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Reassess Your Retirement Plans

Approximately five years before you plan to retire, thoroughly reassess your retirement plans and ensure that all significant financial pieces are in place. Once you retire, you probably won't have the option of going back to your former job. So before you retire, consider these points:

✔ **Take a serious look at your retirement plans.** You're close enough to retirement that you should have a good feel for your retirement expenses and expected income. While you may be anxious to retire, remain flexible about your retirement date. Working an additional year or two can add substantially to your retirement savings and may boost your retirement benefits.

✔ **Get a fix on your Social Security and pension benefits.** Make sure you know exactly how much you can expect from Social Security and defined-benefit plans. How much will your benefits increase if you delay retirement by one year, five years, etc.? If you retire before full retirement age for Social Security purposes, do you plan on still working? Be aware that for those under full retirement age for Social Security purposes, earnings over $15,480 in 2014 will cause you to lose $1 of benefits for every $2 of earnings over this threshold. Make sure you understand your distribution options for any defined-benefit plans. Typically, those decisions are irrevocable.

✔ **Determine how much income your retirement investments will generate.** As a general rule of thumb, you can multiply your retirement investments by 4% to get an idea of how much you can withdraw annually. You can go through a more detailed analysis, reviewing a wide range of variables for a more precise answer. However, the younger you retire, the more conservative your withdrawals should be.

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The Benefits of Low-Correlated Assets

By combining assets with low correlation, you can potentially improve portfolio returns while reducing risk. Correlation is a statistical measure of how one asset class performs in relation to another asset class. Correlations can range from +1 to –1. A correlation of +1 means the two assets move very closely together in the same direction. Combining assets with a high positive correlation will not provide much risk reduction. A correlation of –1 indicates the assets move in opposite directions, a rare event in the investment world. A correlation close to 0 means no relationship exists in the price movements of the two assets.

Combining assets with consistently high correlations to each other does little to reduce risk. The greatest combination benefit to a portfolio seems to be achieved by combining assets with low correlations, which results in reduced risk.

When selecting investments for your portfolio, don't just look at their risk and return characteristics. Also consider the diversification aspects for your overall portfolio. ❍❍❍

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Reassess

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Investigate work options. If you plan to work at least part-time during retirement, have you decided what you'll do and how much it will pay? Make sure you investigate your options, including asking your current employer about part-time opportunities.

Finalize living arrangements. Determine whether you want to stay in your current home or move to another one, either in the same city or a different location. At this point, you should be able to determine whether you'll have a mortgage and how much equity you'll have in your home. While most retirees continue to live in their current home, explore whether it makes sense to downsize, freeing up home equity for investments.

Deal with health insurance and long-term-care costs. Two of the most significant costs in retirement are medical care and long-term care. Make sure you have plans to deal with both. If you are retiring at age 65 or later, you'll be eligible for Medicare, although a spouse under age 65 will not. You will probably need supplemental coverage with Medicare. If you are retiring before age 65, make sure you know exactly how much coverage will cost you, especially if coverage is not provided by your employer. Now is also a good time to take a look at long-term-care insurance.

Live with your retirement budget for a couple of years. Want to really make sure your retirement budget is reasonable? Try living with your retirement budget for a couple of years before retirement. If you can do so without increasing your debt, you can be reasonably confident that your budget will work during retirement.

Please call if you'd like help assessing your retirement plans before you retire. ❍❍❍

Developing an Investment Strategy

How do you go about developing an investment strategy? Here are four steps:

Step 1: Determine your goals. As in any aspect of life, your financial goals will drive your investment strategy. Whether you are planning for retirement, a child's college education, or a vacation, you have to know what you are working toward. If your goal is retirement, for example, what does that look like? A five-star luxury tour of Europe and around-the-world cruise? Or visiting the grandchildren down the street? For your strategy to be successful, it has to be founded on a concrete, detailed articulation of what it's designed to achieve.

