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financial SUCCESS
MAY 2007

Get the Basics Right

The sheer number of financial decisions required to manage our finances can seem overwhelming. But often we spend an inordinate amount of time on small stuff — getting the bills paid on time, reconciling bank accounts, and calling to have a late charge waived. While those things need to get done, how do we judge whether we're headed on the right course? There are six basic financial decisions that can determine the course of your financial life:

1. How you earn a living.

Sure, we all want to enjoy our work. But within that parameter, why not choose a job that will pay more than another? Your income is going to drive all your other financial decisions, so investigate your options:

✔ Are you sure you're being paid a competitive wage with competitive benefits? Even if you aren't interested in changing jobs now, pay attention to what is going on in your field.

✔ Do you have an outside interest or hobby that can be turned into a paying job? This could be a good way to supplement your current salary, or it could turn into a part-time job or business after retirement.

✔ Can you get some additional training to help secure a promotion or qualify for another job? Read up on what jobs are expected to experience the highest growth rates and/or highest salaries over the next five years. If you don't enjoy your current job, you'll have even more incentive to implement these suggestions.

2. How you spend your income.

The amount of money left over for saving is a direct result of your lifestyle choices, so learn to live within your means. To get a grip on spending, consider these tips:

✔ Analyze your spending for a month. In which categories do you spend more than you expected? Are you wasting money on impulse purchases? Give serious thought to your purchasing patterns, trying to find ways to

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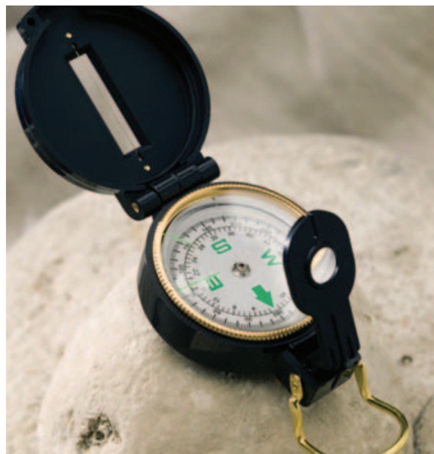

A Happy Retirement

So what makes a retiree happy in retirement? This is an important question, since you could spend 25 to 30 years in retirement. Knowing what makes retirement pleasurable for other retirees may help you plan your retirement.

One study found that approximately 60% of retirees are very satisfied with their retirement, 32% were moderately satisfied, and 8% were not at all satisfied. Retirees who were most satisfied with their retirement were older, had traditional pension benefits, and chose when to retire. Working increased retirement satisfaction, although a working spouse reduced satisfaction, indicating that spouses prefer spending retirement together. Good health also increased retirement satisfaction. The most significant determinant of retirement satisfaction was whether the individual retired voluntarily. Individuals forced to retire were 30% less likely to be very satisfied with their retirement (Source: *What Makes Retirees Happy?*, February 2005). ❍❍❍

Gifting Carefully

With the high divorce rate in this country, you might have concerns about making large gifts to a married child. It's one thing to worry about your child using the money wisely. It's an entirely different worry to think your ex-son- or daughter-in-law might leave the marriage with your money. Some ways to ensure the money stays in the family include:

✔ **Pay for specific expenses.** Rather than making a general cash gift to your son or daughter, offer to directly pay for a specific expense. You might pay for a vacation or private school for your grandchildren. Probably the best option is to directly pay for medical expenses or education costs, since those expenditures won't count toward your annual tax-free gift limit of $12,000 in 2007 ($24,000 if the gift is split with your spouse).

✔ **Keep the money separate.** If you make cash gifts to your children, you might stipulate that the money be kept in a separate account solely in your child's name. Typically, those accounts won't be included in divorce settlements, so the funds will stay with your child.

✔ **Consider trusts.** One way to keep control of the gifts is to set up a trust, naming your children as beneficiaries. However, due to the costs involved in setting up trusts, you probably won't want to use this strategy unless significant sums of money are involved.

✔ **Encourage your child to sign a prenuptial agreement.** This agreement specifies how assets acquired during the marriage, including gifts and inheritances, will be distributed after death or divorce. While a prospective spouse may not like the idea of signing a prenuptial agreement, it is probably in his/her best interest if it encourages you to gift more generously to your child.
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Using Average Returns

When setting up an investment program, the assumed rate of return is typically an average annual return for some historical period. While that is generally viewed as a conservative approach, there are some issues with this approach:

✔ Average returns are an average of past returns and do not indicate what will happen in the future. Economic and market events may or may not replicate past events.

