The Power of Three When it Comes to Your Retirement

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"It's not hard to make decisions
when you know what your values are."

—ROY DISNEY

Introduction: The Power of Three

When I was a kid, I had a ritual on Saturday mornings. I would usually wake up before my two older sisters so I would have the television all to myself. I would typically grab the largest bowl I could find and fill it to the brim with Cap'n Crunch, pour in the milk, and plop in front of the TV for Saturday morning cartoons. Those who grew up in the 1970s most likely remember Schoolhouse Rock, the animated musical series that was entertaining and educational at the same time. Schoolhouse Rock had a catchy little tune called "3 is a Magic Number," and it's one of those songs that if you hear it again you can't help but sing along.

Human beings tend to remember things in groups of three, like phone numbers, which are broken into three chunks of digits—the area code, prefix, and line number. It shows up often in pop culture; The Three Stooges, Three's Company, Snap-Crackle-Pop, three wishes, three guesses, the Three Little Pigs, and, of course, Schoolhouse Rock.

Sports is filled with significant threes as well. Horse racing has the Triple Crown—the Kentucky Derby, the Preakness, and the Belmont Stakes. Hockey celebrates the hat trick: three goals in one game by the same player. Baseball is loaded with threes: three strikes and you're out, three outs in an inning, nine players on a team (3x3), nine innings in a game (unless they're tied). Football awards three points for a field goal. Basketball has adopted the 3-pointer, which has revolutionized the sport. Tennis is defined by game, set, match. In golf, three is the

number of strokes players strive to have on most holes because that would result in a great round.

Plays have three acts. The best circuses featured three rings of action going on simultaneously. Realtors tell you the most important three factors in real estate are "Location, location, location." Julius Caesar's most frequently quoted words are "Veni. Vidi. Vici." I came. I saw. I conquered.

For people of faith, the number three biblically represents divine wholeness, completeness, and perfection. It is used a remarkable 467 times in the Holy Bible. There are twenty-seven books in the New Testament, and twenty-seven is 3x3x3. More examples: the three wise men, the three righteous patriarchs, and the three righteous fathers. Of course, Jesus resurrected on the third day, and we have The Holy Trinity: The Father, Son, and Holy Spirit.

In China, three is a lucky number because it sounds like the word for life. Our existence is described in threes as birth, life, death. Time is often described as past, present, and future.

What about when it comes to your retirement? I think you'll be interested in discovering how the number three adds perspective to retirement planning.

Before we get into that, however, I'd like to tell you a little about myself and why I do this.

I've already offered a glimpse of what my childhood was like. Mom would typically already be awake and making her morning coffee and breakfast for the family. But one Saturday morning, everything changed. I was eight.

On that particular morning, when I looked at my mom's face, I noticed something quite different. It was something that I had never seen before in my short life. I noticed a look of concern, a look of deep worry. As a child, I didn't really know what I was observing at the time. I just knew it wasn't normal. I made a mental note of it and then went on about my day.

Fast forward a few weeks later to a family meeting called by my mom and dad. At this meeting, my mom and dad delivered some life-changing news to my sisters and me: my father's business had failed. My dad was in the construction business in the mid-seventies, right after the recession of 1974 and '75. How many folks remember the oil embargo and waiting in line at the gas pump in the mid-seventies? That is the time frame we are talking about and that is when our family business failed.

Upon hearing this news, we naturally had questions. "What is dad going to do?" "Where is dad going to work?"

The next piece of news was even more of a shock: we were most likely going to have to move because we couldn't afford to live in our current home. I have no idea how far behind my parents were on the mortgage payments, but it must have been pretty dire for them to bring it to our attention at the time. Then, the questions really started flying: "Are we going to have to change schools?" "Where are we going to live?"

Then the third and, in my opinion, most devastating piece of news at this family meeting was that my mom would have to go back to work. You see, my mom was a registered nurse and had put her career on hold to raise the kids—something very common back then. Therefore, she was the lady I saw every single morning when I woke up and I also saw every single afternoon when I got off the bus from school.

During the course of a ten- to fifteen-minute conversation at a family meeting, from an eight-year-old's perspective, my life had completely changed! My dad didn't have a job, the family business failed, we were going to have to move and sell the family house, and my mom was going back to work full-time. It was devastating!

Families pull together—and that's exactly what we did. My mom supported the family for a long time, and she never did stop working. My dad landed back on his feet about three years

later after the recession was fully over, working for another construction company.

When it was time to graduate high school in 1986 and go off to college, I had to think about what I was going to study. I decided that I wanted to figure out why my family went through that situation and I wanted to understand why other families faced similar challenges. I wanted to study Business and Economics. What causes these things called recessions? How do markets and economies recover? More importantly: How can I make sure my family never goes through something like that again? Those intentions later blossomed into "How can I help other families prepare for market downturns and stressful financial times in their lives?"

I studied Business and Economics at Towson University in Baltimore. When I graduated in 1991, guess what? The economy was in another recession! I actually landed a job at T. Rowe Price, which at the time was a smaller mutual fund company based in downtown Baltimore directly across from Inner Harbor.

I share this story because it is what drives me to do what I do every single day. The video displays in my office have a saying: "It's not about the money, it's about your life." My passion and my mission are to help families make a plan for LIVING—and make a plan for scenarios such as recessions. We all go through bad times in our lives. My hope is that with a solid financial plan, families can get through those difficult times. If you're at the point of retiring, maybe you can plan well enough that you can actually help others such as family members, friends, loved ones, or the less fortunate get through difficult times in their lives as well. That's what we think it is all about.

This is where the power of three enters our discussion. I would like to share three pitfalls, three principles, and three pillars of investing and planning for your retirement in this book.

If you're ready, get set. It's time to go!

PART 1

Three Pitfalls of Retirement Planning

> *"By failing to prepare, you are preparing to fail." —Benjamin Franklin*

Pitfall #1: Not Having a Plan

Believe it or not, one of the most common mistakes people make as they plan for retirement is … not having a plan. I would even take this a step further. I think this may be one of the most common mistakes in life. To succeed at anything most people know you have to have a plan. It rarely, if ever, just happens by itself. I'll never forget hearing about the Harvard University study on goal setting and planning conducted in the 1950s. The graduating class of 1953 was asked a question. And that question was, do you have a clear and specific set of goals written down and a plan for achieving them? Only 3 percent of the class had written down their goals and what they wanted to accomplish in the future. Some twenty years later, those same researchers tracked down the class of 1953. They

discovered that the 3 percent with written goals were worth more financially than the other 97 percent of the entire class combined. The researchers also noted that they seem to be happier and healthier than the non-goal setting students.

If you're one of the few who took the time to develop a financial plan, I commend you! However, you're not done. You've got to constantly maintain a plan if you ever want to reach your long-term goals. So many people make the mistake of planning their finances once and thinking they can relax. That's simply not the case. I've seen it many times. They say people spend more time planning a two-week vacation than planning a lifetime retirement.

Simply socking money away in a retirement account such as a 401(k) or an IRA is a great start, but it doesn't truly suffice as a holistic plan. The retirement journey has many potential challenges lurking in the shadows, and without proper planning they can derail the "golden years" you have been looking forward to for so long.

So why do so many people have no plan for the most important and challenging period of their lives? I have my suspicions.

I see a lot of folks who have picked up a bunch of stuff along the way. They have been sold various investment and/or insurance products by multiple companies, agencies, or advisors without truly having a plan in place as to how it all fits together to meet their goals in retirement. We call this the "kitchen drawer" approach to retirement.

I distinctly recall a meeting I had with a couple early in my career. Let's call them Bob and Carol. They attended one of my financial seminars and at the conclusion, they said they wanted to meet with me and go over their plan. Two days later, they came into my office and we sat down in my conference room. After I had gotten them each a cup of coffee, Bob told me his biggest concern.

"I'm worried we're behind," he said. "We didn't get the best jump on things, and I'm worried we'll run out of money when we retire."

When I asked him to explain, he told me a little more about his situation. Over the course of about thirty years, Bob had three different jobs. He'd worked in the printing industry. He owned a small business for a little while. And he was about to retire after nineteen years with a local poultry company. Three jobs generated three separate retirement accounts—two 401(k)s and a SEP IRA. Together, he and Carol had a checking and savings account, some bonds, and a few stocks in a taxable brokerage account. Carol had also moved around in her career. She had an old 403(b) annuity along with a traditional IRA she started and barely funded. The more we got to talking, the more it sounded like they kind of had a *junk drawer* full of investment stuff!

What I'm talking about is probably in the kitchen, just to the left of the coffee pot. This thing is incredible. It has *the* most amazing stuff in it—that rare-sized extra battery for the garage door remotes, the set of those tiny eyeglass screwdrivers, the bottle of super glue, the spare key to your son's house, a paperclip, rubber bands, zip ties, a cellphone charger … I almost believe you could survive on a deserted island with what's in your kitchen junk drawer. It's got some *remarkable* things in it, and yet it's the single most maddening experience to ever have to get into, especially if you have just the slightest hint of OCD. It's just a drawer full of disorganized chaos that makes my eye twitch every time I open it.

The more Bob and Carol talked, the more that's what their situation sounded like to me. I remember her saying, "Well, we've got a *little bit* of a *lot*. And every year, we go in for this appointment where our guy tells us how all that different stuff is doing, and we look at a bunch of different graphs and things, and we nod. But then, we walk out together and just kind of shrug

our shoulders because neither one of us has any idea what any of it *really* means or how it's all going to work together. Can't we just make this *simple*?"

As my career progressed, I soon realized this is much more common than I have ever thought—people who, at some point in their forties or fifties, knew they needed to get started. So, they grabbed the phone, set an appointment, and did just that. I must say, I *credit* them for doing it. They simply got started. And someone helped them get some investments going or put an account in motion here and there.

I see folks like this all the time … they just don't have a *plan*. Or if they *do* have a plan, it's way too complicated and unorganized. In retirement, complexity creates uncertainty. And that concerns me. I've been doing this for many years, and in all that time, I've never understood how anyone could *truly* retire without being confident where their income in retirement was coming from. In retirement, income can truly set the tone for your lifestyle. In that sense, you could say, "Income is the outcome."

Ask yourself this: Do you have a *written* retirement plan in place at this point? To be clear, I'm not talking about a variety of retirement accounts or things you could tap into for money if you needed to. I'm talking about a detailed, yet simple, understandable, and well-written plan.

One of the reasons many people fail to plan for retirement is because retirement can seem like a long way off—particularly when you are in your twenties and thirties. Even in your forties and maybe even your fifties, people might think, "I'll get to that … later." But all of a sudden, "later" is right around the corner—and some folks fail to realize that the sooner they begin planning for retirement, the better off they'll be.

To further explain why starting earlier is better, I'll tell you what is widely known as the "Magic Penny" story. There is a relatively popular anecdote that has been circulating the

financial world regarding a “Magic Penny.” The question is, would you rather have one million dollars today or a penny that doubles in value for the next thirty-one days? Let that sink in for a bit and ask yourself, what would you choose? (And yes, there is a correct answer!)

Here it is. I’ve double-, triple-, and quadruple-checked the calculations on this and if you chose to keep the magic penny, you would have over $10 million by the end of that thirty-one days. To prove it, here is the table below:

Day	Amount
1	$0.01
2	$0.02
3	$0.04
4	$0.08
5	$0.16
6	$0.32
7	$0.64
8	$1.28
9	$2.56
10	$5.12
11	$10.24
12	$20.48
13	$40.96
14	$81.92
15	$163.84
16	$327.68

Day (cont’d)	Amount (cont’d)
17	$655.36
18	$1,310.72
19	$2,621.44
20	$5242.88
21	$10,485.76
22	$20,971.52
23	$41,943.04
24	$83,886.08
25	$167,772.16
26	$335,544.32
27	$671,108.64
28	$1,342,177.28
29	$2,684,354.56
30	$5,368,709.12
31	$10,737,418.24

The lesson here is that saving and investing early is critical. If you ask any professional in the world of personal finance, this is a key theme and should not be taken lightly. There is no actual "magic" involved. Yet the penny shows us the power of compound growth and, in a broader sense, could probably mean years, even decades, when it comes to saving for retirement. So, save early and consistently!

Another big reason planning can seem intimidating is because there's so much information floating around out there now. How does anyone keep up with it all? In my experience, a lot of it is useless and harmful to the investor's state of mind. The good news is you don't have to know everything. You just need to know the right things. Keep in mind, plans come in all different forms. They are, or at least they should be, tailored to each individual, couple, or family. Your journey is unique to you and your retirement strategy should be too. With that established, planning is a fluid process that can differ in each stage. To understand this better, let's explore the three different phases of your financial life.

The Three Phases of Your Financial Life

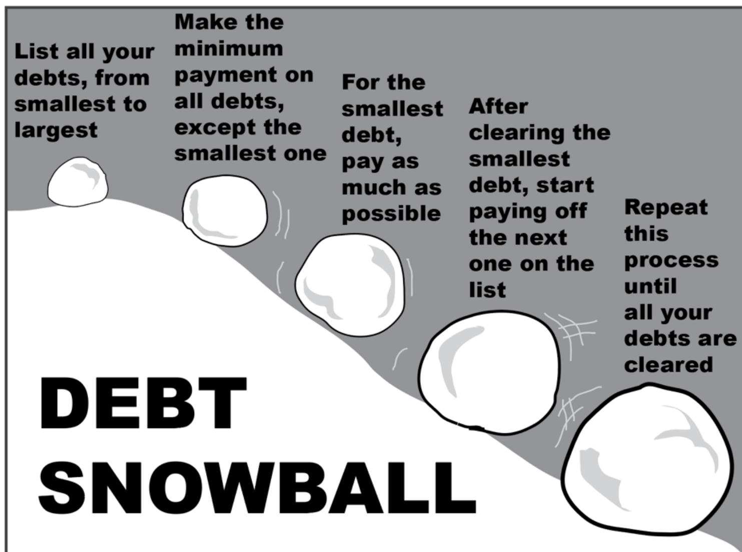
There are typically three phases to your life financially: accumulation, preservation, and distribution. I'll dig deeper into each of them and how you might think about approaching them.

Accumulation Phase: These are the years focused on earning and advancement. These are also among the busiest years of a person's life, both at work and at home. During the accumulation phase, it can be easy to put off retirement planning for other worthy goals and interests, but don't! This is an important time that will help determine your long-term success. You may have decades of working years ahead of you, but you should focus on maximizing your hard-earned dollars.

When it comes to retirement, planning during this phase primarily involves debt elimination, saving an emergency fund, and building net worth. As you're entering the workforce, chances are you may have some student loan debt from college, perhaps a car loan—maybe even a medical bill.

A popular radio personality and personal money managing expert, Dave Ramsey, has what he calls a "debt snowball"

approach to eliminating your debt, and I highly recommend it. Ramsey recommends organizing your debts from smallest to largest. Pay off the smallest debt first while making the minimum necessary payments to your other debts. As soon as that smallest debt is paid off, roll that amount into your next-smallest debt, and pay it off as soon as possible. Continue making minimum payments on the other debts as you progress. Your payments on the smallest debts will grow larger as you go on, just as a tiny snowball gets bigger as it rolls down a hill. Ramsey even suggests taking on side jobs to accelerate debt elimination.



Source: Dave Ramsey, https://www.ramseysolutions.com/debt/how-the-debt-snowball-method-works.

I believe the most important piece of planning during this stage, however, is maxing out your contributions to employer-sponsored plans such as 401(k), 403(b) and Roth individual retirement accounts. How much should you contribute? I usually recommend no less than the maximum amount that your employer is matching because that's free money. When an

employer matches your contributions, you are essentially getting "free money."

There's a second benefit to making contributions to your employer-sponsored plan that many people forget about: your contributions are tax-deferred, meaning your taxable income for that year is reduced by the amount you contribute to the plan. For instance, if your taxable income for the year is $30,000 and you contribute $2,000 to your 401(k) account, your taxable income shrinks to $28,000. That means the amount of taxes you owe will shrink, too. You'll eventually pay taxes on that 401(k) money when you withdraw it in retirement, but you may be in a lower tax bracket by then and pay fewer taxes on that same $2,000 than you would have had you not contributed it to your retirement account.

Another extremely valuable tool during this phase is the possibility of contributing to a Roth IRA. This type of retirement account is different from a traditional 401(k) or 403(b) in that the contributions are made *with after-tax dollars*. In return for using after-tax dollars, your money grows tax free. When you make a qualified withdrawal at retirement from your Roth account, you pay no taxes on your original contributions and all the growth during the many years the account has accumulated. Many employer-sponsored 401(k) plans have a Roth option, and it would be wise to consult your plan administrator to see if that is available. And for some, depending on income limitations, you may be able to open a Roth IRA account completely separate from your employer and increase more of your tax-free savings possibilities! There are contribution limits and possibly income limits on all of these accounts, so you'll want to investigate those before making any contributions. Also, withdrawals from the Roth are tax-free as long as you take them after age fifty-nine-and-a-half and the account has been open for at least five years.

Preservation or Withdrawal Phase: During this phase, you should start to focus on preserving the assets you have worked

all your life to accumulate. There is no specific age range for the preservation phase simply because everyone's retirement age is different. Some folks may retire very early in age. This may pose a significant challenge because they will have to prepare for a longer retirement. And some may actually never retire, either because they are not financially capable of retiring or they simply enjoy their chosen profession and don't want to retire at any set time.

