decisions when markets are surging or slumping.

To help keep a level head, predict your buy and sell decisions on quantifiable factors, such as:

- **Fee:** When adding funds to your portfolio, generally favor those with lower operating expense ratios, as every dollar you pay in fees is one you can’t invest for future growth. That’s an easy rule to follow with index funds, whose fees tend to be relatively low, but it’s not so cut-and-dried where actively managed funds are concerned.

> “Pay a higher fee for an actively managed fund could make sense if you believe the fund will deliver superior returns,” says Michael Tachau, vice president and head of manager research at Charles Schwab Investment Advisory. “But don’t base such decisions on past performance. Your fund’s returns could be due to luck and might not persist.” The same holds true for these you already own. “If any of your mutual funds, which tend to be more volatile, seem similar on the surface could take very different approaches with their investments.

Likewise, it’s a good idea to check in on your current funds’ strategies periodically—especially your active funds. “Managers may adjust their strategies from time to time in an effort to boost returns or respond to the current environment,” Michael says. “If this happens with any of your holdings, make sure you’re comfortable with the direction in which the fund is heading.”

**Cool it**

When your emotions are running hot, they can steer you in the wrong direction—but slowing down and focusing on the facts can help ensure you’re making the right decisions at the right time and for the right reasons. That may sound obvious, but it’s harder than you might think—especially in the heat of the moment.

**Investment strategy:** Whether you’re looking for broad exposure to the market or access to a specific sector, always confirm that a fund’s investment strategy is in line with your expectations. Two funds that seem similar on the surface could take very different approaches with their investments.

**Fundscreener**

> **Fundscreener**

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**ETF screener**

> **ETF screener**

You can screen for ETFs by theme or by category.

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How much can you really handle?

The answer may surprise you.

Market shocks are an inevitable part of investing—but that doesn’t make them any easier to stomach. Whether you’re just starting out or have been saving for decades, watching your hard-earned gains evaporate overnight can cause you to question the entire enterprise.

“When the market is going up and up, it’s easy for investors to think they’re more comfortable with risk than they actually are,” says Mark Riepe, head of the Schwab Center for Financial Research. “But the 34% market decline between mid-February and mid-March1 may have forced people to confront their true risk tolerance.”

So, how do you go about reassessing your tolerance for risk, come what may? Ask yourself these three questions.

1. How much can I stand to lose emotionally?

Investing is an act of faith—to say nothing of willpower. The assets that offer the highest potential reward are often the riskiest, but if you can steel yourself against their occasional surges in volatility, you’re more likely to reach your long-term goals.

The question is, how much risk can you really handle? To help answer that question, consider the downsides and upsides of five hypothetical portfolios (see “More pain, more gain,” page 25).

Although portfolios with larger allocations to stocks delivered higher returns over time, they were also more volatile—which may not work for everyone. If you need the money in the next few years, for example, you
should choose a more stable investment mix. The same is true if you simply can’t bear to see your portfolio plummet in value. It’s perfectly reasonable to say, “I’m willing to accept lower returns in exchange for more stability,” Mark says. “But that means you may have to save more—or rack up your spending expectations—to compensate.” Indeed, reducing your exposure to stocks and other relatively high-risk, high-reward assets during your peak earning years comes with its own kind of risk: falling short of your goal. “Market turbulence feels risky because it’s something you have to face again and again,” Mark says. “But the more pernicious risk comes from undercutting your long-term returns, because there’s no coming back from that.”

To help manage your emotional response to market volatility, consider cutting back on how often you review the performance of your long-term accounts. In fact, research suggests that the less often people check their investments, the more risk they may be willing to take—and the better their returns are likely to be over time (see “Less is more,” right).

“You can’t wish your emotions away,” Mark says. “But you can take steps to keep them in check.” That said, there may be reasons to review your portfolio more frequently. “You should check in on your investments and your broader financial plan anytime your situation changes substantially.”

2. How much can I stand to lose financially?

While many people think about risk in terms of their ability to endure losses emotionally, there’s another component to risk that’s equally important: your capacity to recover financially.

“Time is a big factor here,” Mark says. “When you’ve got a decade or more until you need to tap your savings, short-term volatility isn’t a big risk. But if you’ll need the money in, say, five or fewer years, a more liquid account. “The COVID-19 outbreak demonstrated how quickly a portfolio can plummet in value. “It’s perfectly reasonable to relieve financial stress during a downturn,” Mark says. “But that means you may have to save more—or ratchet back your spending expectations that might otherwise get the best of you,” Mark says.

Sleep easier

In the end, figuring out how much risk you can really handle is an art as much as it is a science. “Sure, we can give you guidelines based on your age or time frame, but it ultimately comes down to how much you can stand to lose—both emotionally and financially,” Mark says. “Once you know that, you may also be able to help identify whether you’re acting with your head—or your heart. “An advisor can help curtail the emotional responses that might otherwise get the best of you,” Mark says.

