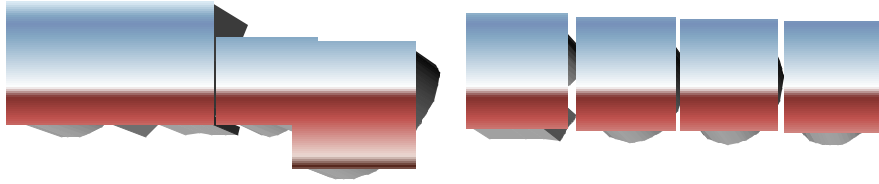


®

# Your Retirement



RETIREMENT PLANNING CONSULTANTS



A Guide To Your Retirement Planning – May, 2006, Volume III - Number 5

Welcome to Your Retirement, our monthly web-newsletter with information that can help you with your retirement planning efforts. We provide straight-forward, easy to understand, unbiased and candid information. Feel free to use this information and to also pass it along to your friends and associates. You will find previous issues of our newsletter on our website. If you are interested in additional information that can help you, be sure to check out our web site; [retirementplanningconsultants.com](http://retirementplanningconsultants.com) or contact Robert R. Julian, at [rrj1@cornell.edu](mailto:rrj1@cornell.edu)

## In This Issue:

- **Our Brand New 2006 Workshop: Saving – Investing For Retirement --- A Simple Approach: You Can Do It**
- **What You Should Know: Should Your Portfolio Contain International Funds?**
- **Our Brand New 2006 Workshop: Saving – Investing For Retirement -- Simple Portfolio #3**
- **Getting To The Nitty-Gritty: - What Are The Odds? Winning The Lottery vs. Buy And Hold Investing?**
- **A Retirement Diary: It's Hard To Get Excited About Index Funds**
- **How Can I Find Out: How Much I Need To Have Invested**
- **Building Your Nest Egg: Patience In Investing**
- **Interesting Perspective: Will Social Security Be Enough To Finance Your Retirement**
- **Sandy The Smart Saver: Spread Your Dollars Among Basic Asset Classes**
- **Sandy Cartoon**
- **Quick Takes #1 Why Past Performance Is No Guarantee of Future Results**
- **Quick Takes #2 Defined Contribution Plans Don't Do Enough To Help Workers**
- **Stock Market – Wall Street --- Investment Humor**
- **Quotable Quotes**

## **Our Brand New 2006 Workshop: Saving – Investing For Retirement --- A Simple Approach: You Can Do It**

Mark Hebner, in his new book, *Index Funds = The 12-Step Program For Active Investors*, states that the biggest problem investors face today when they select their investments is their continued reliance on information sources other than empirical research from organizations like the Center for Research in Security Prices at the University of Chicago.

Mark states, “Investors often speculate, rely on Lady Luck, market time, and chase recent successes of managers, stocks and investment styles. As opposed to following the expertise of Nobel laureates, they blindly wander into the beckoning arms of active managers who dominate Wall Street walking right past the financial academics.”

What can these experts offer the average investor --- “the one thing active managers cannot --- unbiased , rigorous and empirical research that will guide them to a risk-appropriate tax-managed, and highly efficient portfolio of low cost index funds.”

What does the research show? While the S&P 500 index is criticized by Wall Street and the fund companies that market actively managed funds as being “average,” it has beaten the managed fund average over the last ten and five years and trailed only in the last three and one-year periods – not bad for being just “average.”

In our brand new workshop, we look at and discuss 10 simple, lazy-low-maintenance portfolios that utilize index funds. What is the aim of this approach? It is to produce a portfolio of low-cost mutual funds investing in asset classes that are likely to outperform the S&P 500 Index and many, if not most actively managed mutual funds

On page 2 of this newsletter, you can take a look at Simple Portfolio #3.

“Question: I wonder if I might ask you, ...how do you think people should invest for the future...? Should they buy index funds? Answer: Absolutely. I have often said, and I know this will get some of your readers mad, that any pension fund manager who doesn't have the vast majority and I mean 70% or 80% of his or her portfolio in passive investments is guilty of malfeasance, nonfeasance or some other kind of bad feaseance! There's just no sense for most of them to have anything but a passive investment policy.” An Interview with Merton Miller, Nobel Laureate in Economics, 1990

**What You Should Know: Should Your Portfolio Contain International Funds?**

If you take a look at the returns of mutual funds in 2005, you will notice that for the fourth year in a row, international stock funds outperformed domestic ones with an average gain of 17.5% vs. 6.9%.

