

Retirement Planning

Why is Retirement Planning Important?

With Social Security's assets being consumed and the number of workers that will support it shrinking, we will have to rely more on our personal savings when it's time to retire.

Today, we have a myriad of options to help each of us prepare. Yet, without a plan of action, many find themselves falling short when it's time to retire.

How Much Money Will I Need?

To calculate how much income you will need in retirement, you must estimate your retirement cost of living. You should calculate how much it will cost in today's dollars to sustain the life style you want. Then you should estimate the rate of inflation you expect and factor that into the equation. You will need to estimate the number of years you plan to be retired and the date you would like to retire. Armed with this information and a projected rate of return for your investments you should be able to calculate how much you will need to save every month to retire comfortably.

Although there are tools on the internet to help you do this, it is advisable to consult with a financial planner when making such an important decision that will affect your retirement.

Sources of Retirement Income

Sufficient retirement savings is often the biggest factor in a comfortable retirement, below are other sources that can provide a foundation or supplement your retirement savings:

Pension

Defined benefit retirement programs or pensions are increasingly becoming a thing of the past. But, if you are fortunate enough to be covered by a pension program it is likely that it is backed by the Pension Benefit Guarantee Corporation, a government sponsored entity that insures the funds companies put aside in their pension trust accounts. A pension is a great building block for a secure retirement.

Social Security

Your benefit amount is based on your earnings averaged over most of your working career. Higher lifetime earnings result in higher benefits. If you have some years of no earnings or low earnings, your benefit amount may be lower than if you had worked steadily. If you work for someone, your employer reports your earnings. If you are self-employed, you must report your earnings yourself.

Your benefit amount also is affected by your age at the time you start receiving benefits. If you start your retirement benefits at age 62 (the earliest possible retirement age) your benefit will be lower than if you wait until a later age.

To help you plan for retirement, each year the Social Security Administration sends you your personal *Social Security Statement*, which gives you an estimate of the monthly benefit amounts you and your family may qualify for now and in the future. If you've received your *Social Security Statement* and have questions you may want to review your statement with your financial planner so he can help you make decisions now that will lead to a secure retirement.

IRAs, 401k and Deferred Annuities

IRA's are tax deferred retirement savings accounts that can be set up as a mutual fund or annuity account with a variety of investment options. A regular IRA account can provide a tax deduction for the original contribution amount. Taxes would be paid when the funds are withdrawn during retirement, when you would likely be in a lower tax bracket. A Roth IRA does not provide an initial tax benefit, but its growth is non taxable, assuming that congress extends the authority of Roth IRA's past the 2010 sunset provided in the sunset provision of the law.

401K contributions enjoy the same tax benefits. You may be able to contribute more to a qualified plan if your employer offers one. Your employer may also match your contributions. Usually it is advisable to set aside at least enough to benefit from your full employer match.

Deferred annuities are also available with IRA status through insurance companies so that you can set aside income on a tax deferred basis and enjoy earnings with taxes deferred.

Life Insurance

Most people need life insurance when they are younger to provide for their family in the event of their death. If you purchase permanent insurance you may be able to enjoy estate planning benefits and retirement benefits from the purchase of your policy.

Equity built up in a cash value Life Insurance may help you fund your retirement. Universal, Whole Life and Equity Indexing policies can build value which could be borrowed or paid upon a surrender of your life insurance contract.

Real Estate Income/Reverse Mortgage

A second home, investment property or even your primary residence can be a source of retirement income. A second home or investment property may be rented to provide income or sold to receive the cash needed to create an annuity (income stream) through your retirement.

A Reverse Mortgage may be obtained to help you access the equity you have built up in your principle residence to pay off your traditional mortgage, create an annuity or lump some of cash for use in your retirement.

Life Stages

Having a sound overall financial strategy requires that you recognize that your finances are in a constant state of change. Not only do financial markets fluctuate, but also your financial needs change over time. Luckily, it is easier to predict the changes in your financial life stages than it is to predict the direction of the financial markets.

Most individuals pass through three primary financial life stages as they age. Income levels, spending patterns, family situations and areas of financial concern, while not exactly predictable, tend to follow a pattern.

Remember that there is a big advantage in starting to save earlier in life rather than later.

Life Stage	Life Events	Financial Events
Early	Enter work force Marriage Children	Develop financial habits Purchase car Purchase home
Mid Life	Family grows Career advancement Inheritance	More home purchases Accumulation of wealth Funding college educations
Approaching Retirement	Major promotion Retirement Grandchildren Death of spouse	Greater tax sensitivity Preserving wealth Estate planning

Risk Tolerance

Handling Market Volatility

Your grandparents may remember a time when the investment markets were more regular, with no huge mood swings in either direction. Investing was relatively easy. But like manual typewriters and black and white TV, those days may be gone forever.

