

## Potentially Higher Returns with Less Risk in Retirement

The Grangaard Strategy® approach to retirement financial planning uses a strategy that takes advantage of “holding periods” to help retirees go after potentially higher rates of return while managing the related risks. These holding periods—ranging from five to twenty-five or even thirty years, afford investors the time they need to ride-out the inevitable ups and downs in their growth accounts while going after the potentially higher returns they may need to maintain their income over longer and longer retirement periods.

One of the challenges with this approach is making reasonable rate of return assumptions for each of the growth accounts. Keeping in mind that there are never any crystal balls when it comes to estimating future investment performance, historical experience can provide some overall guidance as to what you might reasonably expect.

To illustrate how historical data can help you develop reasonable return assumptions, we will focus on a fifteen-year investment horizon. Using a similar approach for each of the other holding periods can help you develop a comprehensive set of planning expectations.

**Table 1** provides an analysis of a portfolio comprised of 50% large cap and 50% small cap stocks, over all 56 fifteen-year holding periods from 1936 to 2005. (*Source: Calculated by author using data from Ibbotson Associates Stocks, Bonds, Bills, and Inflation® 2006 Yearbook. The data does not include investment fees and expenses.*)

**Table 1: Historical Return Data for the 56 Fifteen-Year Holding Periods Between 1936 and 2005**

50% LC / 50% SC	(1)	(2)	(3)	(4)	(5)	(6)
	100% of Target Value			95% of Target Value		
	Target Value	Success Percent	Ave. # of Times	Target Value	Success Percent	Ave. # of Times
Rate of Return Objective						
(a) \$100 at 11.0% for 15 years	\$478	80.4%	4.6	\$454	85.7%	4.8
(b) \$100 at 10.5% for 15 years	\$447	85.7%	4.9	\$425	92.9%	4.9
(c) \$100 at 10.0% for 15 years	\$418	92.9%	5.0	\$397	94.6%	5.2
(d) \$100 at 9.5% for 15 years	\$390	94.6%	5.4	\$371	98.2%	5.6
(e) \$100 at 9.0% for 15 years	\$364	98.2%	5.8	\$346	100.0%	6.1
(f) \$100 at 8.5% for 15 years	\$340	100.0%	6.2	\$323	100.0%	6.8

The table shows how often historical market performance would have allowed an investor to meet a variety of fifteen-year growth objectives—using rate of return assumptions ranging from 11.0% down to 8.5%. Column (1) shows the target accumulation value for each rate of return. For example, Row (a) illustrates that \$100 compounding at 11.0% for fifteen years would grow to a value of \$478, while Row (b) shows that the same \$100 compounding at 10.5% for fifteen years would grow to \$447, and so on. Then, Column (2) provides historical success percentages for each rate of return. For example, Row (c) considers all 56 fifteen-year holding periods to assess the likelihood of actually hitting a target value of \$418.

As you can see, the odds are pretty good. Column (2) shows that in 92.9% of all fifteen-year periods, a \$100 investment would have made it to \$418 at least once. Then, Column (3) shows that in all of those successful fifteen-year periods, the target value would have been achieved, on average, in at least five

separate years. For example, you might have hit \$418 in year eight, then dropped below it in year nine, than been at or above it again in years ten, eleven and twelve, then slid back down in year thirteen, back up in year fourteen, and ultimately back down again in year fifteen.

That’s why your ability to “navigate” retirement portfolios is so important—because you need to be able to take advantage of these fluctuations when they occur. In other words, if you hit your target values earlier than expected, you may want to harvest your gains ahead of schedule—because it’s impossible to know what will happen next. In this case, there would have been plenty of opportunities to sell before the end of the fifteenth year—and had you not taken advantage of them, the downdraft in the final year would have taken you below your expected value.

Columns (4), (5), and (6) provide the same information, except that the target values have been reduced to 95.0% of the original amount—so as you can see in Row (c), Column (4), success would mean hitting \$397 (95.0% of \$418) at least once. In Column (5) you will notice that the likelihood of hitting this lower target value increases to 94.6%, and in Column (6) you can see that on average you would have met or exceeded that value more than five times. To take advantage of these opportunities, you could simply sell the growth assets and reinvest the proceeds in safer, fixed-income investments. Then, if you earned 5.0%, you would make it back to 100.0% of your target value in just one year—which shows how much your odds of success can be improved by knowing how to “navigate” your retirement accounts.