For most folks, the preservation phase is when time is growing shorter and shorter toward their chosen retirement age. You now have less time to regain any losses that may have occurred in investment accounts that are susceptible to market risk. That is typically about five years before someone expects to retire.

Since timing is so important, you must understand exactly how much risk you can afford to accept leading up to this phase. What is so exciting at this time in history is that "Fintech," or financial technology, has really helped advisors determine the risk tolerances of clients approaching different phases of their investing lives. With a simple risk questionnaire combined with an analysis of a client's existing portfolio holdings, an advisor can narrow in on a risk number that is completely personal and individual to each client. Not all investors are the same. Some can handle a substantial amount of market risk while others are completely risk-averse. Using tools that can compute a personalized risk number from one to one hundred really helps to identify the individual's risk personality and may help them achieve greater success in sticking with the overall plan when markets inevitably become volatile. So ask yourself this question: Do you have absolute clarity around how much risk you are willing to take with your investments as you get ready to retire? In other words, what's your risk number?

Another important step when planning for this phase is to determine the costs of your basic needs—such as food, clothing,

housing, utilities, transportation, and health care—combined with your "fun money" income needs. These expenses can be specific to each person's individual goals for fulfilling their core values and should shape how you invest your hard-earned money during this phase. Keeping some of your money safe during this phase is a key component to achieving a stable income plan—one you can rely on and not outlive.

For all the "do-it yourselfers" out there, it's entirely possible to do all the research, seek out all investment options, and put a plan together on your own. If this is something you really enjoy tackling as part of your retirement years, then I wholeheartedly encourage it. For most folks, though, I think it's wise to seek out financial professionals who focus solely on retirees, or those soon to retire, and all the various challenges they may face.

Preserving what you've accumulated plays a significant role in providing you with an income plan. Retirement and estate planners deal with investments that focus on the preservation of assets. Many investors do not have a sound plan for retirement, so turning to professionals in this area can be a shrewd move.

Modern medicine has improved so much over the years that if a couple retires at the age of sixty-five, there's a 50 percent chance both will live another sixteen years and that one will survive twenty-seven more years—roughly one-third of their life.[1] Social Security and any pensions should continue for as long as they live, but they may not provide enough to live on. This is why intelligent planning for your retirement years is so important.

Some folks think retirement is the "final chapter," but I actually don't! I look at it as a new beginning or a second act, if you will. I love working with folks that approach retirement with this mindset.

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[1] Carla Fried. Rate.com. July 19, 2019. "Whats Your Retirement Number? No, Not Savings – Life Expectancy." https://www.rate.com/research/news/retirement-expectancy.

By the way, it is no accident that The Number of Three comes into play here as well. That's because your actual retirement years are often broken down into three sub-phases. They are commonly referred to as the "go-go years, the slow-go years, and the won't-go years."

The initial stage, let's say the first ten or fifteen years of retirement, is referred to as the "go-go" years. Retirees at this stage typically have their health, they have plenty of energy, and in most cases, have the wealth to do the things they have always dreamed of doing. They also have friends of similar age that have those same characteristics and interests. As an added bonus, you may even have grandchildren young enough to actually want to hang out with you. And yes, you can finally book that long-awaited vacation you have always dreamed about taking with the whole family.

Eventually, however, you'll begin to slow down a bit. Father Time catches up to us all sooner or later. You may not travel as much, and you'll generally start to take it easier as your body lets you know how much it can handle. I call this stage your "slow-go" years. Your spending habits may change a bit during the "slow-go" years. Some of the "fun money" that was set aside for travel may shift toward health care expenses, gift giving, dining out locally with friends, and less extensive travel expenses.

The last few years of your retirement might find you staying home a lot, unwilling or unable to travel because of your health. Except perhaps for medical bills, you may not spend as much as you did early in your retirement. I'm not trying to be a downer here; simply being realistic, I call these the "won't-go" years.

It's important to consider what your spending habits might look like during those three different sub-phases of retirement. Typically, what I see with my clients is that they are spending a bit more in their go-go years, and for the record, I encourage them to do that. They've worked their entire life leading up to this moment of retirement, and I believe it's part of my job to

make sure that they enjoy it while they have their health, and they have the energy. This is yet another reason why having a plan in place is so crucial: so you can genuinely enjoy retirement without worrying about whether you are spending too much money. Showing folks they have the ability to take that European cruise, to go ahead and buy that dream boat, or to take their whole family to Disneyland is one of the most rewarding parts of my job.

So, do you have a written retirement plan? Do you know where your money will come from during these different stages of retirement? Have you got a 401(k) or IRA to supplement your guaranteed sources of income such as Social Security or a company pension? How much you've been able to save in those accounts isn't the only thing that will determine whether you're able to live the way you want to or the way you have to in retirement. What truly matters is the actual plan, strategies, and procedures you have in place.

Distribution Phase: This phase defines what happens to your money *after* your death. Depending on how long you live and your specific estate planning goals, there may not be much left to distribute to your heirs. For those who will leave assets behind, however, it's important to have a distribution—or estate—plan when you depart this life. The more defined that plan is, the fewer the headaches—and perhaps heartaches—for those you leave behind. Remember the "kitchen drawer" approach we spoke about earlier? Just imagine leaving that mess behind for your loved ones to sort out.

You'll also want to distribute your assets in the most efficient and tax-advantageous way possible. Estate planning attorneys and retirement planners can help you get there. Don't make the mistake of thinking, "I'll get to it eventually," because leaving this world without an estate plan in place will not serve your loved ones well. You'll want a will, a durable power of attorney, a health care power of attorney, and a trust or multiple trusts set

up, if applicable, to avoid probate, estate taxes, and possibly nursing home spend-down.

Without proper planning and documentation in place, probate costs and estate taxes may take a substantial bite out of your assets. And bear in mind that you may need to adjust these plans as your circumstances evolve. That flexibility could be valuable as you strive to make the most of your retirement years.

Pitfall #2: Analysis Paralysis

> *"The secret of getting ahead is getting started."—Mark Twain*
>
> *"Investing and technical analysis are two realms of the financial industry that can be highly susceptible to analysis paralysis. A broad range of theories, concepts, and best practices have been established to help all types of investors arrive at investing decisions." —Investopedia*

Have you ever heard of the ancient fable, the Fox and the Cat? The fable involves the two animals having a conversation on the best way to avoid and survive the hunting party's vicious dogs. The Cat tells the Fox he can think of only one way to escape while the Fox brags to the cat of the numerous solutions he has come up with. The next day, the hunters arrive with their dogs to begin the hunt. The Cat immediately escapes up the closest tree while the Fox contemplates the numerous ways he could choose. Unable to decide which option is best, he fails to take action and meets his fate.

Information bombards us each day and it's hard to ignore it all. In fact, we may be tempted to absorb as much "news" as we can, telling ourselves we need to stay "informed." But that can be a mistake. I believe most of it is useless and harmful to the investor's state of mind. "Analysis paralysis" describes an individual or group process when overanalyzing or overthinking a situation can cause forward motion or decision-making to become "paralyzed," resulting in no solution or course of action.

The biggest thing that causes Analysis Paralysis is simple, yet so common: feelings of anxiety, fear, worry, and mistrust, to name a few. Sometimes, folks deal with crippling anxiety when it comes to their finances because it is a big deal, especially when

it comes to your retirement. And who wants to make poor decisions when it comes to your financial health? In reality, doing nothing is sometimes worse than doing the wrong thing. What are the most common worries when it comes to retirement? How can you help alleviate them? Let's discuss the three most common worries amongst pre-retirees and retirees nowadays.

The **first major worry** when it comes to folks' retirement is the **fear of running out of money.** For nearly half of Americans, their worst fear is not saving enough money for retirement. A survey by the financial institution Primerica found that 43 percent of Americans list that as their biggest fear. Conversely, only 25 percent said they feared death the most.[2] That should tell you just how important it is to plan well for your retirement.

When it comes to your retirement, what do you really need? Income! The beauty of working is you earn income. Will you still need a paycheck when you quit working? One hundred percent. Do you want that paycheck to come regularly? Absolutely.

Seriously, let that sink in for a moment. *What really matters when you retire is: "Where is your income going to come from?"* and *"How will you get your income to be consistent and stable?"* To help answer those overarching questions, try asking yourself a few sub-questions.

The first and seemingly obvious question to make sure you have answered is simply, where is the money? The first step to answering this is to take an inventory of where you have your money. More than likely, it's scattered in several different locations, accounts, companies, policies, etc. Creating a retirement plan pulls this all together, and frequently, the simple act of consolidation is a huge weight off people's shoulders. Seeing all your money in one comprehensive plan will allow you to have complete clarity over your finances to help you stop

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[2] Katie Brockman. Yahoo Finance. April 12, 2019. "Americans Fear This One Thing More Than Death." https://www.yahoo.com/now/americans-fear-one-thing-more-101500978.html.

worrying about your money. Taking this one step can help you feel better about where you stand financially, because you will have a clear and accurate picture.

Once it's all pulled together and clarified, the next question to ask is: where is the income? Knowing where your income will come from, how you will receive it, and how much you will receive can help you live your best life in retirement with confidence.

The goal is to create an income stream for life that will likely never run dry. So, the next question you want to ask is how long will it last? The entire purpose of the retirement plan is to be able to spend your available money and not be worried about whether you will run out. So, we must stress-test the plan: Run a test with over a thousand trials and see if it holds up under good times and bad!

That leads us to another question and what is also the **second major worry** when it comes to retirement planning**. The question is, how risky is your portfolio? And the worry is, am I taking too much risk in my portfolio?** Let's recall that great phrase from when you were a kid: "Don't put all your eggs in one basket." Well, that adage could not be truer when it comes to retirement! That can range from taking on too much risk by having too many "eggs" in risky investments to having too many "eggs" sitting in low-risk investments and thus not keeping up with inflation.

If you ask a room full of people what their risk tolerance is, you'll get a variety of answers. Some might say, "Oh, I'm moderate or slightly moderate." Or "I'm conservative, risk-averse." Or "I like to take a good amount of risk." Ultimately, those are just words. Your version of moderate might mean a loss of 10 percent in a given year, whereas to your advisor it might mean a 20 percent loss in a given year is acceptable. It's extremely important to be on the same page as your financial advisor.

I like to take a different approach with my clients, and it starts with elements of statistics and math, because the most important thing to remember is that risk *can* be measured. There are various tools used to measure risk, such as standard deviation, beta, R-Squared, and Sharpe ratios, to name a few. Standard deviation is a measure of risk that an investment will not meet the expected return within a given period. The smaller the standard deviation for an investment, the less risky it is. The Sharpe ratio is the measure of a portfolio's risk-adjusted return. A portfolio with a higher Sharpe ratio is considered superior in relation to its peers.

I briefly mentioned in the previous section that I like to use something we call a risk number, which falls on a scale of one to one hundred. It's pretty simple to understand and I like the fact that it's based on mathematics, which is widely deemed as a "universal language." A financial technology company called Riskalyze developed tools to help financial advisors create portfolios individually tailored to a client's needs. That includes a questionnaire to help precisely measure the appetite and capacity for risk that each client has. The resulting "risk number" allows both the advisor and the client to understand the level of risk being considered while making investment decisions. (Check out the QR code at the end of this chapter to help determine your risk number.)

Financial advisors often liken risk numbers to speed limits—the higher the number, the greater the risk. As clients get closer to retirement, it's not unusual for their risk numbers to shrink as they navigate toward more conservative investments.

To get a sense of your level of comfortable risk, let's take a look at a couple of general examples. Let's say one of your investments loses 14 percent of its value a short time after you buy it due to a market correction. How would you react? Would you want to sell the investment, so you no longer have to worry if it continues to decline? Would you prefer to hold onto it and

wait for the value to recover? Or would you want to buy more shares of that investment because at the now-lower price, it's an even better bargain in your eyes than it was before?

The most important thing about measuring risk and finding out your risk number is the clarity it provides because now we can test that number—or should we say stress-test that number. How that works is putting your plan through a series of tests using historical data of more than a thousand different market scenarios. For example, we would compare how a portfolio might have performed in a bull market like 2013 to how it might have performed in a financial crisis like we saw in 2008, The Great Recession. This can truly provide clarity for a plan, give clients an idea of what kind of risk they are willing to tolerate, and let them see probable success rates of their plan.

A third major worry for folks when it comes to their retirement plan is long-term care (LTC), specifically the high costs associated with it. So, to delve a little further into understanding why this is such a concern for many, let's look at some numbers from Genworth.[3] The national median cost for 2020 for an assisted living facility was $51,600 per year. For a home health aide, it was $54,912 per year. The cost of nursing homes varied based on whether they were private or not but averaged between $93,000 and $106,000 per year. These costs are astronomical and what is even more worrisome is they are increasing an average of 3 to 4 percent each year. No wonder this is a major worry for folks!

When discussing long-term care and exploring how to integrate strategies into your retirement plan to mitigate the potential costs, a realistic question to ask is: How healthy are you and do you have a history of longevity? None of us know exactly

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[3] Genworth. 2020. "Cost of Care Survey." https://www.genworth.com/aging-and-you/finances/cost-of-care.html.

when that day will come, but from a health and family history standpoint, you can glean some clues. Females, on average, live longer than men by about five years. Therefore, looking at a withdrawal rate with the understanding ladies tend to live longer is another factor in any plan. On that note, I'd like to point out that retirement plans can be more important for women, in my opinion, because they're the ones who will more likely suffer the consequences of poor planning. Many men who never bother to create a plan will never find out that it did not work. Of course, when talking about health, you cannot dismiss health care costs later in life, especially with respect to any long-term care. An LTC event can drastically accelerate your withdrawals.

There are products and strategies out there that can help mitigate risks associated with an unexpected LTC event. The two most common methods are self-funding and insurance. If you choose to rely on self-funding, make sure you let your family and financial advisor know which funds to draw from to pay for your expenses.

There are also ways to reduce risk as you invest with long-term goals in mind. They include dollar cost averaging, in which you commit to spending a set amount of money on stocks, bonds, and/or mutual funds on a regular basis. This will result in buying fewer shares of a stock when prices are higher and more shares when the price of the stock drops. Over time, the objective is for the average cost of your shares to be lower than the average price of the individual shares. Because you've committed to consistent investment, you're less vulnerable to emotional decisions driven by swings in the market. Index funds mimic stock indexes such as the S&P 500, charge lower fees than actively managed funds, and thus leave more of your invested money to compound over time.

If you choose to acquire LTC insurance, I often suggest you buy the policy early and apply for the insurance with your spouse or partner. LTC insurance rates are based on age, and most

health insurance companies offer a discount when a policy is purchased with a spouse or partner. Women are more likely to require LTC, because they typically live longer than men. A family history of health conditions that are chronic or debilitating may indicate a greater need for LTC options as well. How much should you pay for a LTC policy? The National Association of Insurance Commissioners reports that some experts advise the premium should not exceed 5 percent of your income.[4] Products and solutions for LTC events can get extremely hairy and are certainly not "one size fits all."

In discussing LTC planning, I would be remiss to not mention the benefits of utilizing a skilled elder law attorney who specializes in this area. If there is a history of chronic illness in the family or a family member is in declining health, a skilled elder law attorney could create an asset protection plan to protect some of the assets from the devastating costs mentioned earlier. There are a number of ways, outside of purchasing insurance, to shelter some of your life savings, preserve a nest egg, and leave a lasting legacy.

The moral of the story, or this chapter at least, is to start planning *now*. I think it is important to get both clear and honest with what you want to do in retirement—not a decade or two from now. I find many of those I sit down with are afraid to spend money in retirement. Worse yet, they are afraid to spend money while they have their best health (remember the go-go years.) A written financial plan lets you know where you stand financially in black and white and how your money works for you.

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[4] National Association of Insurance Commissioners. Feb. 9, 2021. "Long-Term Care Insurance."
https://content.naic.org/cipr_topics/topic_longterm_care_insurance.htm.

Source: Riskalyze, www.riskalyze.com.

Chapter Resource: Risk Number Questionnaire

Pitfall #3: Bad Advice

> *"Everything we hear is an opinion, not a fact. Everything we see is a perspective, not the truth." —Marcus Aurelius*

We see it often these days—people confusing opinions with facts and perspectives with truths. That leads to false images of reality. It helps explain how people who live on opposite sides of the same street can have completely different views of their neighborhood. Reality is extraordinarily complex, and in response, we tend to organize it, forgetting that what we see and know is just a small glimpse of a much wider and greater image.

The Three Myths of Investing

Have you ever thought about the greatest myths that have been propagated throughout society for centuries? Universal myths like, "The world is flat, and you can sail off the edge!" On the surface, this seems like a ridiculous belief, but centuries ago, it was widely held, cropping up in various cultures separated by thousands of miles.

Myths of all shapes and forms continue to exist and spread throughout society to this day. There are still people today who believe the world is flat—the Flat Earth Society group on Facebook has more than 68,000 members! Thankfully, a myth is typically no longer believed by society when contrary scientific evidence is presented.

Most myths cause little to no harm to individuals and society as a whole. I mean, if someone really wants to believe the Earth is flat, then what harm can they really do to society? Unfortunately, this is not the case when it comes to the "Myths of Investing." Belief in these myths can have significant effects

on an investor's peace of mind, and, more importantly, have a negative impact on the success of their individual investment and retirement goals.