Less is more

In one study, participants who received monthly feedback on the performance of their hypothetical portfolios had a higher risk tolerance than those who received monthly feedback.

| 20% | Conservative |
| 40% | Moderately conservative |
| 60% | Moderate |
| 80% | Moderately aggressive |
| 95% | Aggressive |

More pain, more gain

Consider five hypothetical $25,000 portfolios—from conservative (smallest allocation to stocks) to aggressive (largest allocation to stocks):

<table>
<thead>
<tr>
<th>Year</th>
<th>Conservative</th>
<th>Moderately conservative</th>
<th>Moderate</th>
<th>Moderately aggressive</th>
<th>Aggressive</th>
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</thead>
<tbody>
<tr>
<td>Worst</td>
<td>-4.6%</td>
<td>-12.6%</td>
<td>-20.9%</td>
<td>-29.5%</td>
<td>-36.0%</td>
</tr>
<tr>
<td>Best</td>
<td>22.8%</td>
<td>27.0%</td>
<td>30.9%</td>
<td>34.1%</td>
<td>36.7%</td>
</tr>
</tbody>
</table>

The greater the allocation to stocks, the greater the potential downside ...

After 40 years, the portfolios with greater stock allocations had significantly larger values than those with smaller allocations:

Table: Average annual returns

<table>
<thead>
<tr>
<th>Portfolio Type</th>
<th>Average Annual Return</th>
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</thead>
<tbody>
<tr>
<td>Conservative</td>
<td>7.5%</td>
</tr>
<tr>
<td>Moderately conservative</td>
<td>8.9%</td>
</tr>
<tr>
<td>Moderate</td>
<td>9.6%</td>
</tr>
<tr>
<td>Moderately aggressive</td>
<td>10.1%</td>
</tr>
<tr>
<td>Aggressive</td>
<td>10.4%</td>
</tr>
</tbody>
</table>

Need help reassessing your risk tolerance? Work one-on-one with a CERTIFIED FINANCIAL PLANNER™ professional when you enroll in Schwab Intelligent Portfolios Premium™. Learn more at schwab.com/portfolios premium.

Source: Schwab Center for Financial Research. Data from 01/01/1980 through 05/31/2020. The example is hypothetical and provided for illustrative purposes only. It is not intended to represent a specific investment product. Historical returns are weighted averages of the performances of the indexes used to represent each asset class, including the reinvestment of dividends and interest, and are rebalanced annually. The example does not reflect the effects of taxes. The indexes representing each asset class are: S&P 500® Index (large-cap stocks); Russell 2000® Index (small-cap stocks); MSCI EAFE® Index (international stocks); Bloomberg Barclays U.S. Aggregate Bond Index (fixed income); and FTSE 3-Month Treasury Bill (cash investments). Indexes are unmanaged, do not incur management fees or expenses, and cannot be invested in directly. Past performance is no guarantee of future results.
Get Cracking

How to convert your nest egg into a reliable monthly paycheck.

One of the biggest challenges facing new retirees is how to replace their regular paycheck with a steady stream of income from their savings and other sources. Social Security and pension plans—which provide a reliable monthly paycheck for life—certainly help, but they’re unlikely to cover most retirees’ ongoing expenses. Indeed, Social Security was designed to replace only about 40% of average annual earnings (the percentage is actually lower for those in upper-income brackets), and the median monthly benefit for private pension plans is just $819.

As a result, most retirees must figure out on their own how to cobble together guaranteed payouts, irregular income streams, and withdrawals from their hard-won savings to create a steady “paycheck” in retirement. “Generating predictable retirement income is like putting together a puzzle,” says Rob Williams, vice president of financial planning at the Schwab Center for Financial Research. “Because every retiree’s puzzle looks slightly different, there’s no one way to put it together.”

Here are five steps for creating your own retirement paycheck, whatever your individual circumstances.
Nail down expenses

One rule of thumb is to assume your future monthly expenses will be at least 75% to 80% of your current income once you reach retirement, since some big-ticket expenses—such as retirement contributions and commuting costs—will likely go away. That said, a ballpark estimate gets you only so far, so it’s best to create a budget where you can assign real numbers to your expenses.

Tools like the Monthly Budget Planner at schwab.com/budget can help you calculate your income needs.

Subtract guaranteed income

Once you know your monthly outflow, it’s time to figure out how much guaranteed income you can expect to receive. Social Security figures prominently here, and the timing of when you collect can have a big impact on your total benefit.

Collecting early—anytime from age 62 through to your full retirement age (between 66 and 67 for today’s retirees)—means taking a reduced benefit (between 66 and 67 for today’s retirees)—means taking a reduced benefit, which is always appealing, but they may also come with tax consequences that shouldn’t be ignored,” Rob says.

“It’s wise to consult a qualified financial planner or tax advisor about the potential benefits and drawbacks of such income sources as you map out your income plan.”

Estimate investment income

With interest rates near historic lows, income-generating investments aren’t as powerful as they once were. Even so, regular interest and dividend payments can play an important role in your retirement income.

