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## financial SUCCESS

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### Finding a Balance between Risk and Return

One of the most basic investment principles is that returns reward you for the risks that you take. While investors are often uncomfortable with the concept of risk, it is this uncertainty that makes higher rates of return possible. Some basic principles related to risk and return include:

- ✓ Returns on specific investments are not known in advance. Investors can review historical rates of return, but there is no guarantee that past returns will be indicative of future returns.
- ✓ With most investments, there is the possibility that the investment will not meet your return expectations.
- ✓ The uncertainty regarding your actual return creates risk. Greater uncertainties typically lead to greater risk.

✓ Investments are subject to many different types of risk. Cash is primarily subject to purchasing power risk, or the risk that its purchasing power will decrease due to inflation. In addition to purchasing power risk, bonds are subject to interest rate risk, or the risk that interest rates will increase and cause the bond's value to decrease; and default risk, or the risk that the issuer will not repay the principal or interest on the bonds. Stocks are primarily subject to nonmarket risk, or the risk that events specific to a

company or its industry will adversely affect a stock's price; and market risk, or the risk that a particular stock will be affected by overall stock market movements.

✓ There is generally a trade-off between risk and return. Low levels of risk are the most desirable and typically have lower return potential, while higher levels of risk are typically undesirable so must offer higher return potential to encourage investors to invest. Be cautious of claims of high returns

*Continued on page 2*

### Adjusting Your Retirement Portfolio

As you approach retirement age, it is often necessary to adjust your portfolio:

**Assess your retirement financial needs.** To determine what adjustments are needed, you should first assess how much you will need during retirement. Keep in mind any health insurance and medical expenses as you consider your projected budget. You will also want to consider mortgage payments and inheritances you would like to leave heirs. Additionally, determine how much you will receive from retirement income sources.

**Determine appropriate portfolio adjustments.** You will need to take a look at your portfolio to develop an appropriate strategy for allocating your assets. You should align portfolio changes with your individual level of risk preference and ultimate financial goals.

During retirement, you should review your portfolio regularly so you can make adjustments as needed. Life changes, such as an illness, the death of a spouse, or a relocation can significantly affect the amount of money required to maintain your desired standard of living. ○○○



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## Finding a Balance

Continued from page 1

with low risk.

There are strategies that can be used to reduce the total risk in your investment portfolio:

✔ **Diversify your portfolio.** You should diversify among several different investment categories, including cash, bonds, and stocks, as well as within investment categories, such as owning several types of stocks. A properly diversified portfolio should contain a mix of asset types whose values have historically moved in different directions or in the same direction with different magnitudes. By owning several investments rather than just one, a downturn in any one should not have a significant impact on your total return.

✔ **Stay in the market through different market cycles.** Remaining in the market over the long term helps to reduce the risk of receiving a lower return than expected, especially for more volatile investments, such as stocks.

✔ **Use dollar cost averaging to invest.** Rather than accumulating cash so you have a large sum to invest, invest small amounts regularly. Dollar cost averaging involves investing a certain sum of money in set amounts at regular intervals. This spreads your purchases over a period of time. Since you are investing a set amount, you purchase more shares when prices are lower and fewer shares when prices are higher. While a valuable investment strategy, dollar cost averaging does not ensure a profit or protect against losses in declining markets. Before starting a program, consider your ability to continue purchases during periods of low price levels. This strategy requires the discipline to invest consistently regardless of market prices.

If you'd like to discuss how to balance risk and return in your portfolio, please call. ○○○

## 5 Estate-Planning Tips for Dependents

**W**hen you have people who are dependent on you, like children or elderly parents, you want to ensure that they will be well taken care of in the event you can no longer care for them. Here are five tips for creating an estate plan that will ensure your dependents are taken care of according to your wishes.

✔ **Hire an estate planner** — An estate planner will make sure that you think of and lay out every aspect of your estate plan. Estate planners stay up to date on tax rules and other laws and regulations, so they can help you ensure that your plan is legally and financially sound, leaving your dependents in the best situation possible.

✔ **Choose a guardian** — Choosing someone to take care of your children in the event that both you and the children's second parent are deceased is a huge decision to make and deserves great care and time. You want to choose a guardian who loves your children and has the capacity to take care of them into their adulthood. That means a guardian who has the financial capacity to care for your dependents, as well as the physical capacity to do so.