I'm not only talking about a goal like accumulating more money or growing your wealth. I'm talking about your important LIFE goals! These are the goals that ultimately really matter when the time arrives to check out of this world. These goals help you achieve a life of abundance and gratitude, rather than scarcity and regret. Let's face it, we all entered this world with no possessions, and we'll leave with no possessions as well. Remember that old saying: "You can't take it with you."

In my opinion, it's all the relationships and experiences we share with our beloved friends and family that matter the most. Goals like spending time with your grandchildren rather than working to make ends meet in retirement, goals like traveling the world and exploring different cultures and what the world has to offer, goals that fulfill core values like freedom, adventure, love, giving, and independence. This is the stuff that matters! Believing the "Myths of Investing" can destroy those dreams.

I first heard of these myths years ago at a training conference in Cincinnati. I give full credit to Mark Matson and his team for some excellent training in identifying these common myths. In reality, I think I always knew the myths were too good to be true, but it was enlightening to hear them debunked for the first time.

What are these investing myths and how can you protect yourself from harm? In short, three basic and common myths of investing are:

Myth #1: Stock Picking—The myth of stock picking is defined as the belief that a person, whether they be an individual investor, stockbroker, hedge fund manager, television guru, or some other so-called expert, can consistently and predictably exercise superior **skill** in stock picking. The idea is that with this superior skill you can increase the returns of your portfolio by picking the best stocks in advance.

Myth #2: Track-Record Investing—The myths of stock picking and track-record investing are close cousins. Combined, these first two myths are also known as the "Myth of Skill."

Track-record investing is simply looking at the past performance of the so-called "market experts" to determine your investment decisions for the future. On the surface, this seems logical. But we all know that past performance of market experts has zero correlation with future performance.

It's hard to miss all the advertisements on social media and internet search engine pages urging you to see what some "expert" who predicted the bursting of the housing bubble or the market collapse in 2008 is predicting next. In the midst of the overload of information now at our fingertips, it's tempting to find that one thing or one person who can help us make sense of it all. That's why the "Myth of Skill" can be so dangerous.

"The Way to Dispel a Myth is to Present Academic Scientific Evidence to the Contrary."

For nine years in a row, actively managed U.S. mutual funds had lower returns than the S&P 500. A fund manager may outperform for a year or two, but after ten years, 85 percent of large-cap funds trailed the S&P index.[5] The results are even worse for managers who try to pick the mid-cap and small-cap stocks.

Why do investors so often use past performance to make their investing decisions? My argument is most investors have never been presented with an alternative on how to make investing decisions. Let's face it: you don't know what you don't know!

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[5] Bob Pisani. CNBC. March 15, 2019. "Active fund managers trail the S&P 500 for the ninth year in a row in triumph for indexing." https://www.cnbc.com/2019/03/15/active-fund-managers-trail-the-sp-500-for-the-ninth-year-in-a-row-in-triumph-for-indexing.html.

I believe if investors were presented with rigorous peer-reviewed academic evidence to the contrary, they would rethink their entire investment philosophy and strategy.

From a simple statistical standpoint, the chance of these market experts beating the respective market index year to year is no greater than that of simply flipping a coin. Heads, you beat the market, and tails, you don't! Does that sound like a good investment strategy? I didn't think so.

Why would you want to own only a few stocks in your portfolio in the first place? Every day, investors choose to take considerably more risk without the advantage of additional return. They do so by inadvertently purchasing individual stocks through actively managed mutual funds instead of diversifying their risk by buying a basket of the stocks available in passive structured asset-class funds. They may even choose a mutual fund with the expectation that the fund is highly diversified only to learn that the fund manager, through an active management strategy, is buying and selling—thus turning over the portfolio at a ratio of 90 percent or more. Turnover, when it comes to investment portfolios means, "the percentage of a mutual fund or other investment vehicle's holdings that have been 'turned over' or replaced with other holdings in a given year." And by the way, high turnover in an actively managed mutual fund usually equates to additional fees.

Convincing the public that they have the ability to pick the best stocks in advance, consistently and predictably, is the key to these so-called-experts' successes and they know it. There is a mountain of peer-reviewed academic evidence about the lack of skill actively managed mutual fund and stock picking experts exhibit. If you take the time to explore all the evidence, it is truly eye-opening!

When the Wall Street gurus, prognosticators, and the talking heads on all the financial TV shows are correct about their

predictions, they attribute their success to genius and skill. In reality, I believe it is simple luck.

My advice to combat these myths is simple and consists of three action steps to take now: Number one, become educated on this viewpoint. I recommend reading Daniel Solin's book, *The Smartest Portfolio You'll Ever Own,* and Mark Matson's book, *Main Street Money.* Number two, work with an investment coach who will take the time to educate you. In this especially important area of your life, you need an advocate—someone in your corner always looking out for your best interests. And number three, as Daniel Solin writes in his book, "Don't confuse luck with skill!"

Myth #3: Market Timing—Have you ever asked your advisor these questions?

- Is now a good time to get in the market?
- Should I wait until after the election to invest my money?
- The market is at an all-time high. Should I get out?

Simply put: if you have ever asked any of these questions, then you are participating in the myth of market timing and probably don't even realize it.

The problem with these questions is that they all require a prediction about the future to be successful. It's just like using a Magic 8 Ball to make some of the most important decisions in your life—investment decisions! These are the same investment decisions that you are relying on to fulfill your biggest retirement dreams and life goals we spoke about earlier in this chapter. Should you ever use a Magic 8 Ball to make investment decisions? My Sources Say No!

The problem with trying to time the market is simple: You must be right TWICE for it to be successful! You not only have to know when to get out of the market at the right time, but you also have to know the right time to jump back in. This is an almost impossible task to achieve consistently over time.

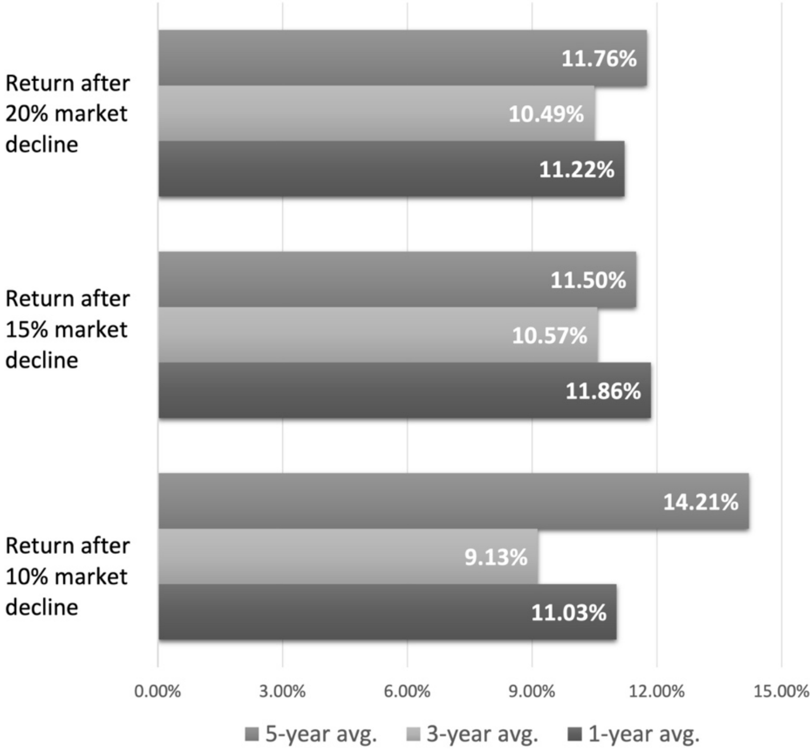
There are many so-called "market experts" who are all too willing to give you a plethora of fancy predictions about the future of the market. They write books, publish articles in magazines, and appear on CNBC, or Fox Business on a daily basis.

These market "pundits" announce they know tomorrow's news … today! Their predictions vary widely, but typically involve telling the audience which way the market is heading over a certain period of time. Don't fall prey to these modern-day snake oil salesmen!

To see a visual representation of the power of staying invested throughout the ups and downs rather than trying to time the market, take a look at the two charts on the following pages. Investors may wonder whether it makes sense to do nothing and stay put during periods of major decline in the market. It's essential that investors put these ups and downs in a larger context. The first chart shows the compound returns of the Total Market Research Index from 1926-2019. AFTER major market declines of 10 percent, 15 percent, and 20 percent, the following one-year, three-year, and five-year returns were all positive, recording average annualized double digit returns for all except the one-year return after a 15 percent decline, which was an impressive average of 9.13 percent.

Fama/French Total U.S. Market Research Index Returns[6]

July 1926-December 2019



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[6] Dimensional. December 2020. "History Shows That Stock Gains Can Add Up After Big Declines." https://my.dimensional.com/dfsmedia/f27f1cc5b9674653938eb84ff8006d8c/33353-source/history-shows-that-stock-gains-can-add-up-after-big-declines.pdf.

Example shown for illustrative purposes only and is not guaranteed. Past performance is no guarantee of future results. Short-term performance results should be considered in connection with longer term performance results. Indices are not available for direct investment. Their performance does not reflect taxes or the expenses associated with the management of an actual portfolio.

What's even more compelling is looking at the cost of trying to time the market. This second chart shows the negative impact of a hypothetical $1,000 investment in 1970 in stocks that make up the S&P 500 index. Missing just a few of the market's best days can be disastrous. For example, if you had stayed invested the entire time, your $1,000 investment would have grown to an impressive $121,353 through March 17, 2020. (This is a fifty-year investment, which is longer than most investors' timelines, but it illustrates my point, nonetheless.) Missing just fifteen of the best days out of fifty-plus years in the market would have dwindled those returns all the way down to $43,472. Wow! Some of you may say, "Well, that's easy, just don't miss out on the best days."

Well, that is market timing in a nutshell. How do you know if tomorrow is going to be one of those best days? The simple answer is, you don't!

Hypothetical Growth of $1,000 Invested in U.S. Stocks in 1970[7]

TOTAL $121,353

Minus the S&P 500's best-performing day
$108,758
(-$12,595)

Minus the 5 best days
$77,056
(-$44,297)

Minus the 15 best days
$43,472
(-$77,881)

Minus the 25 best days
$26,989
(-$94,364)

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[7] Scientiam. March 2020. "The Cost of Trying to Time the Market." https://www.scientiam.com.au/knowledge-base/the-cost-of-trying-to-time-the-market.

Based on the total return of the S&P 500 from January 1, 1970 to March 17, 2020. In U.S. dollars. For illustrative purposes. The missed best day(s) examples assume that the hypothetical portfolio fully divested its holdings at the end of the day before the missed best day(s), held cash for the missed best day(s), and reinvested the entire portfolio in the stocks in the S&P 500 at the end of the missed best day(s). Returns for the missed best day(s) were calculated by substituting actual returns for the missed best day(s) with zero. Performance data for January 1970–August 2008 provided by CRSP; performance data for September 2008–March 17, 2020 provided by Bloomberg. S&P data provided by Standard & Poor's Index Services Group. Investing risks include loss of principal and fluctuating value. There is no guarantee an investment strategy will be successful. This performance does not reflect taxes or the expenses associated with the management of an actual portfolio.

This indisputably powerful evidence destroys the Myth of Market Timing. What should investors do, considering this powerful evidence?

Follow these three action steps below:

1. Focus on the long term and not the current market high or low.
2. Ignore the market pundits. They do not have a crystal ball!
3. Resist the urge to act! Diversification, discipline, and rebalancing should be the only “actions” to consider.

Beware of Bad Advice

Before we move on, I want to revisit this third and final pitfall of investing. I can’t stress enough that bad advice can be devastating to your investment portfolio—and, by extension, your life goals and dreams. If you’re trying to gauge market trends and take advantage of them, you’re literally gambling with at least a portion of your financial future. As I’ve shown earlier, you’re not likely to be any more successful than if you just flipped a coin to determine the outcome. Are you willing to take that big a risk with something you’ve worked your entire life to build? I’m fairly sure you won’t be.

How do you know when you’re getting bad advice? I’ve learned several indicators in my years of experience as a financial advisor.

If you’re using an advisor or a broker who is not a fiduciary, you may want to consider looking for a new advisor who is one. As a reminder, a fiduciary is someone who has a legal obligation to put the client’s interests above and before their own.

If you’re using an advisor or broker who claims to be able to beat the market, they’re basically gambling with your money. Neither you, your broker, nor your advisor is smarter than the collective wisdom of millions of people looking at the available

public information about a stock. The price that is set is likely to be fair.

Don't chase after returns or "trendy" investments of any kind —including gold and Bitcoin.

When faced with two portfolios that have the same expected returns, go with the one with the least amount of risk. After all, this is your money at stake.

PART 2

Three Principles of Developing an Investment Plan

A principle is defined as a fundamental truth or proposition that is characteristic of the subject being described. In a sense, it is universal and true across all dimensions. So, when thinking about money and investing, are there characteristics of money that can be described as universal truths? I certainly think so.

In a perfect world, all of our investments would have three characteristics. Number one: Protection. This would entail a guarantee that the assets were protected from losses, even in a poor market environment. Number two: Growth. This would guarantee some sort of return over time that exceeds inflation. Number three: Liquidity. This would ensure that if you need access to funds at any time, for any amount, you could access them freely and quickly.

Unfortunately, the perfect investment product doesn't exist, and if you see anyone out there touting that you can have a safe, guaranteed growth and fully liquid investment product, then I recommend you turn around and walk away immediately.

What I've found is that you can almost always get two out of three of these characteristics in a good investment product.

However, let's discuss the difference between investment PRODUCTS like stocks, bonds, gold, real estate, mutual funds, and annuities versus having a well-designed investment PLAN. In the next few chapters, we are going to explore each trait in depth and give some examples of which areas of a typical investment/retirement plan include these traits.

I want to take you back a decade or so ago. It was the end of 2008 and the beginning of 2009. A look at the year's headlines read as follows:

"U.S. Loses 533,000 Jobs in Biggest Drop Since 1974," New York Times, December 5, 2008

"Housing Prices in 20 U.S. Cities Fall a Record 18.5%," Bloomberg News, February 24, 2009

"Stocks Fall to Lowest Level Since 1997 as Dow Drops Below 6,800,"USA Today, March 2, 2009

"Job Losses Hint at Vast Remaking of Economy," New York Times, March 6, 2009

"Global Economic Shock Worse Than Great Depression," Huffington Post, May 8, 2009

"Lehman Collapse Sends Shockwaves Around the World," The Times, September 16, 2008

"Mounting Fears Shake World Markets as Banking Giants Rush to Raise Capital," WSJ, September 18, 2008

"Panic Grips Credit Markets," Financial Times, September 18, 2008

"Worst Crisis Since '30s, with No End Yet in Sight," Wall Street Journal, September 18, 2008

"A New Phase in Finance Crisis as Investors Run to Safety," New York Times, September 18, 2008

Do you remember how you felt during that time, which was later dubbed The Great Recession? For a moment, try to put yourself emotionally back there and connect with how you really felt. Those were some scary times. It was very hard to be positive

about America's economic future or the American Dream as we know it. However, we lived through that difficult economic time and went on to grow and prosper as a nation. And if you take just a quick glance at the last hundred years or so of history, you will see that as a country we have had some really bad times like World War I, The Great Depression, World War II, Vietnam War, Watergate, Cuban Missile Crisis, 1987 Market Crash, Gulf War, 9/11 Terrorist Attack, and most recently the Covid-19 pandemic.

The point is the bad times are not here to stay. This too shall pass as proven time and time again. The simple truth is, when it comes to investing, it is exceedingly rare when all the lights are green. There is always something to be uncertain about. With all that being said, it has never been a better time to grow your wealth. Some of you may say "But Jeff, how can you say that? The world has gone absolutely crazy!" To that I say, how did you think people felt back in WWII or during the Cuban Missile crisis when we were on the brink of Nuclear War? Or most recently at the end of 2008 when reputable news outlets were declaring the End of America?

To drive this point home even further, what if you invested $100,000 at the end of 2008 into a low-cost simple S&P 500 index fund? Today, that $100,000 would be worth over $300,000.[8] That's more than three times your original investment. And if you think I'm just picking a great time during the market and using hindsight bias to run numbers and look at headlines; here are some more headlines up to a full decade after the crisis ended:

"Warren Buffett: U.S. Economy In "Shambles" No Signs of Recovery Yet"—CNBC, 2009

"Foreclosures hit record high"—CNNMoney, 2010

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[8] Financial-calculators.com. "Historical Investment Returns Calculator." https://financial-calculators.com/historical-investment-calculator.

"Financial Crisis Spreads Throughout Europe"—NPR, 2010

Fears grow over length of US jobs crisis"—Economic Times, 2010

"U.S. approaches 'fiscal cliff,' and world watches from the sidelines"—The Washington Post, 2012

"Millennials are afraid to invest in the stock market, Ally finds" —CNBC, 2017

"Dow plunges 1,175 -- worst point decline in history" —CNN, 2018

If you blindly followed the media narrative, then you might always be fearful and never think it's a good time to build a plan and invest your money. Don't let the daily negative news immobilize you. Your plan must focus on the big picture, not the headline of the day. Sharp investment advisors do not encourage their clients to make impulsive decisions. Headlines should be mere distractions, not drivers of investment decisions. Knee-jerk reactions fueled by anxiety ignited by headlines can have long-term negative consequences for your portfolio. An effective retirement plan isn't just about putting the right pieces in place, it's having the discipline to stay the course when the financial waters get choppy, and others are jumping ship. Start today and build a retirement plan that incorporates each of the three principles I mentioned above: Protection, growth, and liquidity. Let's explore them in a little more detail.