The roller coaster ride of the last several years has left many investors shaken, confused, and unsure of what to do with their investments. Opening their 401(k) statements has become a scary proposition—am I up this quarter? Am I down? How far down? What do I do? And when should I do it?

Volatility: It's a Fact of Life

First of all, we need to understand that it's normal for the markets to fluctuate as a regular part of the business cycle. The 18-plus-year steady run-up that produced huge gains was an anomaly. How you deal with the volatility will affect your ultimate investment balance, and also how well you sleep at night. Here are a few common sense tips to help you get started.

Asset Allocation is Basic

Experts agree that asset allocation—spreading your money across different asset classes (stocks, bonds, and cash equivalents)—is a good way to help minimize some of the risks of investing. And taking that a step further by diversifying your investments within each asset class (large-cap stocks, small-cap stocks, long-term bonds, short-term bonds, etc.) can potentially stabilize your investment returns while further decreasing

your investment risk. That's because different investment types tend to move in different cycles; when one kind of investment is up, another type may be down. Having a variety of asset classes in your portfolio will enable you to better weather the rough spots in the market. The mix of investments that's right for you will depend on your age, your retirement time horizon, your investment objectives, and your risk tolerance. There are a number of interactive worksheets and modeling tools readily available with sample portfolio allocations to help you create your own strategy.

Time in the Market vs. Market Timing

If you're saving for retirement through your employer's 401(k) plan, you're already using a proven investment approach called dollar-cost averaging that can help minimize some of volatility's adverse effects and turn it into an advantage. Because your contributions come out of each paycheck, you're investing a fixed amount of money in the same investment over regular intervals. This way, your contributions buy more units of that investment when the price is lower and fewer units when the price is higher. As a result, your average cost per unit tends to be lower than the average price of the unit—whether the market is headed up or down. Dollar-cost averaging doesn't guarantee a profit or prevent a loss, and it involves continuous investment regardless of fluctuating price levels. However, it can help you minimize the risk of investing all your money at a market high. It's an old saying—time in the market is more important than trying to time the market.

Think Long-term, Not Short-Term

Create a long-term investment strategy and stick to it. Ever been on a boat in rolling seas? An old sailor's trick for easing the queasiness in your stomach is to keep your eye on the distant horizon and not focus on the swells beneath your feet. It's the same with investment volatility. Keep your eye on your long-term goals and don't overreact to short-term market swings. You can make yourself crazy by watching the daily fluctuations in both the markets and the value of your retirement plan balance. Don't make drastic portfolio changes based on current market conditions. Selling off poor-performing investments might turn a potential short-term loss into a permanent loss. Although past performance is no indication of future results, history shows us that markets tend to recover, even if it takes a year or more to do so.

Periodic Check-ups for a Healthy Portfolio

Even with a long-term strategy, it's important to review your portfolio periodically to make sure it's still keeping pace with your life and your goals. The birth of a child, or sending one off to college, can change your financial priorities. It's important that your financial strategy reflects your current circumstances, so make a point to review your financial goals, your asset allocation, and your risk tolerance level at least annually. Even if you haven't had any life-changing events recently, you may need to rebalance your portfolio to bring it back in line with your original intentions if there have been significant shifts in the markets.

Risk, Return, Reality

Remember that there are all kinds of risk, and that all risk is not created equal. The kind

of risk most people think of first when they think about "risk tolerance" is market risk. That's the risk that your investment will lose money, and it's what keeps many people from investing in the first place, or leads them to choose more conservative investments. That kind of "safe" approach overlooks inflation risk, which is the risk that your investment will not keep up with inflation. This may actually prove to be a greater threat to your future financial security.

Remember, too, that the flip side of risk is return. The greater the potential risk that an investment has, the greater the potential reward. How much reward are you aiming for, and how much risk are you willing to tolerate in order to possibly achieve that goal? Generally speaking, the younger you are, the more risk you should be able to tolerate, given that you have a long time frame until you're going to need that money. The closer you are to retirement, and to needing to tap into that nest egg, the more conservative you probably want to be.

Make it Work for You

There's no such thing as a risk-free investment, and volatility is a fact of life. Handling volatility, and turning it to your advantage instead of trying to avoid it, involves finding a comfortable balance between appropriate risk and desired returns and managing your investments to that end. Help is available from a variety of sources, including the Internet, the library, and professional investment advisors.

Retirement Planning Consultation

It is never the wrong time to set up a Retirement Planning Consultation with your Financial Alliance Partner. It can be the first step in the right direction for many people. It is also important to meet them at least annually to make sure your plans stay on track.

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