This kind of performance, as you might guess, triggered a predictable stampede by performance chasing investors. Penelope Wang, in her Fund Watch column in Money magazine (March 2006), states that “most of us don't have enough money in foreign stocks so we may be doing the right thing for the wrong reasons.”

More and more of the experts warn us that it is always a mistake to chase after a hot market ---- just remember the stampede to be in high-tech, internet related funds in the late 1990s.

Wang tells us that if you have been one of the investors jumping in and out or maybe ignoring foreign funds, “it's time you understood the real reason to invest abroad: done sensibly, it makes your portfolio safer and boosts your long-term returns.” “Foreign markets don't move in lockstep with U.S. exchanges and they also improve your chances of earning strong returns.”

Wang states “financial advisors typically recommend that you keep 25% to 30 % of your equity portfolio in foreign stocks.” But Wang warns us to “Avoid the temptation to keep piling in.”

“The long run is a misleading guide to current affairs. In the long run we are all dead. Economists set themselves too easy, too useless a task if in tempestuous seasons they can only tell us when the storm is long past, the ocean will be flat.” - John Maynard Keynes 1883 – 1946, British economist, 'A Tract on Monetary Reform', 1924.

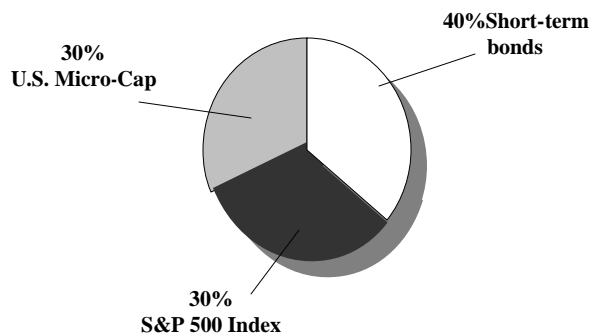
**Our Brand New 2006 Workshop: Saving – Investing For Retirement -- Simple Portfolio #3**

In the March 2006 edition of this newsletter, we featured from Paul Merriman's book, *Live It Up without Outliving Your Money*, Portfolio #1--- had an annualized return of 10.4%. In April, in Portfolio #2 which allocated 60% to the S&P 500 index and replaced the 40% in the Lehman Government - Corporate Bond index with a shorter - term fixed-income component (Short-term bonds). It also had an annualized return of 10.4% (1/1973 – 12/2005)

In Merriman's Simple Portfolio #3, he reduces the allocation to the S&P 500 Index (large-cap U.S. stocks) from 60% to 30% and adds 30% to U.S. Micro-Cap (small-cap U.S stocks). It maintains 40% in short-term bonds. The result is a higher annualized return of 11.2%.

**Simple Portfolio #3**

In portfolio #3, we reduce the allocation to the S&P 500 Index (large-cap U.S. stocks) from 60% to 30% and we add 30% to U.S. Micro-Cap (small-cap U.S stocks). We still maintain 40% in short-term bonds. The result is a higher annualized return of 11.8%.



Annualized Return From January 1973 – December 2005

Portfolio 1 -	10.4%
Portfolio 2 -	10.4%
Portfolio 3 -	11.2%
\$100,000 grew to \$3,593,685	

Talk to the people in your benefits – compensation – HR office about this workshop and how it can help you and your fellow employees. Ask them to get in touch with us so that we can bring this informative program to your work place. We think you, the average investor, can gain a great deal from participating in this workshop.

Email: [rrj1@cornell.edu](mailto:rrj1@cornell.edu), Phone: 607-255-4405

**Getting To The Nitty Gritty: What Are The Odds? Winning The Lottery vs. Buy And Hold Investing?**

Back in February, we all had the chance to see-hear-read about America's 8 new millionaires --- workers at a meat packing plant who won a record U.S. lottery prize of \$365 million. They each opted to take a lump-sum payment of \$177 million.