Principle #1: Protection

The first principle of investing and having a solid retirement plan is to have some element of **protection.** This means that a portion of your overall investing plan is considered guaranteed in the event of a severe market downturn.

There are a couple of elements in a financial plan that could be considered guaranteed. The most obvious one is cash. The first and most basic piece of advice I give to all of my clients, no

matter what age or situation they are in, is to always have three to six months of an "emergency fund" saved in cash. An emergency fund should cover all of your basic living expenses such as food, housing, utilities, health care, and transportation.

Let me be clear, seeing a great deal on a used boat, fancy new patio furniture, or a sports car doesn't qualify as an emergency. I'm talking about you or your spouse or partner losing your job—or the air conditioning unit going out in the middle of summer. More likely, in your retirement phase of life, this could be a health care event or lifestyle changes to accommodate the slow-go years.

I mentioned Dave Ramsey earlier. He often lists three questions to ask yourself when you're considering dipping into your emergency fund. By the way, there's that magic number of three again. His questions are:

1. Is it unexpected?
2. Is it necessary?
3. Is it urgent?

The more you answer "yes" to those questions, the more likely the situation you're in is an emergency and requires you to dip into your fund.

How large should your emergency fund be? It depends mostly on your personal preference, but there are a few things to consider that might help you decide just how much you are comfortable with having saved. For example, if you're part of a two-income household, then a three-month emergency fund is probably sufficient. But if you're a one-income family, you're self-employed, or you earn a straight commission, then an emergency fund able to carry you for a longer period is probably a better idea for you since a job loss could make you unable to pay the bills.

As mentioned previously, if someone in your house has a chronic medical condition that requires frequent visits to the doctor or hospital, then you might want to increase the amount

in your emergency fund. Even if there's room in your monthly budget to pay for the expenses, it's good to be prepared in case a big emergency strikes.

Your emergency fund should be liquid, meaning you keep it in a place where you can get to it easily and quickly. The best option, in my opinion, is a simple checking account or a money market account that comes with check-writing privileges or a debit card. Those would allow you to pay the doctor or mechanic quickly and easily.

How do you best build your emergency fund? First, make a budget and live by it. By doing that, you'll see how much money you have available to put toward your savings goal. Second, set a monthly savings goal. It will take discipline, but you'll be surprised at how quickly you can build that emergency fund by making regular deposits. And third, look for ways to add to your savings efforts. Maybe you're getting a raise or have an opportunity to tighten your budget even more. Every little bit helps and gets you to your goal even faster.

Another place people often look for protection is to insurance companies. Insurance companies offer products called annuities. As with all financial products, there are pros and cons. However, from my experience, annuities seem to have the worst reputation and are often the most misunderstood insurance products on the market.

Annuities: The good, the bad, and the ugly

Annuities can scare people off. Chances are, you or a loved one has gotten locked into an annuity contract that wasn't suited for you or them in the first place. Maybe they lost money, maybe their money was tied up, illiquid, or inaccessible. For whatever reason, they were unhappy with the annuity. It may simply boil down to the fact they were unaware of complex terms that can

get hidden in the fine print of an annuity and can greatly restrict what they could do.

Annuities are not inherently "bad." Annuities are merely a tool to be used as necessary and they have a time and a place for some people—but not all. Unfortunately, annuities are often pushed by insurance agents who are not operating within a fiduciary capacity. They are often pushing a product that is best for themselves and their company—perhaps incentivized by a big commission check—and they might not be selling the product because it is truly what is best for the client and their unique situation.

By the way, a fiduciary holds a legal responsibility to put the interests of clients before their own. I take this responsibility seriously by making recommendations that go beyond what would simply be suitable for my clients' situations and provide guidance based on their best interest.

Let's take a closer look at annuities so you'll know which ones to avoid and which ones to gravitate toward if you're considering adding them to your portfolio.

The Ugly

I'll start with what I consider the "ugly"—variable annuities. Right now, if you are a broker, you are probably thinking to yourself, "Oh great, here's another advisor bashing variable annuities!" Well, you are right! I'm really not a fan of these products. A variable annuity is an insurance contract that guarantees a safe stream of income for the rest of your life. But variable annuities are complex and expensive products that typically make money for only one person: the insurance agent or broker selling them. There can be anywhere between 3 percent and 5 percent in disclosed and hidden fees with commissions on top of that, so they're a cash cow for the seller.

The annuities come with a surrender period, during which the holder would incur a stiff penalty if they withdrew money from

the account. If you fund a variable annuity with after-tax money, all future gains are tax-deferred. They'll be taxed at a higher ordinary income tax rate than capital gains rates under the current tax code. If you fund a variable annuity with tax-deferred dollars, you won't be doing much more than adding a layer of unnecessary fees.

Ah, yes. Let's talk about those fees. I'll never forget the story of Joe. Joe stopped in our office one day and said he would like to set up an appointment to have me review three variable annuities. The total value of all three combined was well over $500,000. These three variable annuities were with a well-known insurance company, which will remain anonymous. When reviewing these, I noticed that the three accounts had not grown very much since the inception of the policies. I asked Joe if he knew how much he was paying in fees and his answer blew me away! He said, "I don't think I pay anything in fees." I then asked him if it was OK if we called the company and have them tell us what the fees are in these policies. He said sure. When we called the company, we got a very nice customer service representative on the other line. She promptly got permission from Joe to discuss his account with me, and I began to ask a few questions. I first asked what was the mortality and expense fee on the account? Commonly referred as the M&E fee. The rep told me it was 1.25 percent. I then said I noticed an income rider was attached to this policy and asked how much the rider cost. The rep said that was another 1.25 percent. She said there was also an administrative fee of .25 percent. If you're keeping a total, we are now up to 2.75 percent, but we are not done. I asked, what are the sub-account fees? She said that they average 1 percent. I then asked her if she knew what the turnover ratio was on those sub-account mutual funds. She did not know, so we had to look up those up ourselves. Some of the funds had close to 100 percent turnover, which means the entire portfolio was being sold and replaced once a year by the active

manager of those mutual funds. This adds a tremendous amount of hidden fees—let's say at least an additional 0.25 to 0.50 percent. So, the grand total of all fees was estimated to be at least 4 percent per year. Joe thought he wasn't paying anything in fees, and it turns out he was paying more than $20,000 per year and didn't even know it! This means the accounts had to earn at least 4 percent per year just to break even. No wonder I didn't see much growth in his accounts.

A closer look by Forbes some years ago showed fees are typically very high—at least 2 percent a year and as mentioned earlier I have seen them as high as 5 percent. Most stock mutual funds (outside of the variable annuity blanket) have much lower rates than that. Investment options with variable annuities usually are limited and often have high underlying expense ratios and turnover ratios. Your money is commonly invested in sub-accounts comprised of these active mutual funds, which are professionally managed funds that can invest in stocks, bonds, money market instruments, or a combination of the three. These "active" managers are often trading or turning over the portfolio holdings at very high percentages per year. Hence the definition of active. Every time an active manager makes a trade there is a cost involved and that cost is paid by the investor. By the way, remember our explanation earlier about the three myths of investing? Most of these active mutual fund managers are participating and perpetuating these myths.

Don't be fooled, either, by the word "insurance" when it comes to variable annuities. That term in variable annuities typically means you'll receive at least the amount of money you initially invested into the annuity if you die (i.e., the death benefit). If your death is sudden, Forbes says,[9] you (well, maybe not you if you're dead) get the value of your account if you

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[9] Eve Kaplan. Forbes. July 2, 2012. "9 Reasons You Need To Avoid Variable Annuities." https://www.forbes.com/sites/feeonlyplanner/2012/07/02/9-reasons-you-need-to-avoid-variable-annuities/?sh=5c61b825f195.

haven't yet annuitized. However, I have reviewed many of these products where the death benefit is the actual account value, even if the account value has eroded away through market loss and fees over the years.

To top it all off, annuities are disadvantageous if they don't go to a spouse. If the money invested was after-tax dollars, Forbes[10] says, the heir receives no step-up in basis on accounts with gains. If you were to invest the same after-tax dollars in a stock fund, your heirs would benefit from a step-up in basis at the date of death or six months later under current tax law. A step-up in basis is a powerful tool to reduce capital gains taxes.

The primary advantage to using annuities, experts say,[11] is to defer taxable income in the future. But you don't have to use the high fee "variable" kind to capture this benefit. The use of a variable annuity is typically limited to investors that have already maxed out their 401(k) for the year as well as their Roth IRA contributions.[12]

It can take several years for the benefits of tax deferral to offset the higher costs and the way an annuity converts tax-advantaged long-term capital gains into ordinary income. Market corrections have made some insurers vulnerable to credit downgrades, so check an institution's financial history and standing before deciding to invest in a variable annuity.

An agent or broker may argue that a variable annuity is pretty much like an IRA. Indeed, both are essentially tax-sheltered shells that house investment funds. But annuities have higher fees and expenses than an IRA and they're classified as an asset.

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[10] Ibid.

[11] Ken Nuss. Kiplinger. Dec. 11, 2019. "When Used Correctly, Deferred Annuities Deliver Powerful Tax Advantages." https://www.kiplinger.com/article/retirement/t003-c032-s014-deferred-annuities-can-deliver-major-tax-advantage.html.

[12] Daniel Kurt. Investopedia. Dec. 11, 2020. "Variable Annuities: A Good Retirement Investment?" https://www.investopedia.com/articles/personal-finance/090915/variable-annuities-good-retirement-investment.asp.

An IRA is an account that holds retirement assets. Buying and holding a variable annuity within an IRA makes the tax advantages of the annuity redundant but doesn't offset the variable annuity's high fees and lack of liquidity.

As you can see, there are plenty of reasons to be wary of variable annuities. Particularly with the advent of exchange-traded funds in recent years, there are better ways to reduce the tax impact on your investments.

The Bad

Next, we'll look at forms of annuities I don't often recommend, but—full disclaimer—*they can* be useful and even necessary tools in some situations.

Immediate annuities—in which payouts must begin within a year—can prove useful in various scenarios. Those include providing an immediate pension for those who may not have been provided with a defined benefit plan through work, making a bequest to an individual privately when there are concerns about their ability to handle funds, and managing the investment of a trust when the surviving spouse is not the parent of the remaining beneficiaries of the trust.

But immediate annuities also have drawbacks, the most significant being that they're irrevocable. Once you have made your payment to launch the annuity, you no longer have control or access to that money. This means those funds will not be available for emergencies or other uses.

There's also a chance your annuity payments may not keep pace with inflation, so talk to your financial advisor about an inflation adjustment feature if you're considering single premium immediate annuities.

Fixed annuities are insurance contracts that pay a guaranteed rate of interest on the investor's contributions. They can be turned into immediate annuities by "annuitizing" the annuity. Because a fixed annuity is a tax-qualified vehicle, its earnings

grow and compound tax-deferred. Annuity owners are taxed only when they take money from the account, whether it's through occasional withdrawals or as regular income.

Once a fixed annuity is annuitized, it is then irrevocable and will generate a guaranteed income payout for a specified period or the life of the person owning the annuity.

Just like with immediate annuities, however, there's a risk that inflation may outstrip the rate of return. There are typically high fees and a surrender charge if more than 10 percent of the annuity is withdrawn. Annuity owners under fifty-nine-and-one-half may have to pay a 10 percent tax penalty along with income taxes on money taken out of the annuity.

The Good

A fixed index annuity earns interest that is linked to a stock market index—such as Nasdaq, NYSE or the S&P 500—without actually being invested in the market. A fixed index annuity's growth is subject to floors and caps, so it won't rise or fall outside of specified return levels regardless of how much the stock indices fluctuate.

To put it simply, the insurance company issuing the fixed index annuity bears the risk if there's a sharp stock market decline. Investors can't lose any of their principal with a fixed index annuity due to market loss. In return, potential interest credits are capped—usually somewhere between 3 percent and 9 percent. If the market soars, the insurance company reaps the benefits above the cap.

Earnings within an annuity contract are tax-deferred, meaning you don't pay income taxes on them until you withdraw gains from your account. This also means annuity earnings do not offset Social Security benefits. Earnings from bonds, CDs, and other investments do offset Social Security benefits.

Many fixed index annuities offer the ability to provide a guaranteed source of income for family members in case the

original owner is no longer there to provide for them. That flexibility helps clients tailor estate plans to their specific needs. An example might be allowing the option of surviving spouses receiving income for the remainder of their lives.

Fixed index annuities allow owners to specify a beneficiary, which means clients may be able to pass on a portion of their wealth without having to go through the probate process. Probate can delay heirs from receiving assets for several months. On top of that, it's expensive. Between court costs and attorney and appraisal fees, probate can cost as much as 5 percent of the value of an estate.

With many popular retirement investments, such as certificates of deposit, you pay taxes on the earnings each year. With annuities, you don't owe a penny in taxes until you withdraw the funds. That gives owners some control over when they pay taxes. Leaving money in a deferred annuity can also reduce your Social Security taxes since you'll have less taxable income when you delay withdrawals.

Perhaps the most attractive feature of an annuity is it generally provides income you can't outlive. Remember those surveys we've mentioned in which people said they feared outliving their money more than they feared death itself? Many fixed index annuities offer this option without making the irrevocable decision of annuitizing. Many of these products have income riders that allow lifetime income while still maintaining access and liquidity to the funds. Some companies offer these riders at no charge, unlike the variable annuity counterparts we discussed earlier.

Traditional investments can't guarantee lifelong income, unless one's nest egg is particularly large. For those with more modest means, an annuity ensures you'll have something to supplement Social Security, even if you live to be quite old.

If the index falls, your account stays the same. Your principal is guaranteed, even if the index linked to your annuity loses

value. This protection is one of the strongest appeals of a fixed index annuity. However, you must read the terms carefully because the insurance companies can adjust the caps and participation rates of the index.

Your potential interest credits are calculated and credited every year on the policy anniversary. Once they're credited, they can't be taken away by negative market performance.

A fixed index annuity offers an element of the protection we've discussed earlier in this chapter. It also provides an opportunity for growth, which can protect against inflation.

Like other annuities, however, it lacks liquidity during the length of the surrender penalty period (usually ten years or so)—though some contracts can offer a degree of liquidity like penalty free withdrawals of up to 10 percent per year. There are steep penalties, too, if you withdraw money within the surrender period or if you remove money before you turn fifty-nine-and-one-half.

Protection is paramount! Consideration for the many investment and retirement plans and vehicles can leave one's head spinning. But keep this in mind: protection is arguably one of the most important principles of any retirement plan.

Principle #2: Growth

In George S. Clason's famous book titled, *The Richest Man in Babylon*, the first law of gold is "gold cometh gladly and an increase in quantity to any man who will put by not less than one-tenth of his earnings to create an estate for his future and that of his family."

The second principle of investment planning is growth. However, there is no point in talking about growth unless you have something to grow. It is no accident that the first law of gold is to save 10 percent of everything you make. We have all

heard the old financial adage, *pay yourself first,* which is as true today as it was 4,000 years ago in fictitious Babylon.

In Clason's book, the second law of gold is "gold laboreth diligently and contentedly for the wise owner who finds for it profitable employment, multiplying even as the flocks of the field." So following this law, it is not enough just to accumulate massive sums of money. We must grow it through proper management. The other laws all deal with seeking guidance from those experienced in handling money. Investing is a profession and should not be taken lightly.

Most importantly when growing your wealth, patience and time must be employed to work for you, not against you. Realize that time is your ally, not your enemy. I think the best way to demonstrate the concept of time being on your side is to take a look at the story of twin sisters, Mary and Isabelle. They both just graduated from college at the age of twenty-one and landed their first jobs at the same company. Mary decides to participate in the company's 401(k) plan and through salary deferral and a 3 percent company match, she saves $5,000 per year. She saves this amount every year for the next ten years until she reaches age thirty-one and then stops. Isabelle thought about doing the same but decided her lifestyle couldn't support the savings and thought she would just make up the difference later in life. So, Isabelle saved nothing for ten years but then decided it was time to start, and invested the same amount of $5,000 for the next 20 years from end of age thirty-one to age fifty-one. So the question is, who did better? Is it Mary, who started early and invested half as much, or Isabelle, who started late? Let's assume a modest rate of return of 6 percent per year for each portfolio.

As you can see from the table on the next page, Mary, who started earlier, is far better off than Isabelle. In fact, Mary's portfolio is $237,487.34 compared to Isabelle's total amount of $194,963.63 at the age of fifty-one. Remember, Isabelle started later but she contributed twice as much as Mary!

Hypothetical example for illustrative purposes only and does not represent any specific product or investment. Values do not reflect investment fees or taxes, which would reduce the figures shown here.

