Q. My daughter is 26 and getting her first job with a 401(k). How should I tell her to invest it? I know she's young so she has time, but I think the stock market is pretty high right now and using all stocks could be a mistake.
— Trying to help

A. Glad to hear your daughter is on the road to being self-sufficient.

Participating in a 401(k) is an important step on that path.

Many young people do not take advantage of contributing to their company 401(k) plan because they do not feel that they can afford to do so, said Marnie Aznar, a certified financial planner with Aznar Financial Advisors in Morris Plains.

But participating in the plan is the only way to take advantage of employer matching funds.

Aznar said she should contribute at least enough to get the full company match. If she can do more, that's even better.

"The more she can save and the sooner she can do so, the better off financially she will be in the long run," Aznar said. "Additionally, assuming that your daughter is contributing to a regular 401(k) plan on a pre-tax basis, this will allow her to reduce her current tax burden by reducing the amount of income that will be subject to income taxes."

In terms of helping her make a choice about the underlying investment options, there are a variety of issues to consider.

Aznar recommends you look at the expense ratios of the investment options with your daughter, knowing the lower she can keep her expenses, the more she will be able to keep in her pocket. This may mean opting for the index funds or other low-cost options within the plan, she said.

Another consideration is a target fund, if one is offered by the plan.

"These funds are often ideal for young employees and/or inexperienced investors who are looking for a well-diversified, low-cost option that will be appropriately aggressive depending on his/her age," Aznar said.

For example, if your daughter is 26 and thinks that she would like to retire when she is 60 years old, that would be the year 2034, Aznar said. So if her plan offers target retirement funds, there's probably an option that corresponds closely to this year, such as "Target Retirement Fund 2034."

"Because your daughter is quite young and has many years to ride out the ups and downs of the market, it is likely that this fund will be quite aggressively managed at this point in time, but over the years, will become more conservative," she said.

Aznar said you should look at the underlying investments within the target retirement fund. Usually, there is at a minimum a domestic stock fund, an international stock fund as well as a well-diversified U.S. bond fund. This one holding should provide her with a fairly well-diversified global portfolio, she said.

You're correct that the market is higher now, but keep in mind she will be contributing for many years at varying market levels.

"Due to the fact that she will be investing a lump sum on a regular basis, this lump sum will allow her to purchase more shares of the investment that she chooses when the market drops and holdings are less expensive, a form of investing called dollar cost averaging," Aznar said.

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