Step 2: Examine your financial profile. This is a great opportunity to get a detailed view of your finances — your income, your debts, your assets, your budget, and your existing investments. It will help you learn where you are relative to where you want to be and allow you to develop a strategy to get there. If you have mounds of debt, your first priority may be to pay that off. If your finances are in order but you don't have an emergency fund saved, that may be your first priority. Once you know what you have to work with, you can better achieve your goals.

Step 3: Analyze your investment appetite. Are you a conservative or an aggressive investor? Aggressive investors are willing to accept the potential of substantial financial loss for the potential of substantial financial gain. Conservative investors are willing to accept smaller financial gain for lower risk of financial loss. Whether it's more appropriate to be an aggressive investor or a conservative investor depends in part on where you are relative to your goals.

If your goal is retirement, for example, it is generally more appropriate to invest aggressively when you are younger and further away from that goal. Then it is generally more appropriate to invest more conservatively as you get closer to retirement, pulling your money out of higher-risk investments to avoid losses from which your investments will not have time to recover. Are you striking the right balance?

Step 4: Be advised. Seeking counsel from a credible financial advisor will help you make the best investment decisions based on your goals, your financial profile, and your risk appetite. A financial advisor will ensure that you are getting the most from your investments and your money is allocated properly, helping you rebalance your profile every year. In addition to having expertise in the different types of investments and a deep understanding of what's going on in the market, advisors are not emotionally attached; that can be invaluable in keeping you aligned with your strategy, especially when the market is fluctuating.

Like a good map, an investment strategy will help get you from point A to point Z on the road to achieving your financial goals. To develop a strategy, revisit an existing one, or for help getting back on the road, please call. ❍❍❍

Have You Assessed Your Risk Tolerance?

While investors want the highest returns possible, returns compensate you for the risks you take — higher risks are generally rewarded with higher returns. Thus, you need to assess how much risk you are willing to take to obtain potentially higher returns. However, this can be a difficult task. It is one thing to theoretically answer questions about how you would react in different circumstances and quite another to actually watch your investments decrease significantly in value. What you are trying to assess is your emotional tolerance for risk, or how much price volatility you are comfortable with. Some questions that can help you gauge that risk tolerance include:

✔ **What long-term annual rate of return do you expect to earn on your investments?** Your answer will help determine the types of investments you need to choose to meet that target. Review historical rates of return as well as variations in those returns over a long time period to see if your estimates are reasonable. Expecting a high rate of return may mean you'll have to invest in asset classes you aren't comfortable with or that you may be tempted to sell frequently.

✔ **What length of time are you investing for?** Some investments, such as stocks, should only be purchased for long time horizons. Using them for short-term purposes may increase the risk in your portfolio.

✔ **How long are you willing to sustain a loss before selling?** The market volatility of the past several years will give you some indication of how comfortable you are holding investments with losses.

✔ **What types of investments do you own now, and how comfortable are you with them?** Make sure you understand the basics of any investments you own, including the historical rate of return, the largest one-year loss, and the risks the investment is subject to. If you don't understand an investment or are not comfortable owning it, you may be tempted to sell at an inopportune time.

✔ **Have you reassessed your financial goals recently?** Due to market volatility, your financial plan may need to be revamped. Otherwise, you may find you won't have sufficient resources in the future to meet your goals. Based on your current investment values, determine what needs to be done to meet your financial goals. You may need to save more, change or eliminate some goals, or delay your retirement date.

✔ **Do you understand ways to reduce the risk in your portfolio?** While all investments are subject to risk, there are some risk reduction strategies you should consider for your portfolio. These strategies include:

✔ **Diversify your portfolio.** You should diversify among several different investment categories, including cash, bonds, and stocks, as well as within investment categories, such as owning several types of stocks. A properly diversified portfolio should contain a mix of asset types whose values have historically moved in different directions or in the same direction with different magnitudes.

✔ **Stay in the market through different market cycles.** Remaining in the market over the long term helps to reduce the risk of receiving a lower return than expected, especially for more volatile investments, such as stocks.

