The NEW Rules for Planning Your Retirement

Decades ago we watched older generations retire with a full pension, a golden watch and a firm handshake. Essentially that same generation would have an investment portfolio that looked something like this: Stock in GE, Stock in Coca Cola, Stock in Disney, Stock in AT&T and maybe a few other blue chip US companies that paid a nice dividend, and that would make up about 60% of their portfolio. Then they would have individually issued bonds to make up the remaining 40% of their portfolio. This mix combined with whatever cash they had in the bank earning double digit interest would have been more than sufficient to get them through retirement and maybe even leave a few bucks to their kids.

Today the game has changed quite a bit. For starters many of us will not have a pension to get us through retirement. It will be entirely on us as individuals to generate just about every dollar we make during the golden years. Of course we will have social security, but social security may hardly be enough to cover the ever rising costs of just our most basic needs. We may never see double digit interest in savings or CD accounts again. In the old days, whatever was happening across the globe had very little impact on us. Today our economy has become so globalized that when something happens in Papua New Guinea it sends a ripple across the S&P 500 [1]. In 1994 there was a rule introduced by a financial advisor that said that if you withdraw 4% per year from your portfolio when you begin your retirement, and adjust annually for inflation, you have a low probability of depleting your retirement account before you pass. Since this study was published, many theoreticians have poked holes in the 4% rule, and some have said that 3% or less might be a better rule to play by. What this translates to for you is that for every $1,000,000 you have saved, you should pay yourself $30,000 per year if you don't want to run the risk of outliving your money. Pretty scary right? If $30,000 doesn't sound like much now, imagine what that same amount will sound like in 20-30 years, which is potentially how long you and/or your spouse might live in retirement.

What does all of this mean for you? Why are you reading this e-book? Within these pages, we hope to give you some insight as to what the NEW rules for planning your retirement look like versus the retirement plan of yesteryear.

Phase 1- Discovery Period

In the past, when advisors sat with a new client or prospective client, they were most concerned with what their risk tolerance was which helped determine what the appropriate stock to bond ratio would be. Today, while it is still as important as ever that clients stay within their risk tolerance parameters, it is much more valuable to start the conversation by

1. The S&P 500 Index is an unmanaged index of 500 common stocks that is generally considered representative of the U.S. stock market. Performance of an index is not illustrative of any particular investment and performance figures quoted are historical. It is not possible to invest directly in an index.

establishing what clients' goals are. Are they short term? Are they long term? Are they wishes or necessities? Establishing these goals allows us as advisors to establish the framework we must operate in to build a plan. The reason this is such an important change from the old way of planning is that, now when an advisor meets with a client for a review meeting, conversations are shifted from the performance of the portfolio versus the S&P 500 (which is likely not an accurate benchmark for their portfolio due to the fact that most investors do not have a portfolio consisting of entirely US common stocks), and the focus can be placed on the progress towards pre set goals. This process gives us guidelines with which to measure our success or failure. If you told your advisor in your first meeting that you would like to be able to buy a vacation home within 5 years, with the NEW way of planning you have the ability to lay out exactly what would need to happen along the way in order for you to achieve your goal. If that means you need to save more annually, then so be it. If it means we need to average 20% per year in returns, then that's our goal. But now clients and advisors are able to have real meaningful conversations about what your goals are and what will need to take place in order to achieve those goals.

Here's a case study as an example:

Mr. and Mrs. Client meet with their advisor and express their desire to buy a vacation home in 10 years. They wish to be able to pay cash for their home so they won't have to make mortgage payments. The home they are looking to purchase will cost them about $500,000 in 10 years, and they have $250,000 saved towards this goal so far. In order to achieve their goal without them adding any additional funds, we would need to average 7.2% per year. Now let's assume that 5 years into their plan the market is tanking and they want to come in for a review. The old way of planning would have us sit and discuss how their account has held up versus a benchmark, which really does nothing to help us figure out where they are on their path to buying the vacation home. If, however, we can sit down and show them that even with the recent draw down, they have still averaged 7.2% or thereabouts since inception of the plan, then the conversation becomes easier and clearer as to what we need to do.

Now we're in year 8 of our 10 year plan and Mr. and Mrs. Client are in reviewing their portfolio again. This time it looks like we have averaged closer to 9% since inception and we only have two years to go. At this point we can consider adjusting the account to take less risk for the final few years because we are ahead of schedule and we don't want to have to worry about a significant correction in the home stretch. By establishing this type of frame work, we are able to take a client with a high tolerance for risk and show them that in this particular case, risk may not necessarily be rewarded and it's best to just coast to the finish line. [2]

2. This is a hypothetical illustration only and is not indicative of any particular investment or investment performance. It does not reflect the fees and expenses associated with any particular investment, which would reduce the performance shown in this hypothetical illustration if they were included. In addition, rates of return will vary over time, particularly for long-term investments.