Considering all the return data, you will notice in Rows (c), (d), and (e) that in each case, the success percentages met or exceeded 92.9%—with an average of at least five navigational opportunities. Essentially, the data show that over fifteen-year holding periods, you could probably be comfortable using a 9.0% to 10.0% return expectation, and fairly confident that you would have multiple opportunities to lock-in your investment gains along the way.

When evaluating potential rates of return, another key factor is the overall portfolio allocation. **Table 1** assumed a 50/50 large cap/small cap allocation. However, we might want to consider other possibilities. **Table 2** provides the same information as **Table 1**, except that it relates to a more aggressive portfolio of 40% large cap and 60% small cap stocks. You can see that the success percentages improve for every rate of return. In fact, as illustrated in Rows (b), (c), and (d), this allocation suggests a slightly higher range of potential returns—from 9.5% up to about 10.5%.

**Table 2: Historical Return Data for the 56 Fifteen-Year Holding Periods Between 1936 and 2005**

40% LC / 60% SC				(1)	(2)	(3)	(4)	(5)	(6)
				100% of Target Value			95% of Target Value		
Rate of Return Objective				Target Value	Success Percent	Ave. # of Times	Target Value	Success Percent	Ave. # of Times
(a)	\$100	at	11.0% for 15 years	\$478	87.5%	4.5	\$454	92.9%	4.7
(b)	\$100	at	10.5% for 15 years	\$447	92.9%	4.8	\$425	94.6%	5.0
(c)	\$100	at	10.0% for 15 years	\$418	94.6%	5.1	\$397	98.2%	5.3
(d)	\$100	at	9.5% for 15 years	\$390	98.2%	5.5	\$371	100.0%	5.9
(e)	\$100	at	9.0% for 15 years	\$364	100.0%	6.0	\$346	100.0%	6.3
(f)	\$100	at	8.5% for 15 years	\$340	100.0%	6.4	\$323	100.0%	6.9

**Table 3** evaluates an even more aggressive investment posture—a portfolio allocated 30% to large cap and 70% to small cap stocks.

**Table 3: Historical Return Data for the 56 Fifteen-Year Holding Periods Between 1936 and 2005**

30% LC / 70% SC	(1)	(2)	(3)	(4)	(5)	(6)
	100% of Target Value			95% of Target Value		
	Target Value	Success Percent	Ave. # of Times	Target Value	Success Percent	Ave. # of Times
Rate of Return Objective						
(a) \$100 at 11.0% for 15 years	\$478	94.6%	4.5	\$454	94.6%	4.8
(b) \$100 at 10.5% for 15 years	\$447	96.4%	4.8	\$425	98.2%	5.0
(c) \$100 at 10.0% for 15 years	\$418	98.2%	5.2	\$397	98.2%	5.7
(d) \$100 at 9.5% for 15 years	\$390	100.0%	5.8	\$371	100.0%	6.1
(e) \$100 at 9.0% for 15 years	\$364	100.0%	6.2	\$346	100.0%	6.6
(f) \$100 at 8.5% for 15 years	\$340	100.0%	6.7	\$323	100.0%	7.0

Again, you can see that performance improves over all return assumptions, and as can be seen in Rows (a), (b), and (c), the reasonable range of expectations shifts even higher—from 10.0% to about 11.0%.

So, it seems reasonable that if you consider portfolio allocations of 30% to 50% large cap stocks and 50% to 70% small cap stocks, you should probably be fairly comfortable with return expectations ranging from 9.0% to 10.0% or even 10.5% (before fees.) Ultimately, you should do a similar analysis for each growth account (for holding periods ranging from five to thirty years) to develop a comprehensive set of reasonable return expectations for overall planning purposes. Armed with this information, you should be able to work with your advisors to create better retirement plans, and then help navigate those plans for the rest of your life.

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](http://www.TheGrangaardStrategy.com). Paul Grangaard can be reached at [paul@pagrangaard.com](mailto:paul@pagrangaard.com) or by telephone at 651-917-0139.