Mary's investment	6%/year growth EOY	Age	Isabelle's investment	6%/year growth EOY
$5,000	$5,300.00	21	$0	
$5,000	$10,918.00	22	$0	
$5,000	$16,873.08	23	$0	
$5,000	$23,185.46	24	$0	
$5,000	$29,876.59	25	$0	
$5,000	$36,969.19	26	$0	
$5,000	$44,487.34	27	$0	
$5,000	$52,456.58	28	$0	
$5,000	$60,903.97	29	$0	
$5,000	$69,858.21	30	$0	
$0	$74,049.71	31	$0	
$0	$78,492.69	32	$5,000	$5,300.00
$0	$83,202.25	33	$5,000	$10,918.00
$0	$88,194.38	34	$5,000	$16,873.08
$0	$93,486.05	35	$5,000	$23,185.46
$0	$99,095.21	36	$5,000	$29,876.59
$0	$105,040.92	37	$5,000	$36,969.19
$0	$111,343.38	38	$5,000	$44,487.34
$0	$118,023.98	39	$5,000	$52,456.58
$0	$125,105.42	40	$5,000	$60,903.97
$0	$132,611.75	41	$5,000	$69,858.21
$0	$140,568.45	42	$5,000	$79,349.71
$0	$149,002.56	43	$5,000	$89,410.69
$0	$157,942.71	44	$5,000	$100,075.33
$0	$167,419.27	45	$5,000	$111,379.85
$0	$177,464.43	46	$5,000	$123,362.64
$0	$188,112.30	47	$5,000	$136,064.40
$0	$199,399.03	48	$5,000	$149,528.26
$0	$211,362.98	49	$5,000	$163,799.96
$0	$224,044.75	50	$5,000	$178,927.96
$0	$237,487.44	51	$5,000	$194,963.63

Total invested: $50,000

Total invested: $100,000

So, with all that in mind, growth consists of positive returns that at least keep up with and, ideally, exceed inflation. Unless it exceeds the rate of inflation, your increased balance will actually have less buying power. As I mentioned earlier, growth always comes with some level of risk but not growing your money comes with risk too. That risk is called inflation risk and it is a hidden cost that slowly creeps up on us all.

Inflation is commonly described as too many dollars chasing too few goods. The most popular measure of inflation is the CPI index. In general, inflation reduces the purchasing power of your income over time. See below for CPI Chart of inflation over a 25-year period beginning in 1996.[13]

Furthermore, when people think about growing their wealth, they commonly think of the bond and stock markets. There is no guarantee of returns with a stock/bond portfolio, nor is there any guarantee that you won't lose money. History has demonstrated that stocks have generally outperformed inflation, but there is no assurance of this and it takes patience and discipline to achieve results.

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[13] Trading Economics. July 2021. "United States Inflation Rate." https://tradingeconomics.com/united-states/inflation-cpi.

The benefit of using a portion of one's overall plan allocated toward a portfolio of stocks and bonds is you can potentially increase your expected rate of return overall, hence the possibility of achieving growth! For the folks who lean toward more risk, they may allocate more to this area.

Let's think back to our three characteristics of investments mentioned in the previous chapter (i.e., growth, liquidity, and protection). A stock-based portfolio generally has the characteristics of growth opportunity and liquidity. So, keeping in mind we generally realize just two out of three desired elements, we must sacrifice something. In this case, we give up a degree of protection. How much we give up really depends on the individual's risk tolerance. Some folks can handle a lot of risk and sleep soundly at night, while others can only handle very little if any risk at all. Again, I can't emphasize enough how important it is to identify and maintain your personal risk tolerance.

Since the majority of growth in any retirement plan comes from a stock market-based market portfolio, let's discuss the key rules to follow when investing in the market. I tell my clients all the time that there are three rules of investing. There's that number three again.

Sometimes in life, the rules to be successful at something are quite simple, but they're not always easy to follow. For example, one of the hardest things to do for a lot of us is to lose weight. When it comes right down to it, there are only two rules to losing weight. You exercise more and eat less or healthier. As you can see, the rules are quite simple. However, following those simple rules can be difficult at times. After a long, hard day at work, there's nothing I like better than plopping myself on the couch, turning on the game, and eating a large pizza all by myself. Trust me, I've done it. Although I know it's a terrible idea and bad for my health, I make the excuse that I deserve it because I worked so hard that day. As a matter of fact, human beings often do

things that are inherently bad for them and they know better, but we choose to do them anyway because it feels good at the time. Our emotional brain, in that split second of indecision, overrides our cognitive/logical brain.

The weight loss industry generated a record $78 billion in 2019.[14] If the rules are so simple—eat less, move more—how come the weight loss is a $78 billion industry? Here's why: The rules can be very difficult to follow.

Back to principle two of investment planning, part of my job as a financial advisor is to also be a full-time investment coach. One of my most significant duties is to show folks how to follow these rules and stay disciplined with them, because it's so easy to get off track. I'm going to talk about each rule in detail and offer specific examples of investors' behavior, including how they break some of these rules. I'll also share information about designing a portfolio where you may be able to follow these rules a little easier and possibly achieve more peace of mind. Now, how can you get started and build an efficient portfolio?

Rule #1: Own a portion of your portfolio in equities.

I'm not talking about having 100 percent of your money locked up in equities, which are stocks of corporations or companies. Very few people can handle the risk of 100 percent of their portfolio being exposed to the stock market. I don't really know anyone already retired or getting ready to retire who can handle that level of risk. So, what would be a good mix? Again, that depends on the individual's risk tolerance.

Knowing and accepting your level of risk tolerance is key, because there's volatility in the stock market. You must understand and accept that. When we have a market downturn—and we will, because markets don't go up forever—

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[14] Yahoo. March 26, 2021. "U.S. Weight Loss & Diect Control Market Report 2021." https://www.yahoo.com/now/u-weight-loss-diet-control-092000673.html.

you can't panic with your money and break one of the rules of investing. Similarly, when the market surges and you're tempted to jump on the latest "hot" stock, you must maintain your discipline and not make decisions based on emotion.

Your age and timeframe for the use of the money will factor into how much volatility you can tolerate, too. You can't put everybody into the same mix or the same portfolio. But generally, as you get older, and you need to live on that money for income, you need to decrease your risk a bit. You can't have a market plunge wipe out a big chunk of your portfolio right when you're ready to draw down on the money for retirement. So, age does have something to do with it. Let's say we have a market downturn like we had in 2008. How much risk can you handle? Most people don't know the answer to that question, because they don't know how much risk they're taking right now in their portfolio.

To settle on a good mix, I recommend sitting down with an advisor and recognizing your values and goals. We'll help you out with this in the next section when we talk about "your true purpose." Once you determine your values and goals, you can design a portfolio.

I want to take a bit of a detour here and talk about gold as an investment. Trust me, diversification is extremely important in your portfolio. We preach it all the time and we'll get into more detail in the next section. But I am frequently asked if gold is good for my clients' portfolios.

We constantly see television commercials hawking gold during the news or on Fox Business and CNBC. What they're basically doing is fear-based selling. I must admit, this really irks me! I'll never forget when I received a call from a client in the middle of the day on a Wednesday. Unbeknownst to me, it was a three-way call with an agent from one of the popular gold companies you hear about on the commercials all the time. My client says, "Jeff, I have an agent on the other line from so-and-

so gold company and they would like me to invest my entire IRA in gold coins. I told them you were my investment advisor and I would have to run it by you first. Would you please speak with him?" I was, of course, caught a bit off guard, but I said, "Sure, I would love to talk with him!" I proceeded to ask the gentleman on what basis he recommended my client to move her entire IRA over to gold coins. The response was typical. "The United States currency is in deep trouble. The government is constantly printing money. The country is several trillions of dollars in debt. Gold is your only safe haven!" the representative spouted. I then asked him the following question: "If you are going to sell her your precious gold coins, what will you be receiving in return? In other words, what are you taking in return for selling her the gold coins?" This really threw him for a loop! He suddenly realized he was backed right into a corner. Do you see? The only answer was that he was taking her IRA funds, which are in U.S. dollars, in exchange for his precious gold coins. This made absolutely no sense because he had just finished telling me the U.S. currency was going to be worthless.

In my opinion, diversifying your portfolio with the physical commodity is not a good idea. It may make sense to own stock in companies that participate in precious metals such as gold mining companies, silver mining companies, national retail outlets, etc. for diversification purposes, but not the actual metal. Why do I believe this? Because when you own a company, you could potentially make a return in two ways. The company could pay you a dividend as an owner of the company, but you could also have share price appreciation which probably tracks the physical price of the commodity as well. If you only own the physical ccommodity, you will have to buy gold at a low price and then have the wherewithal to sell that gold at a higher price. Therefore, you receive a capital gain. In reality, this is extremely difficult to do. As humans, we always think the price could go higher. Therefore we may hold on too long. Or if the price drops

suddenly, we are afraid the price could go even lower, prompting us to sell too early. This is a risky and difficult game to play!

Gold is often sold as an inflation hedge. The truth is, it's absolutely a terrible inflation hedge. The way it's pitched is this: the U.S. government is printing money, it's going to devalue our dollar, so put your money in actual physical metal gold. But let's look at some numbers.

When we're talking about returns of a portfolio, we always have to say past performance is no indication of future results. But we're still going to go into the past—the distant past. All the way to 1929. From there, we'll look at performance through the end of 2012. This is eighty-three years of data.

Let's start with a portfolio of 70 percent represented by S&P 500 stocks and 30 percent represented by long-term government bonds (fixed income). Basically, let's design it to capture the market rate of return of those asset classes and then compare those returns to gold over the same time period. Let's say you had $100,000 back in 1970 and you're ready to invest it. You had a choice between investing that money in gold or investing that money in a diversified portfolio of 70 percent equities and 30 percent fixed income. What would be the value of those portfolios at the end of 2020?

That $100,000 in a diversified portfolio of 70 percent equities and 30 percent fixed income would have grown to almost $18 million by the end of 2020 (minus any taxes or investment fees along the way). Keep in mind, we're talking about fifty years of growth. That same $100,000 invested in gold would have grown to a little over $5 million.[15] Which would you rather have? Almost $18 million or $5 million?

When you consider that gold is sold as a hedge against inflation—that it's a "safe" investment—the data doesn't

[15] Financial-calculators.com. "Historical Investment Returns Calculator." https://financial-calculators.com/historical-investment-calculator.

support that claim. As a matter of fact, if we measure risk over that same time period, gold has an annualized standard deviation of 19.19[16] compared to the lower standard deviation of the portfolio of 15.08. Gold as an investment has more risk and less potential return.

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[16] Peter Lazaroff. Aug. 19, 2021. "Want to Invest in Gold? Here's What You Should Know First." https://peterlazaroff.com/should-you-invest-in-gold/.

Rates of Return on $100,000 Investment[17]

Jan. 1, 1970-Dec. 31, 2020

	Annualized return	**Cumulative return**	**Annualized standard deviation**
70/30 mix	10.71%	$17,859,250	15.08
Gold spot price	8.12%	$5,272,870	19.19

How about taking those comparisons further? How about one-month Treasury bills or the consumer price index, which is a measure of inflation?

Here are the numbers: $100,000 invested in one-month T-bills, going back to 1970, would have grown to $894,000 through 2020.[18] Remember the diversified portfolio earned almost $18 million. You can see which one obviously did better. The Consumer Price Index, based on the $100,000 invested in 1970,

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[17] Source: Custom charts created using Dimensional Fund Advisors software. Source: Standard and Poors Index Services Group S&P 500 returns from Jan. 1, 1970 to Dec. 31, 2020 and Long Term Government Bonds Index Morningstar from Jan. 1, 1970 to Dec. 31, 2020.

The results in these charts represent back-tested historical performance of the indexes. Inherent limitations of back-tested performance are discussed in endnotes. The graph is provided for illustrative purposes only and no representation is made that you would achieve similar results. Index performance returns do not reflect any management fees, transaction costs or expenses. In addition, the index is unmanaged and not available for direct investment; therefore, its performance does not reflect the expenses associated with the management of an actual portfolio. Performance results and comparative indices assume reinvestment of dividends and income. Equity factors are provided by Fama/French. Even a long-term investment approach cannot guarantee a profit. Economic, market, political, and issuer-specific conditions and events will cause the value of equity securities, and the investment strategies that owns them, to rise or fall. Stock markets tend to move in cycles, with periods of rising prices and periods of falling prices. Past performance is no guarantee of future result.

[18] Financial-calculators.com. "Historical Investment Returns Calculator." https://financial-calculators.com/historical-investment-calculator.

would have been worth over $700,000 today. In other words, what $100,000 would have bought you in 1970 would cost you $700,000 in 2021.[19]

Which of those is the better inflation hedge? Obviously, a portfolio of 70 percent equities and 30 percent fixed income, spread across all asset classes. I'll delve deeper into those asset classes when I get to Rule #2. Yet, this is why we don't put all of our eggs in one basket or go too conservative with CDs and T-bills. On the other hand, we're not going to the other extreme, which is too much in equities. This leads us to Rule #2.

Rule #2: Diversification

It's a buzzword that gets thrown around quite a bit in the financial services industry, yet few investors know what true diversification means. I'm going to go as far as to say few *advisors* know what true diversification means. In my experience, not many really know how to measure whether a portfolio is diversified or not.

We get clients that, when you meet with them for the first time, believe they are well diversified. When we take an in-depth look, we often discover they have about twenty different things their money is tied up in. They have stocks, they have mutual funds, they have money markets, they have commodities—you name it. In their mind, they believe that's what diversification is. But it's not.

All too often, they've never had their portfolio analyzed to see where their money is. Maybe their money is all in one asset class. They might have five or six different mutual funds, but those mutual fund managers who are picking and trading the stocks, as well as the client, may not realize how much of their money is in the same asset class. When we do a portfolio MRI for folks,

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[19] CPI Inflation Calculator. 2021. "Value of $100,000 from 1970 to 2021." https://www.in2013dollars.com/us/inflation/1970?amount=100000.

we'll examine and break down their portfolio to understand exactly where their money is—how much money, for example, is in the U.S. large growth stock asset class, which is really the S&P 500? It's quite common to see people with 90 percent to 95 percent in one asset class in their portfolio. In 2008, the S&P 500 lost 38 percent. To the extent that market goes down, and all their eggs are in one basket, they're going to suffer significant losses. There's nothing else in their portfolio to protect them.

What are asset classes? Essentially, what I'm talking about is owning the market. Your goal as an investor should be to capture the market rate of return, not try to beat the market. We know from statistics it's impossible to beat the market consistently and predictably.

Dalbar is an independent research firm that conducts substantial studies on consumer behavior. One of their studies explored the market rate of return for the S&P 500 over the past thirty years. From 1990 to 2020, the average investor earned about 5 percent annual growth in their accounts. That's about half the average growth rate of the S&P 500 in the same time frame.[20] That 4 or 5 percent difference can have a dramatic impact on your portfolio. Imagine earning 4 percent more per year on average, and not through stock picking, market timing, or track record investing. It's a big difference. Our goal is to capture the market rate of return. Very few investors do.

How should you diversify your portfolio? The first step is education. It's important to understand what an asset class is and how you can purchase an entire asset class. I have mentioned "owning the market." Here are some examples:

U.S. Microcap stocks are small companies in the United States. I'm not talking about penny stocks. I'm talking about small companies. If you went out and bought every single

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[20] Catherine Brock. The Motley Fool. July 22, 2021. "4 Secrets to Beating the Average Investor." https://www.fool.com/investing/2021/07/22/4-secrets-to-beating-the-average-investor/.

Microcap stock in the category and held onto it from 1927 through 2020—that's roughly 3,000 stocks, if you are wondering—the average rate of return is 11.98 percent per year. You didn't have to pick stocks. You didn't have to time the market. You didn't have to speculate. You didn't have to gamble. None of that was involved in earning that rate of return of almost 12 percent per year on Microcaps. All you had to do was own all 3,000 Microcap companies.

Obviously, for the average investor to go out and buy 3,000 companies in one asset class is a logistical nightmare. It's impossible for an investor to do that on their own. But there are "structured funds" available that do this for you. What they're doing is identifying an asset class and then buying every stock within that asset class. That helps you build a portfolio without speculating, without gambling, and still own the asset class. Don't try to find the needle in the haystack … just own the whole haystack.

There are plenty of people who will pick and choose companies they love. In reality, they're taking on more risk, not less. They're only going to pick three, four, or five companies out of that asset class. I say you're much safer owning stock in the whole asset class. You don't get the benefit of an additional return by owning two, three, or four companies because the expected rate of return is the same as if you own all the stocks in that asset class. When you own them all, you diversify your risk away from the impact if something happens to that one company. Maybe the chief financial officer embezzles money and runs off to Brazil, causing the stock price to plummet. Think of a company that goes out of business because of faulty accounting measures. To protect against that, you want to spread your risk across all companies. If you only own five, and two of those companies go bankrupt, you just lost a lot of money. But if you own 3,000 and two companies go bankrupt, you're more protected.

By the way, "the market" is not just the DOW or the S&P 500 that the popular financial news media reports on and obsesses about on a daily basis. There are other asset categories as well. Let's look at how they performed.

I already mentioned Microcaps, but what about "value"? Small and large value asset categories have had some noteworthy returns when we examine all the data. Small value companies—the key word there is "value"—went up 13.13 percent from 1927 to 2020. Large value companies went up 11.12 percent over that same period.[21] To clarify, these are average annual returns. On another note, the growth over those ninety-three years would blow your mind! A sum of $10,000 invested in small cap value stocks in 1927 would be worth just over $1 billion. That's right … one billion dollars! Now, again, this is a very long period of time, and no one would reasonably hold an investment this long, but this gives us a way to benchmark these asset classes.