There are millions of Americans who each week chase “The lottery will finance my retirement” dream. What are the odds of this happening? According to the Forum for Investor Advice, it is 1 in 4 million --- not very good odds. In fact, you are more likely to be dealt a royal flush: 1 in 650,000.

In an effort to put your odds of the buy and hold philosophy of investing into perspective, consider these additional statistics.

- Odds that Earth will be struck by a meteor during your lifetime: 1 in 9,000
- Odds that you'll be robbed this year: 1 in 500
- Odds that the airlines will lose your luggage: 1 in 186
- Odds that you'll be audited by the IRS: 1 in 100
- Odds that you'll get snake eyes when rolling the dice: 1 in 36
- Odds that you'll go to Disney World this year: 1 in 10
- Odds that the next bottled water you buy will be nothing more than tap water: 2 in 10
- Odds that you'll eat out today: 5 in 10
- Odds that an investment in stocks will make money in any given year: 7 in 10

That's right --- over the past 100 years, the stock market made money 70% of the time. The fact that it didn't in 2000 or in 2001, is both uncommon and irrelevant to your long-term planning. Therefore, you should not let recent performance affect your long-term investment strategy.

*"Overconfidence --- Before you attempt to beat the odds, be sure you could survive the odds beating you." Larry Kersten, Retired Professor of Sociology and Family Sociologist, Wayne State University*

### **A Retirement Diary: It's Hard To Get Excited About Index Funds**

I know --- I know ---the media is constantly trying to get our attention with all of those slick ads on TV and in the financial magazines. There you are --- strolling on the beach, playing golf, spending time with the grandkids, relaxing on a cruise ship, shopping in exotic locations --- you name it. In advertising they tell you to sell the sizzle---not the steak.

I do have to admit, index investing is dry, dry stuff --- not much sizzle here. Just boring information like --- the primary reason to invest in index funds is that in the long run, an index investor will achieve greater risk-adjusted performance from his/her portfolio with less stress than an active investor.

Hundreds of academic studies have shown that managers of actively managed mutual funds do not beat the markets --- the markets beat them. But don't expect to hear, see that on TV or the ads in financial magazines. Unfortunately, not many investors pay attention to what academics and Nobel laureates are saying.

Index investing makes it easier for you to rebalance and maintain a consistent asset allocation. You don't need a sales person to buy or sell shares and pay a commission to help you to do that.

Index funds have low investment costs. They do not have the high annual operating expenses of actively managed funds (about 2.0% vs. 0.18% for index funds). The returns that the actively managed fund takes away from you can, on a long-term basis, eat up a lot of your profit.

And index funds have low portfolio turnover --- as opposed to high turnover by managers who run actively managed funds. The average mutual fund turns more than 90% of its stock each year. This forces the distribution of realized capital gains which become tax liabilities for the actively managed funds' shareholders. On the other hand, index funds buy and hold, so they rarely incur realized capital gains.

An index fund invested in an asset class will always earn the returns of that asset class --- it delivers what it promises to investors. In the meantime, the returns of active funds are erratic and less reliable than index funds.

With index funds, the stress and pressure of investing is eased, allowing the investor to receive the market returns of a diversified portfolio that is matched to risk capacity and at a very low cost.

Like I said --- nothing exciting about index fund investing --- just a lot of dull, boring information that can help you to achieve your investment goals.

Just one final point --- A good number of mutual fund companies sell index funds but --- you won't see them advertised by the fund companies in the ads they buy in investment publications. Could it be that they can make a lot more money by selling you their actively managed funds with the higher fees and sales commissions???

*"On average, if eight blindfolded chimpanzees threw darts at the stock pages of the Wall Street Journal for three years, one of them would end up beating the market.*

*Humans and chimps share roughly 98 percent of the same genes, but that doesn't make it a good idea to give your money to a stock picker who munches on bananas and termites. Our chimp isn't a great investor -- he's just lucky."*

*Jason Zweig, Money Magazine*

### **How Can I Find Out: How Much I Need To Have Invested**

With the help of a calculator, you can compute how much you would need to have invested in order to withdraw a specified amount each year over the course of a specified period of time. Go to [www.pacificasset.net/tools.asp](http://www.pacificasset.net/tools.asp)

### **Building Your Nest Egg: Patience In Investing**

The 1990s was probably one of the best decades we have ever experienced in investing --- probably it was too good. You didn't have to be an expert investor ---just about everything went up. Too many of us investors thought that building a retirement nest egg was a fairly easy process.

