Planning for an Imminent Retirement

As you approach retirement, your priorities must change. Certainly, compiling a sufficiently large nest egg remains important, but now you must focus more on preserving what you've accumulated and generating income to meet day-to-day expenses for the rest of your life. To achieve these objectives, you'll need a strategy to help you manage:

- **Market Risk** – the possibility that your investments won't perform as you hoped they would, especially during the early years of retirement
- **Inflation Risk** – the erosion of future purchasing power when investment returns don't keep up with the annual inflation rate
- **Longevity Risk –** increasing life expectancies are cause for celebration but only if you have enough money to support your lifestyle

At NFP, we recommend a three-pronged approach that we call our "bucket strategy." Imagine your retirement assets are divided among the following three buckets:

1. Current Expenses

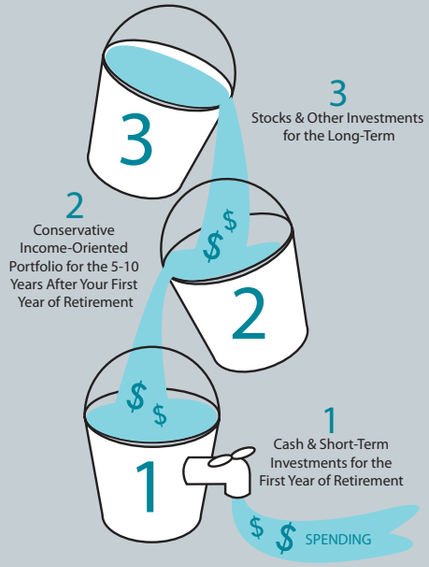
Your first bucket should contain enough assets to fund your first year of retirement and provide an extra cushion in the event of emergencies or unforeseen expenses. Typically, this bucket is funded with bank CDs, money market funds, or other liquid investments. Fixed annuities are also a possibility.

2. Intermediate Expenses

Depending on your risk tolerance, you might fill this bucket with enough assets to fund your retirement income needs for the 5-10 years following your first year of retirement. Certainly, you can fill this bucket with corporate or municipal bonds, but in today's low yield environment, you might also consider a variable annuity that offers a guaranteed income benefit. Available at an additional cost when you purchase your annuity, this benefit provides a specific level of income at retirement, regardless of how your variable investment options perform. Another funding possibility might be the cash value generated by a permanent life insurance policy. This approach may offer tax advantages unavailable with other strategies.

3. Long-Term Expenses

This bucket is filled with the remainder of your retirement assets which are invested in a diversified portfolio of stocks, bonds and possibly alternative investments selected to meet your risk tolerance.



With this segmented income bucket strategy, you create a cascading effect in which one bucket replenishes another on a continual basis. The only bucket that is not replenished by another is #3, the Long-Term Expenses bucket. Consisting primarily of stocks, this bucket should hypothetically deliver higher returns than the others over the long-term. These returns can be used to maintain the bucket's value and refill the Intermediate Expenses bucket when required.

Buckets at Work

By implementing this strategy, you accomplish the following:

1. You can preserve your assets against an untimely market decline

Not that a market decline is ever timely, but it's especially onerous during the early years of your retirement. Your portfolio is declining in value at the precise time you start making withdrawals to support your lifestyle. When the market finally turns around, you'll have less money available to benefit from the upturn. With this strategy, you make no withdrawals from your stock portfolio (Long-Term Expenses). That's because…

2. You've guaranteed you'll have the income you need for the first 5-10 years of your retirement

You've already created a Current Expenses bucket for the express purpose of funding your first year of retirement, plus an emergency cushion. Your Intermediate Expenses bucket can be funded with a laddered portfolio of bonds, each of which matures in consecutive years. As bonds mature, the proceeds can be placed in your Current Expenses bucket to replenish what you've spent and provide sufficient income for the following year.

3. You've given your long-term assets the time they need to grow

Bear markets typically last for approximately 14 months. Because you've made provisions for living expenses, you can ride out difficult markets in your Long-Term Expenses bucket and give it sufficient time to recoup any losses. In years when you have greater-than-anticipated returns, you can use the excess to purchase additional bonds or other income-oriented investments for your Intermediate Expenses bucket. In other words, the buckets are constantly replenishing each other throughout your retirement (see diagram).

Time is of the essence

Common practice for retirees has been to reallocate their portfolio more conservatively and withdraw no more than 4% of their assets each year. With an ersatz plan like this, you place yourself at the mercy of the markets. Consult with NFP to determine whether this segmented income approach makes sense for you, but do it while you're still working and have the flexibility to plan for your unique circumstances and objectives.

About NFP

Our solutions and expertise are matched only by our personal commitment to each client's goals. We're a leading insurance broker and consultant that provides employee benefits, property & casualty, retirement, and individual private client solutions through our licensed subsidiaries and affiliates.

NFP has more than 3,800 employees and global capabilities. Our expansive reach gives us access to highly rated insurers, vendors and financial institutions in the industry, while our locally based employees tailor each solution to meet our clients' needs. We've become one of the largest insurance brokerage, consulting and wealth management firms by building enduring relationships with our clients and helping them realize their goals.

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