Average Annual Returns on Investments

June 1, 1927-Dec. 31, 2020

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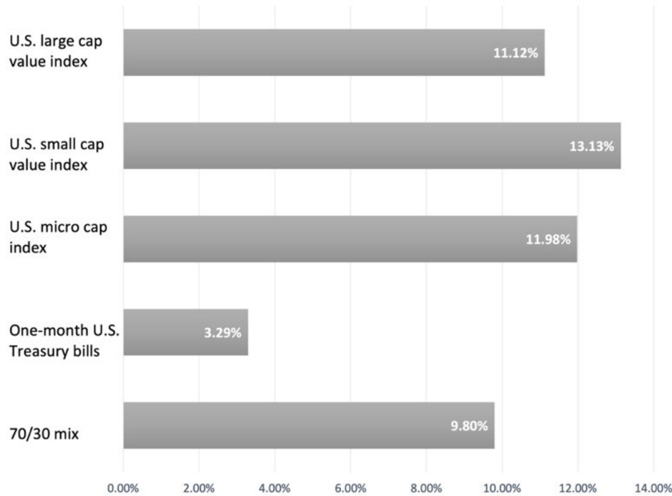
[21] Source: Custom charts created using Dimensional Fund Advisors software. Source: CRSP data provided by the Center for Research in Security Prices, University of Chicago.

The results in these charts represent back-tested historical performance of the indexes. Inherent limitations of back-tested performance are discussed in endnotes. The graph is provided for illustrative purposes only and no representation is made that you would achieve similar results. Index performance returns do not reflect any management fees, transaction costs or expenses. In addition, the index is unmanaged and not available for direct investment; therefore, its performance does not reflect the expenses associated with the management of an actual portfolio. Performance results and comparative indices assume reinvestment of dividends and income. Equity factors are provided by Fama/French. Even a long-term investment approach cannot guarantee a profit. Economic, market, political, and issuer-specific conditions and events will cause the value of equity securities, and the investment strategies that owns them, to rise or fall. Stock markets tend to move in cycles, with periods of rising prices and periods of falling prices. Past performance is no guarantee of future result.



The data for international small companies doesn't go back as far, but the rate of return was still 14.48 percent between 1975 and 2020. For international large companies, the return was 10.91 percent since 1975.[22]

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[22] Source: Custom charts created using Dimensional Fund Advisors software. Source: CRSP data provided by the Center for Research in Security Prices, University of Chicago.

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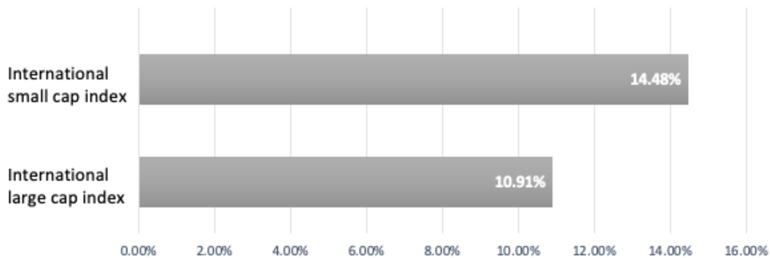
Average Annual Returns on Investments

Jan. 1, 1975-Dec. 31, 2020



It's always important to remind yourself that past performance is no indication of future results. But capturing these market rates of return involved no stock picking, no market timing, no track-record investing. You're just building your portfolio by owning the market. It clearly shows the importance of diversification. And while diversification doesn't ensure success or that you can't lose money, it's an important tool in the investment toolbox to help limit your losses.

Rule #3: Rebalance and Stay Disciplined

Once you build this successful, diversified portfolio, you're not done. You must rebalance to manage your risk. You're not rebalancing because you're predicting the future of the market—say, energy stocks are going to go way up this year and healthcare stocks are going to go way down. None of that is involved. What you're doing is ensuring you're not overexposed in your investments. When you first set up your portfolio, you identified what level of risk you're willing to take. As we maintain your portfolio over time, we have to keep your risk preference on target.

It can be dangerous if you don't regularly rebalance your portfolio. How often you rebalance depends on what the market has done over time. That could be quarterly, every six months,

or perhaps just once a year. But it's important to look at. What we do with our clients is look at their portfolios on a quarterly basis. We don't necessarily rebalance them every quarter, though. It depends on how each of the individual asset classes have performed over the previous quarter and if they are within acceptable tolerances. Let's say you had a portfolio in 1973 of 50 percent equities and 50 percent fixed income, and you didn't touch it. You stayed disciplined and left it alone. But you also never rebalanced that same portfolio. Because stocks have gained more than fixed income over that time, the allocation to stocks is far greater. Today, that same portfolio would have roughly 87 percent equities and 13 percent fixed income. This means it would contain much, much higher risk. If there's a sudden market downturn and you have no idea your portfolio is riskier than it was when you first set it up, then you can end up with a significant loss. You could compound that by making an emotional decision in response—a bad decision, perhaps, by running to cash and locking in those losses. That's why it's important to rebalance regularly to help manage your risk.

Let's look at 2008 as an example. The market suffered a severe downturn. People tuned into the news and heard the market was dead, the economy was dead. It sounded like Armageddon. That's just what the media was promoting: Fear mongering. People looked at their statements and saw they lost a lot of money. For many, that led to an emotion-based decision. They were already feeling bad about losing money. When they watch or read the news, they feel even worse, which reinforces their decision. What do they do? They want to run to so-called "safe money" investments. They want to put all their money in U.S. Treasuries or, even worse than that, cash.

Here's where discipline—or the lack of it—comes in. How many rules did they break in 2008? Remember the three rules of investing: Own equities, stay diversified, and rebalance with discipline. At the end of 2008, how many rules did most investors

break? That would be all of them. Many broke all three. They no longer owned equities because they bailed out of the market. They're no longer diversified, because they don't own equities, which means they can't diversify across all asset classes. As a further consequence, they're obviously not rebalancing—which is buying low and selling high. In fact, they're doing the exact opposite. They're selling low and then buying high because they'll jump back in when the market starts to go back up.

That is a prime example of breaking the rules of investing, which often leads to additional performance losses. Then that cycle repeats itself. This is why it's important to have a good coach to keep you on track and to keep you focused on these three rules of investing.

Principle #3: Income

> *"As in all successful ventures, the foundation of a good retirement is planning." —Earl Nightingale*

The hardest thing for most folks when it comes time to retire is this: they will no longer be receiving that paycheck every week or two. That security blanket is gone. They're left with the unsettling question, "Where is the income going to come from?" This question is arguably the primary reason for creating a retirement plan. It's why folks like me have a job!

When retirees are wondering about their income, their first thoughts will turn to what assets they can access in a timely and efficient manner—their liquidity. How will they pay their bills and support their lifestyle now that they're retired?

I like to refer to what I call **The 3-Legged Retirement Income Stool**. Those three legs are:

1. Social Security
2. Pensions
3. Retirement Savings: IRAs, 401(k), 403(b), etc.

Social Security

Social Security is a retirement staple, and also a hot topic, because it applies to almost everyone and the rules are numerous, confusing, and ever-changing. Any discussions about cuts to Social Security strike fear in the hearts of many Americans, and here's why: Social Security provides the majority of income to most elderly Americans. For about half of the nation's senior citizens, it provides at least 50 percent of their income.[23] For one in five seniors, it provides 90 percent of their income.[24] That's right: 90 percent. That's how important these Social Security payments are to many people.

And let's face it: Social Security is one of the largest financial decisions that you'll ever make regarding when to take it. If you live to the age of eighty-five or beyond, you could be drawing quite a bit of money out of the Social Security system over a twenty-plus year period. This is why it's a crucial financial decision that should not be taken lightly.

One of the first recipients of Social Security is a perfect example of how significant it can be.

Franklin Delano Roosevelt signed Social Security into law on August 14, 1935. But the federal government did not start collecting payroll taxes on workers until January of 1937—nearly two years after it was signed into law. Those who started collecting Social Security back in the late 1930s had a choice: They could choose a lump sum payment or a monthly benefit check.

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[23] Social Security Association. 2021. "Fact Sheet: Social Security." https://www.ssa.gov/news/press/factsheets/basicfact-alt.pdf.

[24] Ibid.

The first person to ever receive a Social Security payment was a gentleman named Ernie Ackerman.[25] He chose to take the lump sum payment. Ernie had paid a whopping five cents into the Social Security system at that time and later received a lump sum payment of seventeen cents. That doesn’t sound like much, but in truth he more than tripled his money!

The first monthly Social Security check was issued to Mrs. Ida May Fuller of Ludlow, Vermont.[26] She paid a total of $24.75 into the Social Security system. Her very first check was $22.54. By the time she received her second monthly check, she had already received more out of the Social Security system than she put in. Keep in mind, the average life expectancy in the 1930s was about fifty-eight for men and sixty-two for women—and the new law only allowed people to start collecting Social Security at sixty-five. That meant a lot of people would end up paying into Social Security without ever collecting any in return. Good old Ida May lived until she was a hundred. If you do the math, that means she collected a total of $23,000 in Social Security, for a total return of 92,000 percent.

Not surprisingly, a number like that causes some alarm and raises a question: How sustainable is this Social Security system that we live under? Will Social Security be there for you when you're ready to take it?

There's not a day goes by I don't read an article about the Social Security system. We often get calls from our clients about something that they've read, or they saw on social media, or they heard on the news about Social Security. The number one myth we hear about in our office is this: Social Security is going broke.

There's no doubt that Social Security is facing some funding challenges, but bankruptcy is not one of them. My guess is this

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[25] Social Security Association. 2021. “Historical Background and Development of Social Security.” https://www.ssa.gov/history/briefhistory3.html.

[26] Ibid.

rumor started in the media back in 2012, when the Social Security Administration put out a statement. The media went wild with it, and they didn't give the full story. The statement announced that the projected point at which the combined trust funds will be exhausted would be in 2033, or three years sooner than what had been projected just a year before. At that time, there will be sufficient non-interest income coming in to pay about 75 percent of the benefits.

That sounds confusing, doesn't it? The media didn't pay much attention to the part of the statement saying there will be sufficient non-interest income to pay 75 percent of the benefits. Non-interest income simply means payroll taxes from the workers. If changes aren't made by 2033, Social Security recipients will start receiving 25 percent less than what they would normally get. Without changes, there is enough coming in from payroll taxes to keep the system sustainable all the way until 2080. So, as you can see, Social Security is not going bankrupt.

But 25 percent is a substantial reduction, so you can expect fixes to be made. We've already seen a few: They pushed the retirement age for people who were born after 1960 to sixty-seven. If you were born in 1954, your full retirement age was sixty-six. For every year after that until 1960, you added two months to your retirement age. Congress may, at some point, push the full retirement age to seventy.

The bottom line is, there are going to have to be some fixes in the system. The math demands it. Back in 1935, there were forty-two workers to every one retiree.[27] The earliest age you could even start collecting Social Security was sixty-five. As I cited earlier, the average life expectancy in the 1930s was the

[27] University of Vermont. 2001. "Quick Facts on Social Security." http://www.uvm.edu/~dguber/POLS21/articles/quick_facts_on_social_security.htm.

upper fifties for men and low sixties for women.[28] In the early years of the program, the average length of time to actually collect Social Security was roughly two years. That was it.

The picture looks dramatically different today. According to the Social Security Administration's website, ssa.gov, there are 2.8 workers to every retiree. The ratio has dropped from forty-two to one in Social Security's early days to less than three to one.[29] The earliest filing age today is sixty-two. People are collecting Social Security earlier than they ever have.

What else is the reality today? Our life expectancies are substantially higher. On average, folks who are collecting benefits at sixty-two could keep collecting until they're age eighty-five. That's more than twenty years or ten times the average time to collect in the 1930s.[30] Octogenarians, those who are eighty years of age or older, are the fastest-growing segment of our population. Thanks to this simple math, people question the sustainability of the Social Security system we live under.

Social Security was originally just a retirement program. That changed in 1939, when they added survivor benefits. Now, if you are married and one person in the couple passes away, the general rule is that the surviving spouse will be "stepped up" to get the higher of the two benefit payments. In addition, a child could qualify for some type of survivor benefits. In 1956, the SSA added disability payments. If you become disabled, and you qualify for Social Security, then you can qualify for Social Security Disability. To qualify for Social Security, you must have worked forty quarters, or ten years of employment.

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[28] Social Security Association. 2021. "Life Expectancy for Social Security." https://www.ssa.gov/history/lifeexpect.html.

[29] Social Security Association. 2021. "Ratio of Covered Workers to Beneficiaries." https://www.ssa.gov/history/ratios.html.

[30] Social Security Association. 2021. "Historical Background And Development Of Social Security." https://www.ssa.gov/history/briefhistory3.html.

You may be wondering how much you'll be receiving in Social Security distributions after you retire. And it may dawn on you that it's been a while since you received a statement from the Social Security Administration. It's not just your imagination, either. It was costing the Social Security Administration over $70 million a year to mail those statements. In response, they decided to only mail those statements occasionally. Typically, you'll now get them on milestone birthdays—forty-five, fifty, fifty-five, sixty, and sixty-five. In the meantime, what if you want to check out your estimate? The best way is to go to the Social Security Administration website at www.ssa.gov. Yes, I know a government website, right? But I've got to tell you: it's a really good website. I was extremely impressed with the amount of information and the number of planning calculators you can play around with and get a good idea of your estimates. When you go to the website, click on My Social Security, so you can create an account. I must caution you, however: Please be careful when you answer the security questions on the website, because they are a little bit tricky. It's going to test your memory. It's going to ask you really obscure things like who held your mortgage on your home back in 1992—things that really test your memory. If you get a certain security question wrong, guess what? You're locked out for twenty-four hours. You cannot try to sign up or register for your Social Security account until the next day. So be very careful when you answer those questions.

Your personal Social Security statement alone provides a wealth of information. The first page tells you how much you or your family would receive in disability, survivor, or retirement benefits. It also includes a record of your lifetime earnings. I think that's really cool. You can go back years and years ago and get the answer for, "Hey, what exactly did I make in 1984?" For me, that was my second year of high school. I made $1,714 back in 1984.

People often ask how these estimates are calculated, as well as what you need to do to qualify for Social Security. On Page 2 of your Social Security statement, you'll see a section that explains how your benefits are estimated. As I mentioned earlier, you typically need forty quarters of employment history, which is about ten years of earnings estimates to qualify for Social Security benefits. But your benefits are calculated on the highest thirty-two years of earnings. They actually index those earnings for inflation, then average and apply their formula to the highest thirty-five years of earnings.

We will often have a client who is deciding whether to retire and start collecting Social Security or continue working. Often, it makes sense to continue working, because that's going to drop off one of those lower earning years from early in their working life—or from a period when they were laid off and had to accept a lower-paying job in the short term.

What happens if you don't have thirty-five years of working history? For each year short of thirty-five, a zero will be reflected on your earning record. Even if you have a part-time job, those earnings will exceed a zero. These are some of the factors to consider when you are thinking about when to start taking Social Security.

As I mentioned earlier, you can start receiving Social Security as early as age sixty-two. You may choose to do that for a variety of reasons. One may be that you need it to help pay your bills. Some people do it because their family history suggests a shorter life expectancy than others. Keep in mind, however, that those who do start drawing on Social Security early will see the basic amount permanently reduced—perhaps 25 to 30 percent.

Earnings restrictions could also come into play. If you start collecting Social Security early, prior to your full retirement age, and you're also working, there are earnings restrictions. Once you earn more than specified amounts, they will reduce your Social Security payments $1 for every $2 you’re over the

maximum annual earnings allowed. There's a myth that money lost in those reductions is gone forever, but that's not true. It's repaid to you on a prorated basis once you reach your full retirement age—but the lower base rate set when you began receiving Social Security stays the same.

One way Congress may attempt to extend the solvency of Social Security is to change the amount of money you can earn before having your monthly benefits reduced. Another may be to change how often cost-of-living adjustments are made to benefits. The easiest—and most likely—step is to raise payroll taxes. This means you'll take home a bit less from each paycheck in exchange for potentially receiving more later in Social Security benefits.

I've mentioned the impact of what can happen if you choose to start receiving Social Security earlier than your full retirement age. It's also possible to delay receiving the benefits as late as the age of seventy. That results in an increase in payments amounting to about 8 percent a year. If, for example, you have a $1,000 monthly benefit at your full retirement age, and you delay that one year, your monthly benefit check would be $1,080. If you delay it two years, it would be $1,160. The longer you wait, the more you get those 8 percent credits—again, up to the age of seventy. After that, the credits stop, so it makes no sense to delay receiving Social Security past the age of seventy.

Looking at all these numbers, you have three basic decisions: You can retire early—as early as sixty-two; at your full retirement age (FRA) when you would receive 100 percent of your retirement benefit; or after your FRA, when you can earn delayed retirement credits all the way up to age seventy. Keep in mind, you can start taking Social Security at any time between sixty-two and seventy. You're not limited to those three ages. The Social Security Administration will calculate your benefit based on the age when you decide to take it.

There are many permutations to when the best time is to start taking Social Security, especially if you're married. Let's say your spouse qualifies for a Social Security benefit, because they have a great working history based on the highest thirty-five years of earnings—not the last thirty-five, the highest thirty-five. So often, one spouse does not qualify for benefits, perhaps because they were a homemaker and do not qualify for their own benefits. In that case, it may make sense for the spouse who does qualify for benefits to delay receiving Social Security if they don't need it for basic needs. That way, if something happens to the person who receives the benefits, the spouse will receive a survivor benefit of that higher amount.