✔ The average annual return can vary substantially, depending on the historical period used. For instance, from 1926 to 2005, the Standard & Poor's 500 (S&P 500) had an average annual return of 10.4%. From 1986 to 2005 (20 years), the average return was 11.9% and 9.1% from 1996 to 2005 (10 years).* Those differences in average return would project a substantially different ending portfolio value over an extended time.

✔ The average return does not reveal the pattern of returns over that period. Some years will experience higher returns, while other years will experience lower or even negative returns. Even if you select an average return that is exactly right, your portfolio's ultimate balance will depend on the pattern of returns over that period.

✔ Most people don't just allow a lump sum to grow, but make deposits and withdrawals over the years. Since your actual return fluctuates from year to year, your pattern of additions and withdrawals can also significantly impact your portfolio's ultimate value.

While it is instructive to consider average returns when developing an investment program, you can't simply project that return into the future. Instead, consider these steps when deciding on an estimated rate of return:

✔ **Evaluate your expectations for future returns against historical averages.** It may be prudent to assume lower returns in the future. It is easier to save less if you obtain higher returns than to try to save more over a short time period if your actual return is lower.

✔ **Consider a range of possible returns for your portfolio.** What would happen to your portfolio's balance if you earned your expected return, 1% less, 2% less, etc.? This analysis can help you determine what adjustments would need to be made to compensate for lower returns.

✔ **Review your progress every year.** This will allow you to make adjustments along the way, so that those adjustments can be gradual. If your return is lower than expected, you may need to increase savings or change investment allocations.

The expected rate of return used in your investment program is an important component in determining how much you should save to work toward your goals. If you'd like help evaluating an appropriate expected rate of return for use in your investment program, please call.
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* Source: *Stocks, Bonds, Bills, and Inflation 2006 Yearbook*, Ibbotson Associates. The S&P 500 is an unmanaged index generally considered representative of the U.S. stock market. Investors cannot invest directly in an index. Past performance is not a guarantee of future results. Returns are presented for illustrative purposes only and are not intended to project the performance of a specific investment.

Get the Basics

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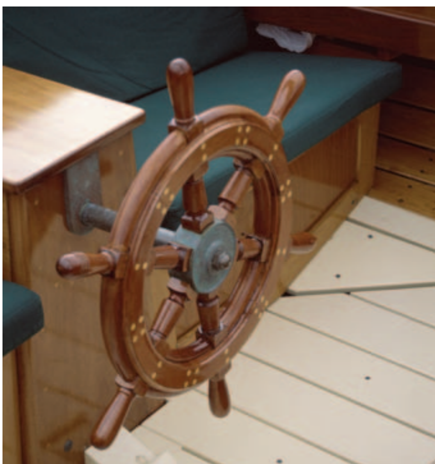
reduce spending.

✔ One of your most significant spending decisions will be your home. Many people purchase the largest home they can afford, often straining their budget. Purchasing a smaller home will reduce your mortgage payment as well as other costs associated with owning a home.

✔ Prepare a budget to guide your spending. Few people enjoy setting or sticking to a budget, but inefficient and wasted expenditures can be major impediments to accomplishing your financial goals. A budget gives you a road map for spending your income. Start by setting a budget for a couple of months, tracking your expenses closely over that time. You can then fine-tune your budget for an annual period.

3. How much you save.

You should be saving a minimum of 10% of your gross income. But don't just rely on that rule of thumb. Calculate how much you need to meet your financial goals and how much you should be saving on an annual basis. If you can't seem to save that much, go back to your spending analysis and cut your spending. First, look for ways to reduce your spending by lowering the cost of your purchases. Perhaps you can refinance your mortgage, find insurance for a lower premium, or use strategies to reduce taxes. At some point, however, you may need to cut your discretionary spending, such as entertainment, dining out, clothing, and travel.



4. How you invest.

The ultimate size of your portfolio is a function of two factors — how much you save and how much you earn on those savings. Even small differences in return can significantly impact your investment portfolio. Typically, investments with potentially higher rates of return have more volatility than investments with lower rates of return. While you don't want to take on excessive risk, you also don't want to leave all your savings in investments with little growth potential. Your portfolio should contain a diversified mix of investment categories, based on your return expectations, risk tolerance, and time horizon for investing.

5. How you manage debt.

Before you take on debt, consider the effect it will have on your long-term goals. If you are already having trouble finding money to save, additional debt will make it even more difficult to save. To keep your debt in check, consider these tips:

✔ Mortgage debt is acceptable, as long as you can easily afford the home.