Case study: One investor is unhappy with his investment in the S&P 500 index fund. Back in 1999, he was told that the S&P 500 index would easily double in 7 ½ years --- so he invested \$10,000. The problem he says is that in early 2006, his \$10,000 was worth only \$10,500. He asks the question --- Would it be better for me to put that \$10,500 in a certificate of deposit?

George Mannes, The Answer Guy for Money magazine, says that "Over the past 20 years, the total return of Standard & Poors 500 index has averaged 12.2% a year." Mannes adds that at that rate, the investor's money would have doubled in about six years "and you would have earned much more than the average 6.2% that five year certificates of deposit have yielded annually since 1984."

The problem with this scenario is that long-term averages don't always deliver in the short run. You will never get a guarantee that in any one single year or years that the S&P 500 will achieve its average return or will it outperform a CD. That is why the SEC mandates the statement "Past performance does not guarantee future results" appear in the prospectus and ads promoting mutual fund.

Sure, as Mannes points out, you can park your money in a CD --- you will protect the principal and it will give you a fixed yield. But, as patient long-term investors know --- like a tree, investments do not go up in a straight line.

As Mannes and many other experts will tell the unhappy investor, "stick with stocks because it's reasonable that they will regain their traditional lead over CDs." Stay with an index fund ---like the S&P 500 and be patient. It is not a slam dunk but history will be on your side.

*"All things come to him who waits - provided he knows what he is waiting for." Woodrow T. Wilson, 1856 – 1924, 45th state Governor of New Jersey and later the 28th President of the United States*

### **Interesting Perspective: Will Social Security Be Enough To Finance Your Retirement?**

A couple of months ago, Putnam Investments conducted a study of median income levels among retirees. Of the \$34,000 your average retiree collects every year, Social Security provides just 41% -- \$13,940. We know that some workers will have a defined benefit pension plan that will add something to the pot and some may have enough in their 401(k) to also help out --- and as we have pointed out in previous issues of this newsletter, retirees are returning to the workplace.

The whole point is that Social Security can supplement your income in retirement but it was not designed to pay for the whole ride. You have to do your part.

The cost of living increase for Social Security for 2006 is 4.1%. However, the Medicare Part B monthly premium is \$88.50 in 2006, an increase of \$10.30 from the 2005 monthly premium of \$78.20. In a good number of households, that increase pretty much took care of the cost of living increase.

And we all know that there are questions about the future of Social Security and whether Uncle Sam can afford to continue to pay the benefits that have been promised to future retirees.

According to the Employee Benefit Research Institute's 2005 Retirement Confidence Survey, fewer than half of all Americans age 55 and older have even \$45,000 saved up for retirement. In fact, excluding home equity, the median net worth of retirement-age Americans is closer to \$30,000.

Some surveys indicate that the average American can fund only about 11% of retirement needs from his/her personal savings. And the most recent results of our savings rate indicate that we are saving less than 0% of our income --- that does not bode well for the future.

Let's pass along a suggestion from The Motley Fool. "Spend less, save more. If you can up your savings by just \$84 per month (\$1,000 a year) and grow that nest egg at the stock market's average historical rate of 10.5% per annum, in 20 years' time you'll have \$45,285 to supplement your Social Security income. And that's factoring in an inflation rate of 3%."

Motley Fool adds that you can start earlier and save more. "If you can save twice the \$84 mentioned above, and start just five years earlier, that \$168 invested monthly over 25 years will more than triple your nest egg, giving you more than \$142,319 by retirement (again, in today's dollars)."

*"I'm saving that rocker for the day when I feel as old as I really am".*

**Dwight D. Eisenhower, 1890 – 1969, 34<sup>th</sup> U.S. President**

### **Sandy The Smart Saver:**

<p><b>Planning - Saving - Investing For Retirement</b></p> <p><b>Sandy Says: Spread Your Dollars Among Basic Asset Classes</b></p>	
--	---

Josephine (my mom---bless her soul) really knows a thing or two about asset allocation. I don't know how many times she told me, "Sandy, don't put all your eggs in one basket." I then asked why and she said, "Two things can happen. #1- If you only have one basket and that basket falls to the floor, you won't have eggs for breakfast. And #2 – If you invest all your eggs (dollars) in technology stocks or funds like your Uncle Elmer did back in the late 1990s, your retirement nest egg will evaporate." Mom always had a way with words.