How to build a bond ladder

Staggering your bonds’ maturity dates can create a steady stream of income from your portfolio.

To build a bond ladder:

1. Purchase a number of bonds with varying maturity dates so they come due at regular intervals—say, every 12 months. (For adequate diversification, Schwab recommends a ladder of at least 10 high-quality, noncallable bonds.)

2. To keep the ladder going, reinvest the principal from the maturing one-year bond in a new 10-year bond, and so on as each bond comes due.

The principal from maturing bonds provides extra cash flow in retirement, which is always appealing, but they may also come with tax consequences that shouldn’t be ignored,” Rob says.

“It’s wise to consult a qualified financial planner or tax advisor about the potential benefits and drawbacks of such income sources as you map out your income plan.”

Plan for change

As you move through retirement, you may find that your income sources change from year to year. If you stop working part time, for example, you may need to make up for that lost income by taking a larger withdrawal from your retirement portfolio.

When it’s time to tap your retirement investments for income, it can be challenging to figure out whether you can afford to withdraw without depleting your savings too quickly or generating a significant tax bill. That’s why Schwab created Schwab Intelligent Income™, which pairs the technology of Schwab Intelligent Portfolios® with a tax-smart withdrawal strategy that generates a predictable monthly paycheck from your investments.

Turn to your retirement portfolio

After accounting for all other income sources, you can estimate how much of the principal in your retirement accounts you’ll need to tap each month. But how will you know if that withdrawal rate is sustainable?

“Could you live on a smaller income for life?” Rob asks.

When it’s time to tap your retirement investments for income, it can be challenging to figure out whether you can afford to withdraw without depleting your savings too quickly or generating a significant tax bill. That’s why Schwab created Schwab Intelligent Income™, which pairs the technology of Schwab Intelligent Portfolios® with a tax-smart withdrawal strategy that generates a predictable monthly paycheck from your investments.

Robo-advisors to the rescue

A robo-advisor can provide a low-cost, efficient way to help meet your income needs in retirement.

When it’s time to tap your retirement investments for income, it can be challenging to figure out how much you can afford to withdraw without depleting your savings too quickly or generating a significant tax bill. That’s why Schwab created Schwab Intelligent Income™, which pairs the technology of Schwab Intelligent Portfolios® with a tax-smart withdrawal strategy that generates a predictable monthly paycheck from your investments.

When you activate the Schwab Intelligent Income feature on your Schwab Intelligent Portfolios® account, you receive a projection of a monthly paycheck amount based on your portfolio value and time horizon, tools to help see how far your savings could go, notifications if you veer off course, and tips for getting back on track.

Learn about Schwab Intelligent Income at schwab.com/intelligentincome.
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*Transfers from qualified accounts must be initiated at the firm holding your assets.

6. Request a check with funds from your enabled accounts

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With thousands of fund choices available, building a diversified portfolio can be challenging. Schwab’s Personalized Portfolio Builder simplifies the selection process by helping you find the mutual funds or ETFs that meet your needs.

How does it work?
The tool helps you create a portfolio of funds using Schwab’s asset-allocation models. These models help you determine an appropriate allocation across various asset classes, based on your financial goals, risk tolerance, and time horizon.

How do I get started?
Log in to schwab.com/portfoliobuilder to build a portfolio in five easy steps:

Step 1: Choose the account in which you want to build your portfolio.

Step 2: Select your fund preference. You can build an all-ETF portfolio or all-mutual-fund portfolio—and choose taxable-bond funds or municipal-bond funds.

Step 3: Select your risk tolerance, ranging from conservative to aggressive.

Step 4: Specify your initial investment. There is no minimum, but we suggest at least $5,000 to ensure proper diversification.

Step 5: Choose from a selection of funds within each asset class and click “Trade” to complete your portfolio.

Create a customized portfolio of mutual funds or exchange-traded funds (ETFs) in just a few clicks.
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Onward/OnInvesting
Bleed: 8.1875” x 10.5”
Trim: 7.9375” x 10.25”
Live: 7.4375” x 9.75”

Issue: September 3, 2020
I was born in 1937, and since then have seen my fair share of times when our country struggled with seemingly insurmountable challenges. Financial crashes, pandemics, wars—big problems without obvious solutions. They were defining moments of my lifetime, and of the generations that endured them.

The COVID-19 outbreak feels unprecedented, and in many ways it is—but so too were polio, the Great Depression, and the 9/11 terrorist attacks. In every case, we endured. We may have gotten knocked down, but together we got back up and moved forward.

That kind of perseverance is the heartbeat of this country—and of investing. The greater the challenge, the greater our resolve to come back stronger than before.

I know times are tough, but look to the future. Things will get better. And in the meantime, remember we’re here for you—at schwab.com, through our Schwab Mobile app, or by calling our experienced representatives at 800-435-4000.

Charles R. Schwab
Founder & Chairman

See page 38 for important information.
(0820-0NMH)
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