

Strategies for making your money last

Unless you've amassed a fortune which continues to produce large amounts of money, you will need a healthy investment return to stretch your retirement nest egg for as long as you and those close to you will live. You'll need to outpace inflation, which has been low over the last decade but could spike in the future. You'll also need some stable investments to help avoid the severe market losses suffered by many over the last 3 to 4 years, especially if you have recently retired.

For many retirees having all their money in certificates of deposit (CD's), money market funds or government bond funds won't produce enough income to make their nest egg last as long as they need.

How then can you make your money last?

Conventional wisdom has suggested that retirees move the bulk of their money from stock funds to income and bond funds only and never spend the principal. The idea is that many retirees assume they need to eliminate all investment risks.

Actually, despite the market's inevitable ups and downs, a healthy investment in stock related funds has been the key to preserving financial security for many retirees. From June 1950 to June 2004 the S & P 500 Composite Total Return posted an average annual return of

11.95%.¹ That is more than the return on 5 year government bonds, 30 day Treasury Bills and CD's.

An inflation rate of 4% will cut the purchasing power of a portfolio in half in 18 years. Maybe that's ok for some, but most retirees will live longer than their ancestors did. In order to keep pace with inflation, a portion of a retirees' portfolio must have some equity related investments.

A general rule would be to consider that the recently retired should keep anywhere from 40% to 65% of their nest eggs in equity funds and the rest in bond funds, fixed and cash accounts. Again this is a general rule and your specific situation may differ. The right allocation depends in part on your time horizon and your tolerance for risk. If you're 70 years old, you would generally have longer to live than a person at age 92.

As for risk tolerance, if the past decline in stock funds kept you awake at night, you probably don't want risky investments. You would also not want too heavy of a concentration in one industry, such as tele-communications or computer



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equipment and software. A good approach is to diversify the portfolio with a mix of stock funds, bond funds and cash. Then choose a set percentage to withdraw every year regardless of your actual return. For example, you could pick a 7% withdrawal rate and with a good mix of investments earning an average return of 8.5% over ten years, you'd be ahead.

How you take withdrawals is very important, since you could pay more in taxes if you make certain decisions. Since withdrawing funds for retirement is a complicated matter, retirees need to plan by having a budget which spells out how much they will spend and what other sources of income are available (Social Security, Pension, etc.).

If you refrain from taking money from the tax deferred accounts, you could avoid paying higher taxes. Your taxable investments could be subject to the long term capital gains rate of 15%, while an IRA withdrawal is taxed as ordinary income at potentially much higher rates. With the introduction of Roth IRA accounts, you also have more options to avoid paying any income taxes on some of our retirement funds. Unlike IRA's, 401-k's and 403-b accounts, the Roth IRA doesn't require you to make any mandatory withdrawals after age 70 1/2.

Your taxes are also affected by how

much you earn from Social Security since up to 85% of it could be taxed, depending on your income and types of investments. You will also need to consider your estate plan since you may want to leave taxable investments to an heir who would inherit the investment with a stepped up cost tax basis.

If all of this seems complicated, it is. Whatever decisions you make, it may be helpful to get a second opinion and discuss it with a financial advisor who is experienced in assisting retirees in the withdrawal stage and with a tax professional. After all your hard work, saving and investing, this description may seem a little daunting. But just like in business or home life, developing a plan, implementing it and providing ongoing monitoring will go a long way to help you to make your money last as long as you need.

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