Where you choose to place your investments is where you will allocate your assets. When you make a choice among asset classes---stocks, bonds, cash---you are engaged in asset allocation. You decide how much (%) of your investment dollars you want allocate to each class.

Jo told me that when you spread your dollars among the basic asset classes, you help cushion those dollars against the ups and downs of different financial markets. Not all of the asset classes will do well at all times. A portfolio spread over good stocks of large, medium and small companies and foreign companies will supply solid returns with much less volatility than a portfolio spread over just one or two of those asset classes.

Each asset class performs differently in different economic situations. Some are up one year, down another --- we've had enough experience with that. It's when you combine them that they smooth out the ride—and over the long term, provide higher returns.

I would like to cite my friend Gary Brinson, president of GP Brinson Investments and a nationally recognized authority on global investing. In his study of 91 large pension funds, he found that 94% of a mutual fund's performance can be attributed to a sound asset allocation strategy while only 7% of portfolio performance was related to the selection of specific securities. Ninety-four percent sounds like pretty good odds to me.

On balance, market timing and specific investment choices detracted from performance. This study has been repeated many times using different databases and the researcher's have agreed with the original study's finding that asset allocation is by far the most important factor in performance.

Successful investing is not picking the individual winning stock or fund. It is not timing the market. It is spreading your portfolio across a variety of investment types. It's not buying the hottest fund during the past six months.

Mom told me more than once, "Don't listen to your Uncle Elmer when he talks about investing. He thinks that asset allocation is just allocating your acorns in different piles on the dinner table. Nice man but he don't know squat about investing."

You know what...Josephine has her act together. She'd be an excellent host for one of the financial shows on TV. She has a great portfolio and she really watches out for her dollars and cents—and her acorns too! She's a great C.E.O, cook, gardener, interior decorator. We call her "Martha"--- you know what I mean.

*I didn't end up going bankrupt. . I made some great investments and I held on to my money, which also enables me to have the freedom to do what I want now. But it's not about finances. No matter what, it's about keeping it real. Vanilla Ice, an American rapper*

### **Sandy Cartoon:**

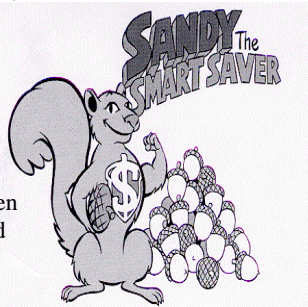
**Camille (wife):** Did you know there was a tremendous turnaround in the stock market this afternoon?

**Sandy:** Really? What happened?

**Camille:** It's been reported that a stock broker on Wall Street jumped out of a window on the 14th floor of his office, looked at a computer screen on the 8th floor on the way down and quickly did a U-turn.

**Sandy:** And he quickly got on the phone to his clients and told them about the rally?

**Camille:** Of course!!!!



### **Quick Takes #1: Why Past Performance Is No Guarantee of Future Results.**

You have probably seen the statement “Past Performance Is No Guarantee of Future Results.” --- It appears in ads for mutual funds, TV commercials , the prospectus of your mutual fund, etc. It is there --- usually in small print --- because the Securities and Exchange Commission mandates that this disclaimer must appear in print.

And one of the reasons that it is there is that the past performance of mutual fund managers has nothing to do with future results. Every study over the past 30 years has found that there is no reliable way to know if the superior managers of the past will win again in the future --- those who have outperformed some benchmark are more than likely to underperform in the future.

Burton Malkiel, Professor of Economics at Princeton states, “It does not appear that one can fashion a dependable strategy of generating excess returns based on a belief that long-run mutual fund returns are persistent.”

Why is this so? Researchers tell us that the outstanding record turned in by a mutual fund manager is primarily the result of the market favoring his particular investment style. As Mark Hebner, in his book, *Index Funds – The 12 Step Program For Active Investors* states, “One implication of this is that any such performance is entirely unpredictable --- as is the time period that such good fortune may or may not last. Since market returns are correlated to risk factors (not to managers) there is no reason to expect that one manager will do better than another.”