The age difference is important if a higher-earning spouse is older, too. Let's say the higher earning spouse is five to ten years older and does not have longevity in their family history. It may make sense to delay the higher-earning spouse's Social Security to earn those delayed retirement credits I mentioned earlier, because when that one spouse passes away, the surviving spouse will get that much more in a survivor benefit. Again, that's if the Social Security isn't needed to take care of basic expenses.

If you're single, it's an easier decision. It'll come down to your basic needs and your expected longevity. What's your family history? For good or bad, few people know when that final day will come. But if your basic needs are met with all your other sources of income—maybe you have a great pension, maybe you saved properly during your working years and you have a great retirement account—you don't have to rely on Social Security. You don't need the money right away.

There's a break-even amount out there in terms of how much you've paid in and how much you'll be drawing out. If you have longevity in terms of life expectancy, you may decide to wait all the way to seventy to collect. We have the Social Security planning software that shows, depending on when you started

collecting benefits, that break-even point is somewhere between ages seventy-eight and eighty-two.

If you have longevity in your family, and you think you're going to live longer than, say, eighty-two, and you don’t need the money, it may make sense to delay starting benefits until you’re seventy. In this example, after age eighty-two, you will have collected more money out of Social Security by waiting until age seventy than starting at age sixty-two, even though you started eight years earlier.

These hypothetical scenarios highlight some of the factors to consider when pondering the best time to start receiving your Social Security benefits. I would advise meeting with your financial advisor to sort through the various options to see what works best for you.

Pensions

Pensions are the second leg of the retirement income stool. Like Social Security, they provide a monthly income upon your retirement. Unlike a 401(k), the employer bears all of the risk and responsibility for funding the plan. The amount of your pension is typically based on your years of service, level of compensation and your age at retirement. Typically, an employee has to work at a company for a specified number of years before becoming “vested” in the pension plan. That will vary from company to company.

Not all companies offer pensions. In fact, the concept of the traditional pension is becoming less and less common. Company-sponsored pension plans are essentially being phased out in modern-day corporate America.

That’s a shame because pensions help provide something everyone wants during retirement: peace of mind. As your retirement journey unfolds before you, there are risks that can come along and rob you of your peace of mind when it comes to guaranteed income. For example:

- Longevity— that you may outlive your income.
- Excess Withdrawal Risk—that you take out too much and deplete your assets too quickly.
- Markets and Miscalculation Risk—that you don't invest wisely and calculate your returns and what you need to do in the future poorly.

Most of these risks were mitigated by a traditional pension plan. So now that pensions are not an option for most folks, how can you mitigate those risks?

One tool that can be part of an overall plan and serve as an effective alternative for the guaranteed income of a traditional pension is an annuity. As I mentioned earlier, fixed index annuities in particular earn interest tied to a market index—such as Nasdaq, Dow Jones, or the S&P500—rather than a fixed interest rate. A fixed index annuity's growth is subject to floors and caps set by the issuing company, so it won't rise or fall outside of specified return levels, no matter how much the markets fluctuate.

Interest earnings within an annuity contract are tax-deferred, meaning you don't pay income taxes on them until you withdraw them in retirement. It also means annuity earnings do not offset Social Security benefits. In contrast, earnings from bonds, CDs, and other investments do offset Social Security benefits.

Perhaps the most attractive feature of an annuity is it generally provides income you can't outlive. In addition, many fixed index annuities can provide a guaranteed source of funds for family members in case the original owner is no longer there to provide for them. If a traditional pension is not an option for you, consult with your financial advisor about effective alternatives for your retirement plan.

Retirement Savings Accounts

This is where most folks have the bulk of their retirement plan assets. Since this is typically the largest asset within one's

retirement plan, one could argue it's the most important. Therefore, building an efficient portfolio and allocating this money into that vehicle is arguably the most important part of planning. We'll discuss more on what it means and how to build an efficient portfolio later, when I discuss the Markowitz Efficient Frontier.

In the past, it was pretty common that someone would get a job and stay there for the rest of their career—hopefully rising through the ranks over time and getting the raises and other perks that come with the new responsibilities. There might be a watch or a plaque or some other acknowledgement of that longevity along the way, too.

But those days are gone. It's far more common for someone to work for multiple employers over the course of their working years. This means they could also have contributed to multiple employer-sponsored plans. One of the easiest things to do is to consolidate these accounts, or roll them over, into a single IRA. Sometimes this simple act can lift a huge weight off someone's shoulders. It's utterly amazing to see that being organized, knowing what you have, and where it is, can be a real relief! There's also the added benefit of compound interest on the higher consolidated amount.

One question I've been asked often in my career is this: "If an individual needs income, where should they draw from first? A 401(k)? A Roth IRA? Social Security?" That's a bit of a loaded question because the answer depends on several factors: age, employment status, personal financial situation, how much is in each account, marital status, and more.

Let's use an example of a sixty-two-year-old, married retiree who has a 401(k) that has yet to be rolled over into an IRA. This retiree also has a Roth. If this person is no longer working and needs the money as income, it may make sense to start Social Security early. If their sole income is just Social Security and it's

enough to pay for general living expenses, the Social Security will have zero tax.

Let's say this person wants to draw from other taxable accounts, such as a 401(k) or a traditional IRA, in addition to collecting Social Security. When money is withdrawn from these accounts, it could possibly incur ordinary income taxes. If the withdrawal is below the standard deduction, it may not incur income taxes. However, withdrawals from these taxable accounts could potentially trigger taxes on the Social Security being collected! You have to be careful about withdrawing from these accounts in combination with collecting Social Security.

Roth IRAs have different rules, which we previously discussed. Let's assume you have had the Roth for at least five years, and you are over fifty-nine-and-one-half. Any money that comes out of the Roth that is a qualified distribution is tax-free. As a bonus, it is not counted as provisional income (which determines if Social Security is taxed). Therefore, this might be a good option depending on the situation, and an individual might want to take money out of each account.

When you contribute to a Roth, the money has already been taxed. As a result, if you are over fifty-nine-and-one-half, even if the Roth hasn't been open for five years, you can always take out that original contribution without penalty. What you do have to be careful about is withdrawing the growth and earnings of your account. We usually don't have to worry about this, however, because when money is withdrawn from a Roth, all custodians distribute your contributions first, not the interest earned.

The Three-Legged Retirement Income stool is a foundation of our planning for folks at our firm. Because once folks retire, the most basic thing they need to plan for is how to maintain their lifestyle during retirement. And that means figuring out how to create a "paycheck" to pay for basic living expenses, at the very least.

So, to recap, when planning for your retirement, ensure you focus on these **3 principles: Protection, Growth, and Income.** By putting these three principles as the foundation of your plan, you are setting yourself for a better chance of a successful, stress-free retirement.

PART 3

The Three Pillars of a Successful Retirement Plan

Pillar #1: What is Your True Purpose for Money?

This question may seem to have an obvious answer: to pay for the things you want and need. But I believe there is a deeper reasoning behind money and what it can mean for you in your life. Your true purpose for money is so much more than answering the questions of how much you need and how much you want in retirement.

Without even knowing the answers to those questions, I can tell you this much: money can't buy you happiness. Studies have shown this.

Forbes quoted a study done by Illinois State University, where they looked at folks who won the lottery.[31] They measured their happiness compared to folks who didn't win the lottery and discovered those who won the lottery were no happier than

[31] Susan Adams. Forbes. Nov. 28, 2012. "Why Winning Powerball Won't Make You Happy." https://www.forbes.com/sites/susanadams/2012/11/28/why-winning-powerball-wont-make-you-happy/?sh=4d6a7d76593a.

people who didn't win. We've all heard the stories where people who won the lottery eventually went broke and had to rejoin the working world. They spent their winnings on frivolous items such as cars, boats, houses, and jewelry. We've seen similar stories with professional athletes who sign huge contracts and are broke before they know it.

How does this happen? They buy one big-ticket item after another, chasing happiness and fulfillment. When those don't come, they buy something else. Then something else. Before they know it, the money is gone.

What we really need to do is identify what makes us happy. A lot of times, when we're looking at our core values, we express what's most important to us through the financial decisions that we make. When our financial decisions are in alignment with those values, we feel a sense of fulfillment, a sense of purpose and peace of mind. If those financial decisions are not in alignment with our core values, then we're probably going to feel uncertainty, anxiety, and stress about things—and follow one bad decision with another in attempt to make up for it.

The circle of wealth is an enigma. We spend a great deal of our lives working, trying to capture wealth and grow our assets. Because those kinds of things don't really make us happy, we need to understand something of an alignment equation. That equation starts out with a question, an underlying current of fear, a general uncertainty about survival: "Are we going to make it? Are we going to outlive our money?"

That's a valid concern. It's what we call "survivorship stress." Once we have our basic needs—food and shelter—fulfilled, we move on to "human wants." We're all good at obtaining what we want. Napoleon Hill has an interesting quote on this. He says, "What the human mind can conceive and believe, it will achieve." How often have we seen that happen? We'll go out and obtain what we really want to get. We're really good at this.

If we put our mind to something and we want it bad enough, usually we can find a way to get it.

Once we get it, there might be a sense of exuberance, relief, joy and excitement. Yet that's usually fleeting. Want an example? Think cars.

Most of you might say, "At one point in my life, I really wanted a new car." You went out and purchased that car. You were driving down the road, you're thinking, "Yeah, I've actually made it now." But then a month or two passes—maybe even a year—and you find yourself thinking, "It's kind of cool, but maybe there's something better out there." After all, car companies come out with a new model every year. You're sitting at the traffic light, you look over to your right and there's a brand-new model of the same car that you have, except with new features. You start saying, "Wait a second. Maybe what I have isn't quite good enough. Maybe I need that new model."

We can apply this mindset—or mind "trap," in reality—to a lot of things. Apple comes out with cellphones every year with some type of new design or new feature. You may have a brand-new cellphone, but if you're not careful, the cycle begins again. The latest version may have features yours doesn't, leaving you feeling like your phone isn't good enough. Anxiety and stress may kick in, and you break down and get the newest phone. How many examples of this are in your life?

A common one for me is golf. Every year, TaylorMade comes out with a new driver. A few years ago, I bought the TaylorMade M2 driver. Guess what? They not only have an M3 out, but they also have the M4, M5, M6, and now the SIM. I don't know if it's going to get me any more yardage. If I hit the ball five more yards, I'll probably be five more yards into the woods.

I'd like you to write down a few examples of where you might be doing this in your life, and then reflect on whether it's something you want to keep doing.

This same cycle happens in investing. Pretty much everyone experiences this at some point—maybe multiple points—in their investing career. They felt some type of survivorship stress: “Am I going to have enough money to live on when I retire?” We really don't have to go too far back to look at this. Remember 2008, when the markets were dropping? I'm sure a lot of folks out there felt stress after the dot com bubble collapsed in the early 2000s. Feeling that stress is completely normal for investors.

In the circle of investing, we start to look around and we say, “Maybe I should look at this investment.” Perhaps you got an email promising 20 percent returns. Typically, as we search for information, we pay attention to track records. We’ll look at a three-year track record or five-year track record of an investment manager. Maybe they’re running a mutual fund that's quite common, and we’ll say, “Okay, that's the best thing to do. Let me have some of that.” We'll use that track record to determine what investment to choose. We've all read it in the prospectus, that past performance is no indication of future results. But as human beings, that's what people tend to do.

You get that mutual fund and maybe you do really well. Maybe you have a year like 2017 where your portfolio was up 10, 15, 20 percent. But then your neighbor comes by and says “Hey, I made 30 percent. How did you do last year?” Suddenly, you feel inadequate.

Maybe you grab a magazine in the checkout line at the grocery store and there's a mutual fund manager on the cover—or, even worse, a hedge fund manager—saying they made 50 percent or 100 percent. You start to believe, “Maybe what I have is not good enough.” Then we feel that stress again. We end up with no fulfillment, no peace of mind, and no journey toward that peace of mind.

It’s important to break out of this cycle and understand how we can create happiness. One way to do that is to remember times in your life when your behavior was not in line with your

core values. What are your core values? Are they health? Security? Faith? Family? Take some time to reconnect with those values and then reflect on times your behaviors strayed from those values.

You might have developed a pattern of eating junk food even though health is important to you. Perhaps you skipped going to church on Sundays even though you have a strong faith. Perhaps keeping to a strict budget is important to you and you ran up some credit card debt on unnecessary purchases. These are the kinds of departures from your core values that I talked about earlier. How did those changes make you feel? You probably lost some peace of mind and a sense of fulfillment that comes with living a life aligned with your core values.

If you're not sure what your core values are, take some time to make a list of what matters to you most. It may be family or health or faith or security or any number of other values closest to your heart. Your core values belong to you. Going forward, let your decisions be shaped by how they integrate with your core values. You'll feel a sense of satisfaction and fulfillment as you do this because your choices support what matters most to you.

A good way to make progress on this journey is to set goals that help you attain what you want out of life. Maybe you want to travel extensively or make sure your spouse and children are well taken care of in the event of your death or you want to leave a lasting legacy—whether to future generations or via philanthropic ventures.

In the famous Charles Dickens story, *A Christmas Carol*, Ebenezer Scrooge was visited by the ghost of Jacob Marley, his business partner.

"You're going to be visited by three ghosts: past, present, and future," Marley told him.

The future ghost took Scrooge to a graveyard, where he found himself staring at his own grave. Shaken, Scrooge began to think about and ask questions.

The first question has come to be known as the Dickens question: “If I were at the end of my life, what would have to happen to say I lived a life without regret?” In other words, what would I want to have done in my life? How would you answer that question? What would you want to be able to say?

What you should shoot for are extremely specific goals—an object or an end that you strive to attain. This is your destination. This is what we want to really strive for in our life.

You can set these goals whether you’re retired or still in the workforce. Some examples might be financial security for your family, volunteering or helping with charities, or overseas travel when I can be mobile and enjoy it. They could even be as simple as exercising three times a week and eating a keto style diet.

Once you’ve set your goals, I recommend associating some value words with each goal. When we're talking about values, we're talking about the principles or standards held or accepted by an individual. They reveal the actual legacy you want to leave behind. If the goal was our destination, the value is our motivation. It's the “why” in why we want to achieve that goal.

For example, one of my goals was to eventually live the winters in a warmer climate. Don’t get me wrong, I love where I live currently. It’s a great resort style town on the eastern shore of Maryland, on the water. I love it the most in the summertime. I love it all the way through holidays. But maybe, come the heart of winter, I’d like to live somewhere in a warmer climate. That’s the goal. That’s the destination. Why do I want to do that? For me, living in a warmer climate during the winter provides me a sense of health. It's a more active lifestyle. You're not sitting in the house all day on a cold winter day. You’re out and about. It's a sense of freedom, a sense of adventure.

I’d like you to write down two or three values for each goal you’ve established. They could be security, respect, peace of mind, generosity, freedom, happiness, or health. Or they might

be values such as honor, beauty, love, recognition, fulfillment, creativity, abundance, or dignity.

I love a quote from Roy Disney: “It's not hard to make decisions when you know what your values are.”

When you take a look at the values you’ve attached to your goals, which ones show up the most often? For me, it was love, fulfillment, health, fun, and freedom. I recommend you choose three that personify the value stated and really express you as a person the best.

Next, I want you to choose the single most important value and put a star next to it. Select the one value word that is really your innermost core value. Say it out loud. This is your “true purpose.” Knowing your true purpose can help center your investment philosophy, because you’ll have a clear idea of your goals and how to attain them.

We have a saying in our office: It’s not about the money, it's about your life. Money can be fuel for the journey of what's most important to us in our lives.

You may have figured out what is most important to you—what your core values are and how they will shape your investment decisions. That’s good, because those values will shape your investment philosophy. But how will you go about implementing that philosophy? If it’s merely gathering dust on a shelf somewhere, it is of little value to you.

This is where a sound investment strategy, developed with the assistance of your financial advisor, helps provide clarity and direction. It’s not just a convenience, it’s a necessity.

Pillar #2: Have a Sound Investment Philosphy

Three Truths of Investing

Truth #1: Free Markets Work

Hardly a day goes by without some self-proclaimed expert making lofty, and sometimes outrageous, predictions in the media about where the markets are heading and what you should do to protect your portfolio.

Have you noticed their forecasts frequently include dire warnings of Armageddon in the markets? There’s a reason they do it. That's what makes headlines, gets them on those news shows and ultimately sells their services. Typically, these folks work in the active management industry as analysts, portfolio managers, CEOs, or some other position in which they're paid to hunt for hot stocks and bonds. They need you to need them. I'm here to argue that you don't.

I'm a proponent of evidence-based investing—and the evidence is compelling that investors are more successful when they ignore actively managed funds and invest in a diversified portfolio with an appropriate asset allocation. There's no hype, no speculating, and no gambling necessary. Research by some heavy hitters backs me up.

They include Dr. Eugene Fama, who won the Nobel Memorial Prize in Economic Sciences in 2013. Fama first wrote about the efficient-market hypothesis in 1965. That was decades before the internet and a twenty-four-hour news cycle, yet already it was believed that securities markets were extremely efficient in reflecting news as it spread and incorporating that information into stock prices.

Of course, information now goes public in many ways: television, social media, web news, email and, yes, old-fashioned word of mouth. But the outcome is pretty much the same: With the exact same information, some market participants will buy a particular stock, while others will decide to sell. If they come to an agreement on a price, a trade takes place.