So even though grandparents may be able to love and care for your children just as you did, they may not be in good enough health to care for a child or children. On the other hand, your sister may be able to love your dependents just as much as you did and be in perfect health, but is unable to hold a steady job or stay in a committed relationship. The goal of choosing a guardian is to make sure your children are loved and taken care of adequately, they receive a good education, their lives remain as stable as possible, and they receive emotional support to cope with your loss. It's crucial to communi-

cate with your chosen guardian. Ask early (and often) if they are comfortable being the guardian of your child or children.

✔ **Develop a trust** — A trust is often used when people have minor children or dependents that are incapable of taking care of themselves. You, the trustor, puts a trustee in charge of the beneficiary's property and/or assets until the beneficiary meets certain requirements, such as reaching a certain age or milestone. Usually the named guardian is also the trustee, however each situation is different. Make sure you take time in choosing a trustee and pick someone who is trustworthy and capable.

✔ **Start as soon as possible** — As soon as you have a child or otherwise become responsible for a dependent, it is important to get an estate plan in place to protect them in case of emergency.

✔ **Reevaluate often** — As time goes on, your situation may change quite a bit from your original plan. For example, anytime you acquire a new asset or debt, it should be included in your estate plan. Also, you may realize that the guardian you originally chose for your dependent is no longer the right choice — they may get sick, die, or move far away. You may have more children or unexpectedly start caring for an elderly family member. Anytime major changes happen in your life that impact what you would leave behind and to whom you'd want to leave it, you should revisit your estate plan.

We all want the people we leave behind to be cared for after our deaths as we cared for them during our lives. You may have no control over when or how you will die, but you do have control over what happens to your dependents. ○○○

## Make Pension Decisions Carefully

In the past, a retiree typically received a monthly pension check and Social Security benefits. Now, it's not uncommon for a retiree to have a pension plan, a couple of 401(k) plans, some individual retirement accounts (IRAs), personal savings, possibly some deferred compensation, and maybe an annuity. Deciding how to handle all those different income sources in the most advantageous manner is a daunting task. In many cases, decisions regarding pension plans are irrevocable, so proper choices are imperative.

Before making those decisions, consider the following:

**Prepare a list of all your retirement assets by type of plan.** Indicate the expected monthly income as well as the earliest and latest date you can start taking benefits. Review the payment options available to see if some assets should be used before others. For instance, defined-benefit plans and deferred-compensation plans generally require you to take benefits when you retire, whether you want the money or not.

Other plans, such as 401(k)s and IRAs, allow you to start withdrawals between the ages of 59½ and 70½, providing flexibility of the amount withdrawn. Thus, if you can, it is typically advantageous to leave that money in the plan to grow tax deferred until a later date.

You must begin taking minimum distributions from traditional IRAs (not Roth IRAs), 401(k) plans

(unless you are still working), and other qualified plans by the time you are 70½.

**Decide whether you want to take a lump-sum distribution or receive an annuity.** This option is generally offered with 401(k) plans, profit sharing plans, and some defined-contribution plans. Your decision should be based on the income tax ramifications of the different options, your personal needs, and your financial ability to handle the money.

If you opt for an annuity, you must decide among various payment options, including life only, which pays you a certain amount until your death; joint and survivor, which will also pay a certain amount to your spouse after your death; and life and period certain, which pays a certain amount for your life or a specific time period, whichever is longer. Your payments are generally taxed as ordinary income when received.

You may like the comfort that comes with annuities, since you are assured of a monthly income without having to worry about investment decisions. Guarantees are based on the claims-paying ability of the issuing insurance company and apply to minimum income from an annuity. They do not guarantee an investment return or the safety of the underlying funds. However, annuity amounts are typically fixed, so inflation can seriously erode the purchasing power of this income over the years.

A lump-sum distribution gives you the opportunity to invest your retirement funds. Thus, you receive the rewards of smart investment decisions, but you can also suffer from poor decisions. Since you own the funds, proceeds can be left to your heirs after death.

The tax treatment of a lump-sum distribution depends on how you handle the distribution. The

least favorable alternative is to include all the proceeds in your taxable income in the current year, subjecting the proceeds to your top tax rate and possibly the 10% tax penalty, if you are under age 59½.

As an alternative, any portion of your account balance in a qualified plan can be rolled over into an IRA within 60 days. This rollover defers the tax on the distribution and allows it to grow tax deferred until withdrawn. Keep in mind that if you take possession of the funds, your employer must withhold 20% of the proceeds, even if you plan to roll over the entire balance.