Hebner concludes, “These factors alone are all that is needed to prove that manager picking doesn't work and is not a good basis on which to invest money.”

### **Quick Takes #2: Defined Contribution Plans Don't Do Enough To Help Workers**

Rep. Earl Pomeroy, D-N.D, a member of the House Ways and Means Committee, said in an interview that the pension reform bill now being ironed out by both the House and the Senate isn't doing enough to help workers save for retirement.

Pomeroy says that the current proposals “fall short of making a meaningful effort to ensure retirement benefits for workers by not encouraging corporations to keep offering defined benefit plans.” “And the White House is even worse. We had White House officials calling legislators in Alaska and encouraging them to freeze the state's defined benefit plan and switch to a defined contribution plan.”

Essentially, Rep. Pomeroy states that defined contribution plans don't do enough to help workers save for retirement, and the pension reform bill should at least require defined contribution plans to offer an annuity option to guarantee a steady stream of income. “A 401(k) plan was originally conceived as a complement to the traditional defined benefit plan — it was supposed to simply be an additional way to save for retirement. But to have a 401(k) plan as a sole means of retirement funding, you've got savings risk and longevity risk without annuity protection that guarantees cash flow to retirees. We're going to have some very broke, very sick and very old Americans,” he said.

*“Just “20 percent of workers in the private sector were employed at establishments that offered defined benefit plans.” Congressional Research Service Report, 2004*

### **Stock Market – Investment Humor**

- *Two women were walking through the forest when they hear this voice from under a log. The women discovered the voice was coming from a frog.*
- *"Help me, ladies! I am an investment banker who, through an evil witch's curse, has been transformed into a frog. If one of you will kiss me, I'll be returned to my former state!"*
- *The first woman took out her purse, grabbed the frog, and stuffed it inside her handbag. The second woman, aghast, screamed, "Didn't you hear him? If you kiss him, he'll turn into an investment banker?"*
- *The second woman replied, "Sure, but these days a talking frog is worth a lot more than an investment banker!"*

### **Quotable Quotes**

- *If you want to have fun in the stock market, make sure you, and not some mutual fund manager, is the one having fun. - Bill Schultheis, *The Coffeehouse Investor**
- *"Few investment choices, be they stocks, bonds, funds, commodities or real estate, can be expected to out perform their peers year in and year out. Nearly all investments go through cycles, and buying one after a good year could just set you up for a quick loss." - James B. Stewart, *SmartMoney*, January 2006*
- *You are my young son, and, as the years go by, time will change and even reverse many of your present opinions. Refrain therefore awhile from setting yourself up as a judge of the highest matters. - Plato 427bc – 347bc, *Dialogues, Theatetus**
- *If you invest in haste, more often than not a loss will result. And unlike the speed with which you made your move, you'll have lots and lots of time to regret it. - Anthony M. Callea, *Bulls Make Money, Bears Make Money, Pigs Get Slaughtered*.*
- *The common idea that success spoils people by making them vain, egotistic and self-complacent is erroneous; on the contrary, it makes them for the most part humble, tolerant and kind. Failure makes people cruel and bitter. - W. Somerset Maugham 1874 – 1965, [English playwright](#), [novelist](#), and [short story](#) writer,*
- *Pouring your retirement savings into real estate instead of stocks may have seemed smart when home prices were soaring in the double digits. But historically, real estate appreciates at a lower rate than stocks --- 5 to 6% a year, not much more than the rate of inflation." - *Money magazine*, February, 2006*

This newsletter intends to present factual up-to-date, researched information on the topics presented. We cannot make any representation regarding the accuracy of the content or its applicability to your situation. Before any action is taken based upon this information, it is essential that you obtain competent, individual advice from an attorney, accountant, tax adviser or other professional adviser. Information throughout this newsletter, whether stock quotes, charts, articles, or any other statements regarding market or other financial information, is obtained from sources which we, and our suppliers believe reliable, but we do not warrant or guarantee the timeliness or accuracy of this information. No party assumes liability for any loss or damage resulting from errors or omissions based on or use of this material.