How long will your retirement capital last?

The table below will allow you to make a rough estimate of the life of your retirement resources, given different assumptions about your initial withdrawal rate and the rate of return on your investments. To account for inflation, the withdrawals are increased by 3% each year after they begin. Rates of return are assumed to be constant, but, in reality, they will vary from year to year. Also important, taxes and transaction costs are not included in the table. That's why the estimate is "rough."

For example, assume that you start with $200,000. If you begin with a 7% withdrawal, or $14,000, your capital will last for 15 years if your rate of return is 4%. If the rate of return could be boosted to 8%, you would get seven more years of payments, each increased by the 3% inflation factor. The table shows just how difficult it is to fund a 30-year retirement.

This example is for illustration only and does not represent any particular investment.

	Rate of Return						
Withdrawal %	2%	3%	4%	5%	6%	7%	8%
4%	22	24	28	30+	30+	30+	30+
5%	18	19	22	24	29	30+	30+
6%	15	16	18	19	22	25	30+
7%	13	14	15	16	18	20	22
8%	11	12	13	14	15	16	18

Source: Merrill Anderson Co.

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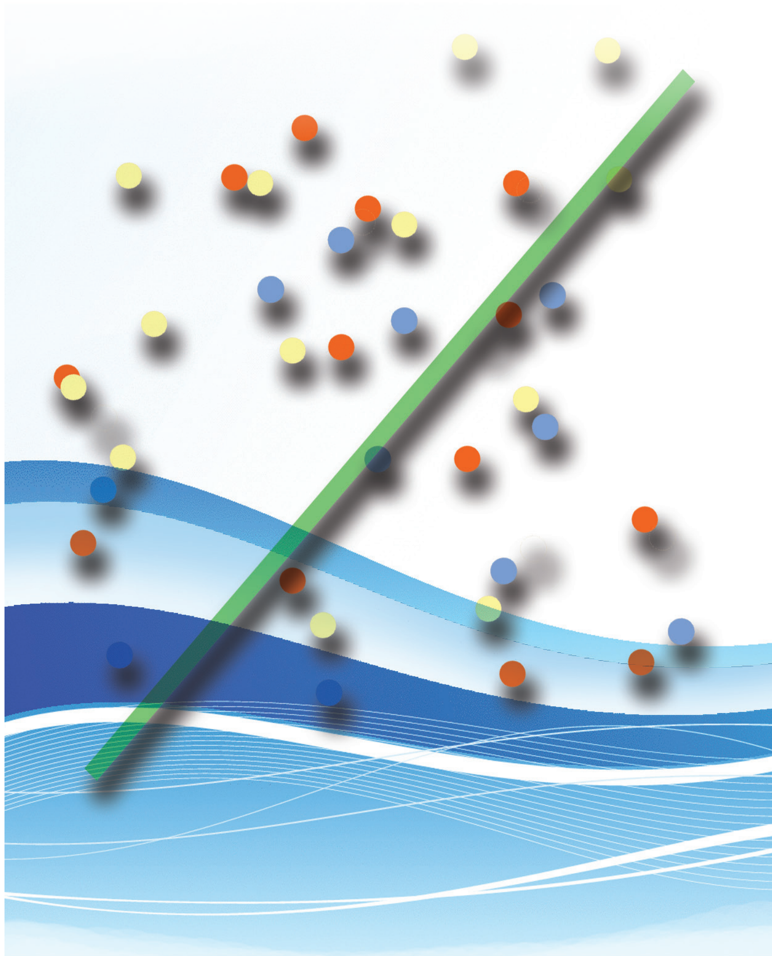
FINANCIAL EDUCATION SERIES

What is Retirement Income Management?



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Retirement income management

When it comes to retirement, there are some things that we can control, and many more that we can't. We can choose how much to save, and how to invest those savings. We can choose the retirement start date. We can choose whether to keep working in retirement, and there may be some discretion in our spending.

We can't control the economic environment that will exist at retirement. Those who are planning to retire in the near term know all too well how financial market reversals can sabotage even the best of plans. Those who were using their homes as a piggy bank for retirement may also face disappointment, as residential real estate remains weak in many parts of the country.

Back to basics

Unless you have won the lottery, there are no magic formulas for creating a secure retirement. Begin with a five-step process:

Review all income sources. Inventory all the predictable income streams that you expect to receive—Social Security, traditional pension, lifetime annuities, rent from real estate, and portfolio income. Compile a list of all financial and real assets, including stocks, bonds, mutual funds, certificates of deposit, IRAs, 401(k) accounts and real property.

Project your expenses. Estimate your monthly and annual expenses in retirement. Divide the expenses into the essentials—food, clothing, housing, transportation, insurance and taxes—and the discretionary—travel, entertainment, gifts and so on.

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Compare income to essential expenses. This will reveal whether there will be an income gap that will have to be filled by touching principal.

Identify assets for essential and discretionary expenses. If you have a gap for meeting essential expenses, you may want to segregate the assets that will be liquidated as needed to fill the hole. Alternatively, you can consider a guaranteed income product, such as an immediate annuity, to take care of the shortfall. Once the essentials are funded fully, remaining assets may be tapped for the discretionary expenses.

Monitor the plan annually. Each year you should review your plan with your financial professional, making adjustments as needed, as your retirement circumstances change.

Five investment rules for retirees

Focus on total return, not yield. When you're living on your investments, you want good income. But you still need to look at your expectable total return—that is, current income plus capital gains or minus capital losses.

For example, when "high-yield" bonds are paying much more than Treasury bonds, some of that extra yield is intended to compensate investors for potential problems or defaults, especially in case of an economic downturn. Going for maximum yield today must be balanced against the need for capital tomorrow.

Don't let inflation creep up on you. Even the yield from good, safe Treasury bonds isn't entirely "income"—except in the eyes of the Internal Revenue Service. Part of each interest payment should be considered an inflation premium. If you spend those premiums rather than reinvesting them, your purchasing power will shrink. For a quick barometer of the inflationary expectations of investors, look to the yield gap between Treasury Inflation-Protected Securities (TIPS) and taxable Treasury bonds. That difference is a measure of the inflation premium, as opposed to spendable income.

Diversify. You never saw an investment article that failed to recommend diversification, did you? Spreading risk is a fundamental way to reduce risk overall.

To diversify adequately, an investor should allocate money among various asset classes. The most basic asset classes are stocks, fixed-income investments such as bonds, and cash reserves. You also need to diversify within asset classes.

Look at the big picture. To control risk through strategic diversification, investors should not look just at their personal portfolios or just at their IRAs. It's the overall financial picture that matters.

Own a $500,000 stake in a closely held business? Think of that stake as the equivalent of $500,000 in small-cap stocks (though less easy to liquidate).

Receiving $40,000 a year from your former employer's tax-deferred pension plan? That's like owning $800,000 worth of bonds yielding 5%.

Unless investors look at their overall financial situation, they're unlikely to develop a properly balanced mix of assets. As a result, they're likely to run more risks than necessary—or settle for unnecessarily low returns.

Seek tax efficiency. Generally, investors who seek higher returns must accept greater risk. But not always. Through careful tax planning, you may be able to live better without taking added risks. Some people who think that they're investing with tax efficiency really aren't. Remember, the goal is not merely to pay the least possible amount of tax. The goal is to net more after taxes.

We can help with your investment choices

Some retirees enjoy managing their investments. Many prefer to enjoy their retirement. If you would like a professional opinion about your portfolio management decisions, please bring your questions to us. We will be pleased to help you on the road to financial independence.