You can avoid this provision by having your employer directly transfer the distribution to your IRA. If you are between the ages of 59½ and 70½, you can access the funds as you need them, penalty free, paying only ordinary income taxes as you withdraw funds. Please keep in mind that rolling over assets to an IRA is just one of multiple options for your retirement plan. Each option has advantages and disadvantages, including investment options, fees, and expenses, that should be understood and carefully considered.

**Determine how to withdraw money from your plans.** After going through this analysis, you can decide when to start taking distributions. These decisions will take into account your life expectancy, your tax situation, your current income needs, the expected inflation rate, and your expected rate of return on retirement assets. The calculations can quickly become very complex if you need to evaluate several different plans under several different payment scenarios.

Since the calculations are so important for your retirement, please call if you'd like help with these decisions. ○○○



## Do You Really Need 70%?

**A** general retirement planning rule of thumb indicates that you'll need 70% to 80% of your preretirement income. Many estimates now indicate that may be too little for those who want to live an active retirement lifestyle. But when you realize how much you need to save, it's tempting to question whether you really need even 70% of your preretirement income.

First, you should prepare a detailed analysis of your expected expenses after retirement. How much you will need depends in large part on how you plan to spend your retirement years.

Keep in mind, however, that things seldom go as planned. How can you help ensure that your expenses will be lower? Consider these tips:

✓ **Pay off your mortgage.** Mortgage payments often consume 30% or more of an individual's gross income. Eliminating this expense can drastically reduce income needed for retirement. If you can't pay off your mortgage, consider selling your home and purchasing a smaller one for cash.

✓ **Get rid of other debts.** It's not unusual for consumer debt payments to equal 10% to 20% of an individual's take-home pay. Try to

enter retirement debt free.

✓ **Keep your automobile.** Instead of purchasing a new car every couple of years, keep your current car for as long as it's in good working order. That will eliminate car payments from your retirement budget.

✓ **Look for ways to reduce travel and leisure expenses.** Look for and use senior discounts. Plan activities for nonpeak times, when rates may be lower.

✓ **Consider relocating.** The cost of living varies significantly from city to city and state to state. You may be able to reduce your living expenses substantially by moving to another locale. However, this is more than a financial decision. You also need to decide whether you want to move away from family, friends, and familiar surroundings.

✓ **Work at least part-time.** If you still don't have sufficient funds to support yourself during retirement, consider working at least part-time. Even a small amount of annual earnings can help significantly in funding your retirement.

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*Jennifer*



## Two Types of Diversification

**W**hen you're diversifying within your stock portfolio, there are two types of diversification to consider: horizontal and vertical.

✓ **Horizontal diversification** is holding stocks in, say, one industry. For example, you might own shares in a technology company index. Even though each company in the index faces similar market trends, each is also subject to unique strengths and weaknesses. Again, the principle of horizontal diversification is to mitigate risk. To use our example of the technology index, some of the companies in the index do poorly, but many of them do well — and your gains mitigate your losses.

✓ **Vertical diversification** involves choosing stocks across industries or markets. For example, you might own shares in a technology company, a furniture company, and an energy company (or better yet, their respective indices). Mitigating risk is still your goal with vertical diversification.

In general, the more broadly diversified your stock portfolio is — both horizontally and vertically — the better your balance between risk (losses) and reward (gains).

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## Financial Thoughts

**I**n the class of 2012, 71% of college graduates had student loan debt, with an average loan balance of \$29,400 per borrower. Approximately 41% of college graduates indicated that their jobs don't require a college degree (Source: *The Wall Street Journal*, January 5, 2014).

Currently, 52% of individuals own stocks, down from 65% in 2007 (Source: *Money*, January 2014).

Within the baby boomer generation, the wealthiest 20% of boomers own 96% of all equities held by their generation. Their large net worth could mean sustained high-equity allocations throughout retirement as they consider estate planning and wealth transfer strategies. Baby boomers, on average, allocate 47% of their portfolios to U.S. stocks (Source: *AALJ Journal*, December 2013).

Approximately one out of every four American workers uses 401(k) and other retirement savings accounts to pay current expenses (Source: *REP.*, November 2013).

Approximately 62% of workers between the ages of 45 and 60 plan to delay retirement, up from 42% in 2010 (Source: *REP.*, November 2013). ○○○