

A Better Way to Manage Money During Retirement

Many people erroneously assume that you can simply break your life into two parts for retirement planning—the accumulation years, when you’re trying to build-up a nest egg, and the retirement years, when you actually spend your nest egg. However, it isn’t quite that simple.

First of all, the accumulation phase consists of two parts—an “early” accumulation period and a “late” accumulation period. The early period relates to the majority of your working years when you’re focused primarily on accumulating assets for retirement. The later period covers the years just prior to retirement when you have to start thinking about repositioning your assets to generate the safe, steady, dependable income you’ll need for the rest of your life. The early period starts the day you get your first job and ends about five to seven years before retirement. The later period is made up of those last five to seven years, and it’s a critical time, because you have to decide when to change your overall investment approach from a growth strategy to a growth-and-income strategy.

Your retirement period also has to be broken down into different time-frames—leading to a concept called holding periods. A holding period is simply the length of time you can stay invested in the stock market (or other growth accounts) to ride out the ups and downs before deciding when to sell. In a typical thirty-year retirement scenario, you might decide to use six five-year planning periods—leading to a variety of holding periods ranging from five to twenty-five or even thirty years. Holding periods provide the time you need to stay invested in equity markets to go after potentially higher growth rates, while reducing the variability of returns around the long-run averages you may be building into your plan. Ultimately, we all have to make our own investment assumptions—and history is only a guide. But if you stay within reasonable historic norms, longer holding periods can lead to less investment risk by reducing the range of actual returns around the averages you’re expecting.

Anticipating this series of increasingly longer holding periods during the planning process can help you analyze the possible consequences of various alternative investment scenarios and rate of return assumptions. But ultimately, the question becomes—how do you manage your retirement assets within this kind of conceptual framework?

And it goes something like this. Throughout your working life, you accumulate assets for retirement. Then, as you approach age 59 or 60, you move into the later period of the accumulation phase, in which you have to decide when to start reconfiguring your portfolio to provide the inflation-adjusted income you’ll need for the rest of your life. In other words, sometime within this five to seven-year period, you’ll have to decide when to sell some of your stock market investments to create your first “income ladder”—because you’ll need to have it ready to go as soon as you stop receiving a paycheck.

Income ladders are the lower-risk, lower-return part of your portfolio that can provide the safe, steady, dependable income you need during retirement, and they’re usually created with the money you get from selling some of your stock market or growth investments. They can be constructed in a variety of ways—but they almost always rely on fixed-income investments like

bonds, CDs, or immediate annuities to provide the financial resources you need to pay the bills and enjoy yourself when you stop working.

After using part of your portfolio to create your first income ladder, you can then let the rest of your assets stay invested in the stock market to continue growing at higher potential rates of return. These stock market, or growth investments, can be separated into a variety of accounts with different risk and return characteristics, depending upon the length of the related holding periods. Ultimately, these growth accounts will be systematically liquidated and used to fund your future retirement income needs.

For example, over the initial five-year period, during which you are spending your first income ladder, the first growth account will have a chance to increase over a five-year holding period, and will hopefully be sufficient to fund your next income ladder—which will in turn be used to provide retirement income for the next five years. Because the first growth account will have a five-year investment horizon, you should be able to assume more risk, and invest for potentially higher returns, because you will have more time to ride out the inevitable ups and downs in the market.

While you are spending both of the first two income ladders, the second growth account will have a ten-year holding period, and will hopefully grow enough to fund the third income ladder. Of course, because the second growth account has a longer investment horizon, you should be able to assume even more risk, and invest for even higher potential returns, than you would in the first growth account.

This same process continues on and on, with each growth account having a longer and longer holding period during which it will hopefully increase enough to fund a future income ladder. Of course, as your holding periods increase, you should be able to assume progressively more risk and go after progressively higher potential rates of return, while actually increasing the likelihood of achieving them.

Another important benefit of this approach can be achieved by structuring the final income ladder to provide income for the rest of your life, rather than just five years. This can be accomplished using a variety of investment tools such as variable or single premium immediate annuities, both of which offer a number of different payout options, including lifetime income. By taking advantage of life-certain annuities late in the game, you will not have to worry about creating additional future income ladders—because your income will be taken care of for the rest of your life. Then, any additional funds that may be available in your retirement portfolio can be invested in an “extra growth” account, which can ultimately be used to help you achieve your wealth transfer, legacy, or stewardship objectives.

This overall approach is based on the reasonable assumption that you can invest for potentially higher rates of return by managing investment risk with longer holding periods, and that you can create those holding periods with income ladders constructed of various fixed-income investments. The combination of reliable income, potentially higher returns, lower risk, longer compounding periods, and life certain annuities at the back-end of retirement can help you generate income significantly greater than many of the other common approaches, and can

provide the structure and the flexibility you may need to achieve reasonable lifestyles over longer and longer retirement periods.

You can learn more about The Grangaard Strategy® approach to retirement income planning, and educational events being offered in your area, by visiting www.TheGrangaardStrategy.com. Paul Grangaard can be reached at paul@pagrangaard.com or by telephone at 651-917-0139.

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