✔ **Use dollar cost averaging to invest.** Rather than accumulating cash so you have a large sum to invest, invest small amounts regularly. Dollar cost averaging is a method of investing a certain sum of money in set amounts at regular intervals. This spreads your purchases over a period of time, keeping you from making one major purchase at high prices. Since you are investing a set amount, you purchase more shares when prices are lower and fewer shares when prices are higher. While a valuable investment strategy, dollar cost averaging does not ensure a profit or protect against losses in declining markets. Before starting a program, consider your ability to continue purchases during periods of low price levels. This strategy requires the discipline to invest consistently regardless of market prices and can help develop a habit of regular investing.

Ensuring your investments are compatible with your risk tolerance is an important component of your investment strategy. Please call if you'd like help assessing your risk tolerance. ❍❍❍

Why Have an Asset Allocation Strategy?

Your asset allocation strategy represents your personal decisions about how much of your portfolio to allocate to various investment categories, such as stocks, bonds, cash, and other alternatives. Some of the advantages of an asset allocation strategy include:

✔ **Providing a disciplined approach to diversification.** An asset allocation strategy is another name for diversification, an important strategy for reducing portfolio risk. Since different investments are affected differently by economic events and market factors, owning different types of investments helps reduce the chance that your portfolio will be adversely affected by a particular risk type.

✔ **Encouraging long-term investing.** An asset allocation strategy is designed to control your portfolio's long-term makeup. It should not change based on economic conditions or market fluctuations.

✔ **Eliminating the need to time investment decisions.** Market timing is a difficult concept to implement. Not only do investment professionals have a difficult time accurately predicting the market's movements, but waiting for the perfect time to invest keeps many investors on the sidelines. With an asset allocation strategy, you don't have to worry about timing the market, you just have to ensure your investments stay within the proper percentages.

✔ **Reducing the risk in your portfolio.** Investments with higher returns typically have higher risk and more volatility in year-to-year returns. Asset allocation combines more aggressive investments with less aggressive ones. This combination can help reduce your portfolio's overall risk.

✔ **Adjusting your portfolio's risk over time.** Your portfolio's risk can be adjusted by changing allocations for the different investments you hold. By anticipating changes in your personal situation, you can make those changes gradually.

✔ **Focusing on the big picture.** Staying focused on your asset allocation strategy will help prevent you from investing in assets that won't help accomplish your goals. Rather than investing in a haphazard manner, it gives you a framework for making decisions.

Please call if you'd like to discuss asset allocation in more detail. ❍❍❍

Over-diversification

Diversify. Diversify. Diversify. While this investment advice seems to be continually discussed, it is possible to overdiversify, which can lead to lackluster returns. Thus, it is important to know the difference between healthy diversification and excess diversification.

The primary benefit of diversification for your portfolio is to spread market risk over different stocks in a way that will decrease the impact any one stock will have on your total return. With an appropriate level of diversification, your overall return will not be significantly impacted if one or even a few investments do not perform as expected.

Thus, it is not just the number of investments you hold that impacts your return, but how those investments interact with one another. If you keep adding investments that react to the market in the same way, you are not really diversifying. You are just adding similar investments to your portfolio.

Please call if you'd like to review the level of diversification in your portfolio. ❍❍❍

Financial Thoughts

Current retirees stopped working at an average age of 61, up from 57 in 1991 (Source: *Money* Magazine, November 2013).

In 2013, the maximum monthly Social Security benefit for those retiring at age 66 was $2,533 (Source: Social Security Administration, 2013).

Approximately 62% of couples nearing the end of their careers disagree on their anticipated retirement ages (Source: *Money* Magazine, November 2013).

About 41% of baby boomers do not feel they have adequately discussed their current financial situation with their adult children, while 31% have not discussed whether they have prepared a will, and 68% haven't discussed how they would pay for long-term care (Source: *Kiplinger's Personal Finance*, November 2013).

The average cost of a private room in a nursing home is $248 per day, or approximately $90,000 per year (Source: MetLife Mature Market Institute, 2013).

Only 12% of individuals age 54 take advantage of 401(k) catch-up contributions (up to $5,500 as of 2014) (Source: Fidelity Investments, 2013). ❍❍❍