However, that's not all that goes into the pricing of a stock, which then translates into the pricing of the market as a whole. What about an individual's plans and circumstances? Aunt

Betty's car blows a gasket, so she sells some stocks to pay the mechanic. Newlyweds Jack and Barb cash out their investment portfolio to help with the purchase of their first home. Down the street, Bob just got a huge promotion, which means he has a lot more money to invest and buy stocks. Meanwhile, Sally just turned seventy-two and must start taking required minimum distributions from her IRA.

These highly personal wants and needs are all factored into stock market prices. We also have to talk about the production and consumption of goods and services. For example, let's say you go on vacation and forget to pack your underwear, so you run to the local chain store to buy a few pairs. You just made an unplanned transaction and, in so doing, contributed to that chain's market value. If that underwear was made in Malaysia, you also contributed to that manufacturing sector. That simple transaction had an impact across the globe. Now multiply that by billions of transactions each day.

There are more than 7.5 billion people on this planet. All with their own hopes, dreams, and needs. All contributing to the global markets. All reacting to information that is readily available. That's why the market is so amazing. It is truly an efficient system that can manage all this information and effectively price it in less than a second. The billions of individual transactions going on every day on both sides of the market—buying and selling—quickly and accurately reflect the price and the current information at that exact moment in time. Is mispricing possible? Yes, a stock could be mispriced at a single moment in time. But the market will quickly and accurately correct that mispricing—so quickly that it would be almost impossible to benefit from a mispriced stock.

How can anyone know, with some semblance of accuracy, the hearts and minds of 7.5 billion people and how they will affect the day-to-day or month-to-month price of individual stocks and the market as a whole?

A simple Google search turns up hundreds of articles on the active versus passive investing debate. Most will tell you active management fails to beat the benchmark index roughly 80 percent of the time. According to the SPIVA U.S. Scorecard, over the ten-year period ending Dec. 31, 2020, 78 percent of large-cap managers, 67 percent of mid-cap managers, and 71 percent of small-cap managers produced results lower than their respective benchmarks.[32]

Of course, those statistics mean some managers do beat their benchmarks. But here's the problem: It's not always the same managers year after year. Thus, we're back to speculation and gambling and trying to predict the future—this time trying to predict which manager is going to outperform a particular index. What a waste of time and energy!

What should you do instead?

Believe in the markets over the long term. It's impossible to predict the performance of an individual stock or the market as a whole. But you can trust in the efficiency of the market as prices reflect all known information.

Diversify across many asset classes. Diversification is your friend. Resist the temptation to put all or most of your money into one or two hot stocks or sectors.

Stay disciplined and rebalance. Don't let emotions dictate your stock market moves. Keep your portfolio on track as you work toward your goals.

Remember, no one can predict the future, and listening to short-term or alarmist forecasts may not make you a successful investor over the long term. As the markets do what they do—moving up, down and sideways—stick to a plan that's designed to help meet your personal needs.

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[32] Gaurav Sinha and Berlinda Liu. S&P Global. Sept. 21, 2021. “SPIVA U.S. Mid-Year 2021.” https://www.spglobal.com/spdji/en/spiva/article/spiva-us.

Truth #2: The Modern Portfolio Theory

This theory earned the Nobel Prize in Economics in 1990 for the collaborative work of Harry Markowitz, Merton Miller and Myron Scholes. The theory addressed how investors averse to risk can construct portfolios to maximize expected return based on a given level of market risk.

- The risk of an individual asset is far less important than the contribution the asset makes to the portfolio's risk as a whole.
- For the same amount of risk, diversification can increase returns.
- The mechanism to reduce risk is dissimilar price movements. Therefore, the task is to find assets with low correlations.
- The Efficient Frontier allows individuals to maximize expected returns for any level of volatility.

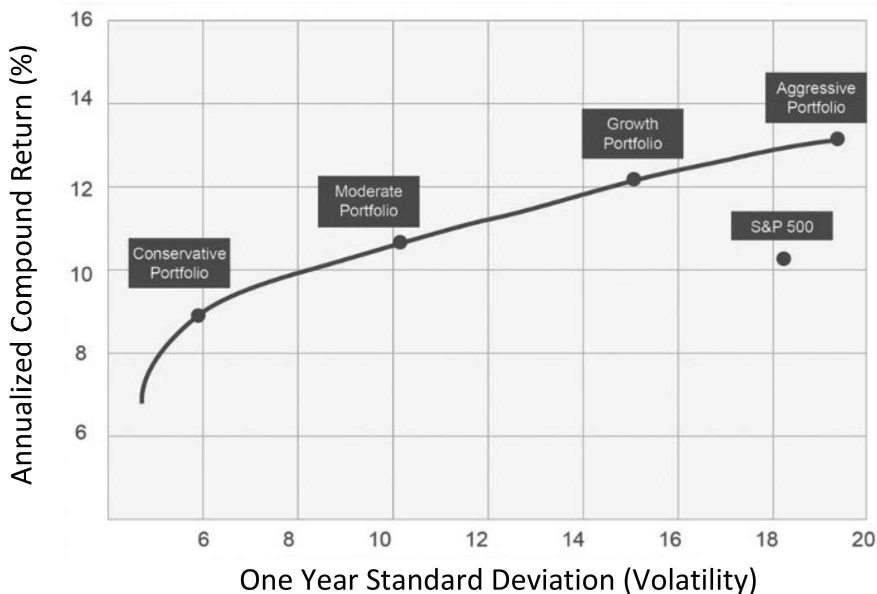
Modern Portfolio Theory also states that, given a desired level of expected return, an investor can construct a portfolio with the lowest possible risk. The theory has long been a useful tool for investors who want to build diversified portfolios. The growth of exchange-traded funds in recent years has made the Modern Portfolio Theory even more relevant by giving investors easier access to a variety of asset classes.

Modern Portfolio Theory allows investors to construct more efficient portfolios. Every possible combination of assets that exists can be plotted on a graph, with the portfolio's risk on the X-axis and the expected return on the Y-axis. This plot reveals the most desirable portfolios.

Let's take a look at how that works.

Markowitz Efficient Frontier[33]

Maximizing potential returns for any level of volatility



By plotting your existing investment information using annualized compound return and annual standard deviation, you can find out the risk and the rate of return of your current portfolio. With this baseline information, you can see how utilizing asset class investing strategies can be used to either decrease risk or increase returns in your portfolio.

The "efficient frontier" is the set of optimal portfolios that offer the highest expected return for a defined level of risk or the lowest risk for a given level of expected return. Portfolios below the efficient frontier are less than optimal because they do not provide enough return for the level of risk. Portfolios that cluster

[33] *For illustrative purposes only. This graph shows 21 years of back-tested market performance from 1993-2013 and assumes reinvestment of dividends, but does not deduct taxes, fees and expenses, and does not reflect actual performance of any portfolio. No representation is made that your portfolio will achieve similar results. Past performance is no guarantee of future success.*

to the right of the efficient frontier are also less than optimal because they have a higher level of risk for the defined rate of return.

Truth #3: The 3-Factor Model

There are three independent dimensions of equity returns, and it is possible to apply these factors to measure the role of each factor in returns. The three factors are:

1. Market Factor: the extra risk of stocks over fixed income.
2. The Size Effect: the extra risk of small-cap stocks over large-cap stocks.
3. The Value Effect: the extra risk of high book-to-market (BtM) over low BtM stocks.

When properly educated, investors have the opportunity to apply these factors to their portfolio productively.

The first risk factor in the 3-Factor Model is the amount of exposure to equities. Since equities are riskier than fixed income, equities historically provided greater returns. Determining your level of risk comfort is important in deciding how much of your portfolio should be in equities.

The second risk factor is called the Size Effect. Small companies historically provided a greater return than large companies.

The third risk factor is the Value Effect. This means value companies historically provided greater returns than growth companies.

Eugene Fama and researcher Kenneth French, former professors at the University of Chicago Booth School of Business, looked for ways to better measure market returns. Their research involving thousands of random stock portfolios showed value stocks outperform growth stocks and small-cap stocks tended to outperform large-cap stocks.

Fama and French stressed that investors must be able to ride out short-term volatility and periodic underperformance.

Conceptually, those investors with a long-term time horizon of fifteen years or more will be rewarded and ultimately compensated for losses suffered in the short-term.

These three truths of investing really are the foundation of my investment philosophy and have been for quite some time. I am a data guy through and through. I like evidence, history, and analyses to back up what I believe when it comes to investing. It certainly helps me sleep at night!

Of course, having a sound investment philosophy is only part of an overall plan. It's time to pull all of these concepts together and build our financial house, using what I like to call a Fiscal Blueprint™.

Pillar #3: Strategy—The 3 Elements of Your Fiscal House

The Fiscal Blueprint™: Building Your Fiscal House to Weather the Elements

Homeowners who live in areas susceptible to inclement weather face the challenge of building a home that can withstand whatever the weather throws at them. The same can be said for an investment portfolio. Over time, our financial assets must weather a multitude of uncertain conditions: market swings, economic downturns, fluctuating interest rates, rising inflation, and changes in our own lives.

Building a strong, flexible, renewable, and sustainable retirement income portfolio is a lot like building a weather-resistant home. The overall strength of a house is dependent on how well its components—the walls, floors, roof, and foundation—work together as a singular unit. When severe weather strikes, such as a thunderstorm, the walls and the roof

bear the brunt of these forces. They need to be strong enough to withstand the inevitable storms that come and go.

Fiscal House Construction: Start with a Strategy

To build a home, you start with a full set of construction drawings. This is the blueprint that details not only what your house will look like, but also all of the individual components that will integrate to create the home. Obviously, you don't just start with one room and then add on later. You design the whole house at one time. To do so, you must first consider all of your objectives for the house. If, for example, you want to optimize energy efficiency, you may want to include items such as solar panels on the roof. Also consider what you don't want to be in the house, such as expensive and high-maintenance flooring. With these objectives in mind, you work together with a professional designer to draw a plan that includes every room and every component of each room until you have a full set of construction plans plus a list of materials and resources needed to build the house.

Similarly, a healthy retirement income portfolio comprises a foundation, walls, roof, and even fencing. The first component on which to build your financial house is the foundation, because without a strong foundation, the house is likely to crumble.

#1: Foundation

What does the foundation of a financial house look like? The foundational elements of a retirement income portfolio are typically its most protected assets—money you can't afford to lose. Generally speaking, these funds will be used for EMERGENCY PURPOSES—now and in the future.

In your fiscal house, the walls and roof are the elements that could be rebuilt over time, but the foundation is the element needed to provide stability for the rest of the house. Your foundation should be composed of accounts that are protected from loss. These can include:

- Checking, savings, and CD accounts, which are protected by the Federal Deposit Insurance Corporation.
- Government bonds, protected by the full faith and credit of the U.S. government.
- Traditional, fixed annuities, protected by the claims paying ability of the company.

Warren Buffett, who is widely regarded as the leading sage on investing, sets this primary rule of investing: Don't lose money. The foundation of your fiscal house is what helps you adhere to this rule. Think of this as your emergency fund. If everything goes off the rails this is your safety net.

#2: Walls

The walls of a retirement income portfolio provide a guarantee for your retirement income. They comprise traditional corporate or government pensions, monthly Social Security checks and investments that can provide various benefits such as income guarantees, cash flow, inflation

protection and possibly some money to pay the costs of treating a chronic illness.[34]

When it comes to the investment portion of the walls, the main purpose is to provide some type of guaranteed income in support of your Social Security and traditional pension benefits. If you don't have a traditional pension, you can effectively create one.

It's important that the walls are coordinated with holdings in both the foundation and the roof because frequently they represent hard-working elements that may contribute significantly to your goals with the least amount of risk possible. Typically, the walls are comprised of the following, as appropriate for the individual:

- Fixed and fixed index annuities
- Social Security benefits
- Pensions from employment

One thing to keep in mind is that corporate pension plans are rapidly becoming a thing of the past. According to Bureau of Labor Statistics data, less than 20 percent of employers with between 100 and 499 employees provided a pension in 2018, and just 7 percent of companies with less than 100 employees offered a traditional pension.[35]

Even large companies, those employing 500 or more people, are gradually phasing out pension plans. Little more than 40 percent of large companies provided pension plans for new hires in 2018, according to the Bureau of Labor Statistics.[36]

There are a few different ways to set up investments that can offer lifetime income like a pension plan does. For me, one

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[34] *Guarantees and protections provided by insurance products are backed by the financial strength and claims-paying ability of the issuing insurance carrier. Examine these when making decisions about which carrier to select.*

[35] Emily Brandon. U.S. News & World Report. "A Guide to Getting a Pension." https://money.usnews.com/money/retirement/articles/a-guide-to-getting-a-pension.

[36] Ibid.

common option to achieve that goal is fixed or fixed index annuities, which I discussed earlier in the book. As you recall, these annuities can provide income you can't outlive. They can also provide a guaranteed source of funds for family members if the original owner is no longer there to provide for them. Interest earnings within an annuity contract are tax-deferred, meaning you don't pay income taxes on them until you withdraw them from your account (assuming you are fifty-nine-and-a-half or older—otherwise you may also pay an additional 10 percent IRS penalty).

#3 Roof

The roof of your fiscal house is represented by the highest level of risk your portfolio can tolerate. These securities have the opportunity to grow, but they can also lose value due to external forces beyond your control—similar to the way a thunderstorm or hail could damage the roof of a home. This is why it's wise to start your retirement income portfolio construction with a sound foundation and strong walls. Should the roof ever be damaged due to risk-based investments, it should not crumble your fiscal house; you need only to replace the roof to repair the damage caused by riskier assets. Roof assets may include:

- Stocks
- Mutual funds, ETFs
- Structured exchange-traded funds/structured mutual funds

It's important to use diagnostic tools to evaluate your level of risk and average expected return you desire. In retirement, measuring and understanding the amount of risk you can emotionally handle is paramount to success.

It may be tempting when constructing your fiscal house to simply steer clear of any risk, but that would open you up to opportunity costs. Also known as shortfall risk, opportunity cost is when a portfolio does not contain financial vehicles that

provide the opportunity for a higher total return. In other words, stocks may be risky—but it can also be risky not to include them in a portfolio designed for growth in order to meet the investor's long-term objectives. Avoiding risk altogether in your retirement portfolio can be like tying an anvil to a hot air balloon: you may still get off the ground, but you won't get anywhere near where you might reasonably expect to under typical conditions.

Bonus Element: Fencing

Finally, as a means to help protect you and your loved ones' futures against potential portfolio losses that may occur before or after your death, it may be a good idea to build a fence around your fiscal house. In this case, the fence represents insurance. Life insurance may help replace your income with a lump-sum payout and can also be structured to help you cover long-term care costs if needed.

An experienced builder has at his or her disposal the knowledge and necessary tools to build a strong, weather-resistant home. Likewise, a competent financial professional will be able to help you deploy both holdings and the proper asset allocation strategies to build a market-resistant retirement income portfolio.

Conclusion

> *"If you don't design the future, you're going to drift to a destination you never chose."—Michael Hyatt*

Congratulations are in order. If you made it this far, you are the exception. You are one of the rare breeds that starts something and finishes it! Believe me, that is uncommon.

We started our journey together discussing the powerful number of three and the profound impact it has had in cultures all over the world. I believe this number can have the same immense impact on your dream of having a sound and successful retirement. We covered a great amount of information throughout this book and my hope is by addressing these subjects in groups of three, they will be more committed to memory. Your journey hasn't ended here, however.

You must take action.

You must take action for yourself and the ones you love. I know life gets in the way and it is very easy to put things off. You say to yourself, "I'll get to it next week." Then, next week turns into next month, next month turns into two months, and soon you are in the exact same place you were a year ago. No excuses, no blame. Take full responsibility and just do it!

Acknowledgments

I truly love what I do and it's an honor to be able to share my passion with you. However, I didn't do it alone. I would like to thank my office staff: Nicholas Craven, Joani Gursky, and especially Kristen Burns. Kristen kept me organized and structured with all the ideas rolling around in my head. I could have never finished it without her.

I also want to thank my wife, Joan, who kept me focused on finishing and completing this book. Without her support at home, it never would have happened. I would like to thank all my mentors, friends, and colleagues.

And, finally, a very special thank you to all my clients. Your success is the most important thing I can help with every day. It is what drives me and what has prompted me to write this book.

Thank you!

About the Author

Jeffrey D. Montgomery is the founder and president of Montgomery Financial Services LLC. As a financial advisor, Jeff is passionate about helping retirees achieve a greater understanding of the need for building a comprehensive financial strategy for retirement.

After graduating from Towson University in 1991 with a degree in business and economics, Jeff worked a well-known mutual fund company, where he specialized in investment services.

He understands the importance of planning for a financially secure retirement and regularly conducts public seminars and gives talks at retirement centers, businesses and other locations in the Delmarva area to spread his knowledge. His topics often include areas of behavioral finance and helping clients deal with the emotions that come with investing.

Investor information is so important to Jeff that he equipped Montgomery Financial Services' corporate offices with a state-

of-the-art financial resource center where he and his staff help inform clients on their investment strategies in a high-tech environment. Many clients comment on his unique ability to explain complex concepts simply and to inspire them to achieve a life of wealth and abundance.

Jeff works primarily with pre-retirees, retirees, and affluent small-business owners, helping them grow, protect, and distribute their financial assets. Jeff and his team have spent years developing and refining a process that helps clients align all the pieces of the financial puzzle to meet their clients individual true-purpose. This trademarked process is called The Fiscal Blueprint.®

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