The Three Legs of Investing and Retirement Planning

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Let's take a closer look at the three legs.

Retirement Planning

First things first – you need to plan for retirement. Too often people do not plan and the lack of preparation results in entering the next phase of life unprepared. And back to our analogy of what happens to a two-legged stool.

You should also remember that your retirement plan is unique, and unlike that of your siblings, coworkers, neighbors or friends. You (and your financial advisor) must consider a myriad of information when developing your plan, such as money saved, expected rate of return, your investment portfolio and social security income. On the expense side you will need to take into consideration expected inflation, living expenses, health care costs, potential emergency needs and retirement goals such as travel or a second home.

The bottom line is that you don't want to outlive your money. The average life expectancy in the United States is just under 80 years of age. But for those who are 65 years old today, 34 percent of women and 22 percent of men will live to be at least 90 years of age. So, it's not a far-fetched statement to say you should consider planning for 25 or more years of retirement.

Risk Tolerance

Everyone enjoys a bull market, but invariably the market is going to undergo declines. The problem is that nobody knows when that is going to happen. The key, in my opinion, is to design a portfolio that will not exceed your volatility threshold in a DOWN market. That is why we always have a frank discussion with potential clients to make sure that we – and they – have a true understanding of that person or couple's risk tolerance.

Risk tolerance will vary by age, years from retirement, financial needs and the ability, or inability, to handle market declines. This is your PDL – personal downside limit. One of the worst mistakes an investor can make is to bail out of the market when there is a decline. History has shown that if you are properly invested in the market your portfolio, over time, will normally recover.

Portfolio Management

A very simple philosophy should shape your portfolio management: focus on the knowable and stay away from the unknowable. This will allow you to play to win.

The knowable:

- The short-term direction of the market cannot be predicted.
- The long-term direction of the market is likely up.
- Market declines are common. People react


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more strongly to the threat of loss than the possibility of gain.
- Stocks in the long term likely will provide superior returns over bonds or cash.

Use your previously discussed PDL (personal downside limit) to develop your asset allocation and determine your mix of stocks, bonds and cash.

Large market swings which go either way – up or down – should prompt you to rebalance your account to the asset allocation mix that best fits your financial goals and risks. Your portfolio requires continuous monitoring and recalibrating when needed.

Additionally, your stock holdings should be diversified with regards to industry sectors and geographic locales (both international and domestic).

Bonds promise a stated interest rate and your principal returned after the bond matures. Bond diversification is also needed, and you should ladder your bond portfolio over a number of years (picture maturity dates like rungs in a ladder) because future interest rates are unknown.

Rather than guesswork, your investment and retirement planning should be guided by discipline and patience. The three-legs – retirement planning, risk tolerance and portfolio management – can work together and provide the structure for achieving success.