Phase 2- Implementation

Now that we have our goals established we can discuss the tools we can/will use to accomplish these goals. There are literally thousands of ways for us as advisors to skin this cat, so no two plans will look alike. It is during the implementation process that you should be having the conversation about time lines, liquidity needs, short/long term investment time horizons, etc. It is also important to address risk management at this juncture. We know that for some people insurance is a bad word. We understand that the mere thought of life insurance makes some people cringe. We want to make it clear that life insurance is not for everybody, but it SHOULD be discussed as part of the planning process. You have worked hard for your entire life, why wouldn't you want to protect what you worked so hard to achieve? Life insurance is more than just passing money to your survivors. Life insurance is protection for your spouse or life partner so he/she doesn't have to sell the home you made so many memories in. Life insurance can also be a great tool to protect your assets in the event you have a long term terminal illness, which as we know can be VERY costly and could potentially wipe out any funds you have saved. Lastly, for wealthy individuals that have maxed out every other tax advantaged savings option made available to them, life insurance can be a terrific savings tool if set up properly. [3]

During phase 2 is when the conversation about the appropriate stock/bond mix for your plan should take place. It is important to understand that risk tolerance can actually be different for varying pieces of your portfolio. In other words, if you know that part of your plan involves money that is going to need to be accessed for short term needs and might require a lot of liquidity, then your risk tolerance for that part of your plan is going to be very low. On the other hand, if you know that a part of your portfolio is not going to be used until well into your 80's, if ever, then this is a place where a little extra risk might suit you well. Remember earlier when we wrote that old retirement portfolios had a few US blue chip companies in them, and some bonds? The NEW portfolio still starts with the stock/bond conversation, but now you'll need to dive much deeper with your advisor. Now you will need to have international and domestic stocks and bonds. Now you will have emerging countries, as well as developed countries. You will have floating rate bonds, high yield bonds, short term treasuries, long term corporate debt. New research shows that you can reduce the volatility in your portfolio and potentially increase returns by adding alternative investments to your portfolio (according to a Wall Street Journal article from October 31st, 2014 titled "The Case for 'Alternative' Investments"). Are you bored yet? As you can see, there is a lot of thought that goes into building a portfolio and implementing a plan. This is why we stress that most people should not attempt to do this on their own. Advisors do a tremendous amount of research and due

3. Policy loans and withdrawals may create an adverse tax result in the event of a lapse or policy surrender, and will reduce both the cash value and death benefit.

diligence to make sure their clients are getting what is suitable in the retirement planning space. [4]

Please don't fall for the robo-advisor ads you read about or hear about on the radio. Seek the help of a human being and have a discussion about your worst fears. Tell your advisor that you love your children but you don't want to leave them a penny. Let your advisor know that you have a charity you believe deeply in and you want to be able to leave a portion of your estate to this charity. Have the discussion about the business you always dreamed you could open someday if you just had the finances and time to do it. We can help!

Phase 3- Ongoing Review

Now that your advisor knows your in-laws are moving in with you and you have a 40 year old son that still collects a monthly allowance from you, a foundation has been laid and a plan has been implemented. The third and final phase is simply to conduct ongoing reviews. These reviews might be quarterly or they might be annual. You might say "We don't want to hear from you unless the sky is falling." The most important thing is that you meet with your advisor from time to time to discuss your progress and evaluate whether we are still on track to meet your goals. It is imperative that if there is ever a life changing event or if goals should shift at any time, this is communicated to your advisor immediately so that we can adjust the plan accordingly. Now the conversations are shaped more around how you are tracking target objectives instead of how we did versus a benchmark. As an investor and planner, you should be focused more on achieving a set of goals and less focused on how your account has performed versus your comrades at the country club, or your neighbor that seems to always be driving a new car and always has hot stock tips.

We have found that all too often, investors want no risk whatsoever until they see on the nightly news that the stock market is up 30% in a year and they are only up 5%. Once that happens, they become investing gurus and want to shoot for the moon. Goals based planning allows us to sit down and say "Sure, you *only* made 5% this year. When we established your goal of buying a vacation home 3 years ago we figured we would need to average 6% per year in order to achieve that goal in two more years. Have we done that so far?" Conversations become much less complicated and the path to success becomes much clearer. It is no longer a conversation about how much risk you are willing to take, but how much risk you will need to take if you want the best possibility at achieving a given objective. If the risk is too much for you to stomach, maybe we need to re-visit the wants/needs conversation again. Even the best laid

4. There are risks involved with investing, including possible loss of principle. Investments will fluctuate and may be worth more or less than when originally purchased. Investment risks associated with international investing, in addition to other risks, may include currency fluctuations, political, social and economic instability and differences in accounting standards when investing in foreign markets. Investments in emerging markets involve heightened risks due to their smaller size, decreased liquidity and exposure to political turmoil or rapid changes in economic conditions not normally experienced by more developed countries. Risks for investing in Alternative Investments, in addition to other risks, may include increased volatility, or higher standard deviation returns, time horizon risk, risks associated with rapid trading and low tax efficiency, and management issues. Prices of fixed income securities may fluctuate due to interest rate changes. Investors may lose money if bonds are sold before maturity.

plans don't always go off without a speed bump, so change should be welcomed and anticipated. The most important thing is just to know what our destination is. From time to time there will be a road closure or horrendous traffic (we're in Southern California…so… you know!) but with a strong foundation, we will have the tools necessary to navigate back to the final target.

Conclusion

We understand this can all be very overwhelming. If you don't have some basic understanding or knowledge of our industry, the thought of doing anything but keeping your hard earned money under your mattress can be paralyzing. What we do as advisors on a daily basis can sound like a foreign language to some folks. The point of this e-book is not to give you the know how to go out into the world and do this all on your own. What we hope to provide you with is a resource that offers a basic understanding of what you should expect if this whole process is new to you. Even for those that have been investors for many years that may either be in retirement or approaching retirement, this might serve as a conversation piece with your existing advisor to say "Hey, let's re-evaluate our plan." And if nothing else, maybe this has all just been a confirmation that you have been doing things right all along so that you can sleep better at night. Whatever you are able to take away from all of this, we hope you have found it useful to some degree. As always, if you have any questions or if there is anything we can do for you, please don't hesitate to contact us!

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