TIME TO TAKE STOCK INVESTORS REBALANCING THEIR PORTFOLIOS SHOULD AVOID TEMPTATION TO BE TOO AGGRESSIVE

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For conscientious investors, it's the time of the year to "rebalance" those investment funds. With the market rally started in March now firmly established, more investors are flocking to stocks. But market watchers and financial planners caution a controlled approach.

In conservative, buy-and-hold investing circles, asset allocation (putting investment funds into various securities according to the risk tolerance of the investor) only works long-term when the investor rebalances his portfolio from time to time to account for fluctuations in the markets.

For example, since the beginning of this year, the S&P 500 index - considered the broadest gauge of how the U.S. stock market is doing - is up about 20 percent, following three years of losses. Meanwhile, returns on bonds have generally suffered.

Under the rebalancing theory, an investor who originally set up a company 401(k) account with a 70/30 stocks-to-bonds ratio should take the profits from the gains in equities and put their cash value back onto the fixed-income side of their portfolio, calibrating back to that original breakdown.

The problem is, most people don't bother to rebalance. An even bigger problem is that taking money off the winning horse and putting it on the loser seems totally counterintuitive on the face of it.

"There's always that fear that the train's going to leave the station without them. (Investors) have to battle the fear and greed," said Christopher Worsh, a professional day trader and editor of Day Trading It, a daily stock picking newsletter.

"We suggest rebalancing every six months," said James Estes, president of Arrowhead Financial Group in San Bernardino and head of the Inland Empire chapter of the Financial Planning Association. "About 35 to 40 percent of our clients rebalance."

For those who do plan to rejigger their portfolios early in the new year, Estes advises they resist the urge to shift their mutual fund mix to more aggressive stock combinations.

"Unless something's changed personally in your life or something's changed with your mutual fund or you just become hugely optimistic, I wouldn't change much."

That philosophy goes back to the unemotional, logical approach that all securities professionals, from financial advisers to day traders, preach. The worst thing an investor can do is react dramatically to a rally, a correction, or even a mutual fund scandal. That's particularly true for people saving long-term for retirement.

On the other hand, there's nothing wrong with putting some of your investment eggs into riskier baskets.

For investors already in large capitalization growth stocks and looking for something else to pair with those positions, he likes financial institutions and the biotech sector. "(Biotech) is where the venture capital is going," he said.

Technology issues, which led the year's runup, have receded recently as investors have shifted holdings into traditional General Motors-type stalwarts and dividend bearing shares. Traders say the shift reflects new concerns about a mini-bubble.

"Stocks that led the rally off the March lows have been under selling pressure; like Cypress Semiconductor, Corinthian Colleges, Intel, Advanced Microdevices. It doesn't mean they're not going to participate, but there seems to be a shift to the traditional favorites," said Dan Sullivan, a portfolio manager in Seal Beach and editor of the Chartist stock newsletter.

He said that the fact that the Nasdaq underperformed the Dow Jones Industrial Average through the rally may be a sign of choppy waters ahead.

Still, he expects any corrective activity will be a blip along the bull run. "Going back to 1941, when you go 100 days without a correction, then there's one of five percent or so, the market still has 40 percent to go."

Worsh, the day trader, is more pessimistic.

"I'm concerned," he said. The first warning that the rally could shift was that the Federal Reserve announcement Dec. 9 that it was leaving interest rates at 1 percent was not well received by the market. Then, stocks fell again on news that Saddam Hussein had been captured.

"Not that the market should rally on good news, but it was quick to sell. It's getting jittery."

He warned that the current rally could be a mini-bull in a larger bear market. But again, that's pure speculation, which he never lets influence his own trading system.

For financial planners like Robert Goldsmith, a principal at Financial Fitness and Living Trust in Simi Valley, the goal is to strip out as much of that speculation and risk as possible. That's why he likes variable annuity instruments that have guaranteed minimum returns, products that have only been around for the few years since the market collapsed.

He said he's getting more interest in the products from younger investors whose retirement funds were hurt during the downturn, but still want some exposure to riskier investments.

The drawback to these annuities are that they come with extra fees. But the guaranteed returns make up for that, he argues.

The best thing about the product, he said, is the peace of mind it brings. "I don't speculate about the markets," said Goldsmith. "But if there's one thing I do know, it's that no one knows what's coming."

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