

DAILY SOUND



Section: Ask S&B
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Title: Wealth Stages of Life

Dear S&B: As I approach retirement, should I view my wealth differently? Fred – Santa Barbara

Whether you plan to or not, as you age, your psychology toward your wealth will either change or it probably will need to change. The “accumulation” vs. “distribution” stages of life are distinctly different and they often times require alternate perspectives.

During the Accumulation Stage (Pre-Retirement Years) of life, people generally focus on saving and growing their “nest egg.” You are trying to figure out how much you will need in order to be “done” where you no longer need to work. The investment philosophy in this stage of life can many times be very different than in other periods (i.e. more aggressive). Attention is usually concentrated on your job and the family. You are building your lifestyle and accumulating wealth through savings. For people in this stage of their financial lives, the wealth strategies that should be focused in on are:

- Understanding future anticipated “known income sources.” These are usually social security, pensions, rental income, bond income, etc.
- Figuring out future anticipated “known expenses.” These usually consist of mortgage, rent, debts, property taxes, health insurance as well as lifestyle desires.
- Calculating the “nest egg” necessary to fund the expected expense / income gap (if one exists) from the above calculations.
- Determining if additional savings are necessary to accomplish goals.
- Computing the investment rates of returns that are necessary to create the desired nest egg.
- Implementing the portfolio that has a likelihood of accomplishing those goals but within the risk tolerances that you can handle. For example, if the necessary rate or return is 10% in order to accomplish your goals but you are risk adverse, there is a problem that needs to be addressed (i.e. save more, decrease goals, increase risk tolerance, combination approach, etc.).
- Purchasing the proper amount of insurance to help protect your ability to “earn” (i.e. life and disability coverage).

During the Distribution Stage (Retirement Years) of life, this is when a person primarily lives off their savings. The investment philosophy and risk tolerances may be significantly different from years past. It is not uncommon for estates to “level” out in value as people consume a large proportion of their investment dividends, interest income, and gains to support their lifestyle

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needs. For people approaching or living in this stage of their financial lives, the wealth strategies that should be focused in on are:

- Are there gaps between “known income” and “known expenses?” If so, they need to obviously be filled. Since a “paycheck” is no longer coming in, the “nest egg” needs to be the “employer” which is giving you your income. This is a major psychological change for most people (it can feel like an invasion of principal).
- If excess income exists, could those funds be better used for estate planning purposes, family gifting, charitable intentions, enhancing lifestyle desires, building the “nest egg” further, or addressing risk management needs.
- If expenses are higher than known income, the investment portfolio must be allocated to fill that gap as best as possible to account for current day needs as well as keeping an eye on future goals. But be careful, studies have shown that if you pull more than 5% from your portfolio each year (adjusted for inflation), your risks of running out of money 20+ years into retirement can be rather significant.
- Where possible, create a financial and investment plan where at least 90% of known expenses are covered by known income sources. This generally gives people the peace of mind having their savings provide a monthly “salary” to them.

At the end of the day, you are either adding to savings or withdrawing from them. The psychology and implementation plans are often wildly different between the two stages in life. The transition between the two can be tough as it requires a change of perspective. A perspective a person may have been living for 40+ years.

Questions can be submitted to asksb@missionwealth.com or the authors can be reached at www.missionwealth.com.

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