Another Problematic Situation

If you are 5-7 years away from retirement or less than five years into retirement, you are now in a problematic situation.

I am referring specifically to affluent families who have worked for 30 or 40 years to build up a retirement nest egg. I have written previously about affluent families who are in their upper 50s or in their 60s and their need to be careful with the assets they have accumulated and protect their retirement nest egg from:

- Burdensome taxation
- Judgments via lawsuits
- Declines in the underlying investments

Declines in The Underlying Investments

The balance of this article will discuss the possible investment situations germane to people in the years around retirement.

After a five-year bull market in stocks with many of the averages increasing over 200% and a similar return on bonds over the past 25 years I find us in another problematic situation. I was recently quoted in the Wall Street Journal (http://www.reuters.com/article/2014/07/08/us-markets-stocks-idUSKBN0FD14H20140708) regarding the lack of growth in company sales versus the significant growth in earnings of large companies on the stock exchanges.

With stock markets at or near record highs and bond rates at or near record lows the possibility of incurring significant losses to your portfolio over the coming years is very real. If you have worked and saved for many years and have successfully grown your assets, now is a time to be very careful.

According to Neena Mishra from Zacks investment research, the average length of a bull market since 1921 is 62 months with a median gain of 115%. The current bull market in stocks started in March 2009 and has gained about 180%.

The Perfect Storm

According to Jim Bianco, president of Bianco research in Chicago, from 1981 when interest rates were near their peak, long-term government bonds have produced a better return than stocks over the ensuing 30 years. Long-term government bonds have gained an average of 11.5% per year versus the S&P 500 gaining 10.8% per year over the same period with much more risk and greater volatility.

So most affluent families who saved their money and invested in stocks and bonds had a tailwind from bonds over the past 30 years. Many investment professionals have forgotten that the allocation to

bonds was not only a stabilizing influence versus the volatility of stocks but also may have produced significant principal appreciation above that of the stock market.

Looking Into the Future by Observing the Present

So the question is: What does the affluent family that has worked to save their money over the past 30 or 40 years to do? If I could accurately forecast the future with respect to investments around the world, economies around the world and geopolitical concerns that would be great. But since I don't have that ability all I can do is look at past history, the present situation of economies around the world, present geopolitical landscape and make an educated guess on the investment climate over the next few years.

It doesn't require a soothsayer to see that bond rates are near historic lows and stocks are near historic highs. Nor is it much of a stretch to observe that not only the United States Federal Reserve but really many monetary authorities around the world are trying to stimulate their economies. I would suggest the US Federal Reserve under Janet Yellen is more worried about deflation and not inflation. As Paul Volker demonstrated in the 80s, inflation can be tamed. But as we observed in Japan, in December of 1989 the Japanese Nikkei 225 was close to 39,000. Currently, which is **almost 25 years later**, the Japanese Nikkei 225 is a bit over 15,000 and the Japanese economy is still struggling with deflation.

So with a zero interest rate policy and abundant amounts of money in the system, I believe one of the goals of the US Federal Reserve is to create a wealth effect via the stock market, which they hope will translate into increased spending and thus spur economic growth and cause more inflation.

My Advice

If you're invested in only stocks, bonds and cash I'd be very careful. The current bull market in stocks could still run for a while. But, if you're a few years away from retirement or a few years into retirement the last thing you want to see is stocks drop by 30% or interest rates rise in a short period of time. Each of these scenarios could produce a significant loss of capital at a time in your life when you can least afford to see a significant reduction in your retirement nest egg.

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