✔ Be careful about taking equity out of your home in the form of a home-equity loan. You might want to set up a home-equity line of credit for emergency use, but make sure it is only used for emergencies. It may also make sense to use a home-equity loan to pay off higher interest rate consumer loans, but don't run those balances up again.

✔ Never purchase items on credit that decrease in value, such as clothing, vacations, food, and entertainment. If you can't pay cash, don't buy them.

✔ If you must incur debt, borrow wisely. Make as large a down payment as you can. Consider a shorter loan period, even though your payment will be higher. Since interest rates can vary widely, compare loan terms with several lenders. Review all your debt periodically to see if less expensive options are available.

6. How you prepare for financial emergencies.

Making arrangements to handle financial emergencies will help prevent them from adversely affecting your financial goals. Make sure to have:

✔ An emergency fund covering several months of living expenses. Besides cash, that fund can include readily accessible investments or a line of credit.

✔ Insurance to cover catastrophes. At a minimum, review your coverage for life, medical, homeowners, auto, disability, and personal liability.

✔ A power of attorney so someone can step in and take over your finances if you become incapacitated.

Making the correct choices for these six basic financial decisions will help put you on the right financial course. If you'd like help with these decisions, please call. ❍❍❍

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Finding Money to Save

Everyone knows that they should be saving at least 10% of their gross income for retirement, but that can seem like an impossible goal after paying all your bills. However, don't just figure that you can't come close to saving 10% of your income without looking at the after-tax cost.

For instance, assume you earn $50,000 annually and your employer matches 50 cents for every dollar you contribute to the 401(k) plan, up to 6% of your pay. So, if you put 6% of your pay, or $3,000, in the plan, your employer will match 3%, or $1,500. Your contribution really costs less than 6%, because the money is taken out before income taxes. If you are in the 25% tax bracket, your $3,000 contribution will save $750 in taxes, or 1.5% of your pay. So, between your contributions and your employer's match, you will contribute 9% of your pay toward retirement, but it will only cost you 4.5% of your pay.

What if you don't have a 401(k) plan at work? Take a look at individual retirement accounts (IRAs). While you won't get an employer match, you can contribute to a deductible IRA, if eligible, and contribute pretax dollars, which reduces your contribution's cost by your marginal income tax rate. In 2007, you can contribute a maximum of $4,000 to an IRA, and individuals over age 50 can make an additional $1,000 catch-up contribution. So, if you are in the 25% tax bracket and make a $4,000 contribution, you will save $1,000 in income taxes. Or, you may prefer to contribute to a Roth IRA. While you won't get a current income tax deduction for your contribution, you can make qualified distributions free from federal income taxes.

Don't just assume that you don't have the funds to save for retirement, without taking a look at the after-tax cost. Please call if you'd like help with this analysis. ❍❍❍

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A Mortgage and Your Retirement

Will your mortgage be paid off by the time you retire? If not, what impact will that have on your retirement? Approximately 80% of retirees choose to live in their current home after retirement. If living in that home includes making a large mortgage payment, that can significantly affect the income needed for retirement.

According to the U.S. Census Bureau, in 2000, 45% of individuals in their 60s had a mortgage on their home, with 20% also having a second mortgage. But that included individuals at all income levels. Of individuals at all ages with incomes between $61,000 and $121,000, 83% had a first mortgage and 13% had a second mortgage. Of individuals with incomes between $121,000 and $182,000, 82% had a first mortgage and 51% had a second mortgage. Mortgage obligations represented 21% of household income for individuals in their 60s and 24% of income for individuals in their 70s.

If you'd like to discuss this topic in more detail, please call. ❍❍❍

Financial Thoughts

When asked how they viewed retirement, 64% of respondents to a recent survey indicated that it was an opportunity for a whole new chapter in life, 23% indicated it was a time for rest, 9% indicated it was a continuation of what life was, and 3% indicated it was the beginning of the end (Source: *U.S. News & World Report*, June 12, 2006).

In 2004, for households with individuals age 65 and older, 38% of income came from Social Security, 27% from working, 13% from assets, 10% from private pensions, 9% from government pensions, and 3% from other sources (Source: *An Update on Private Pensions*, August 2006).

Approximately 74% of individuals between the ages of 50 and 59 are very concerned about the cost of health insurance in retirement (Source: *Kiplinger's Personal Finance*, November 2006).

In 2005, women in full-time jobs earned an average of 81% of what men performing comparable jobs earned. This disparity varied greatly depending on age. Women between 25 and 34 earned 89% as much as men, compared with 75% for women between 45 and 54 (Source: U.S. Bureau of Labor Statistics, 2006). ❍❍❍