

# Focusing Your Future

Kibble & Prentice

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## Any Way You Slice It

**B**ig or small piece? The way you slice a pie probably depends on your appetite. If you're hungry, you might take a large piece. Or, if you're worried about too many calories or carbs, you might eat a thinner slice.

How you divide your investments among the different types of assets that are available may depend upon your appetite for investment risk. If you're focused on long-term returns, you may choose a higher proportion of stock investments. But, if you're worried about volatility, other investments may be more appropriate.

Dividing your investments among different asset types is the strategy known as *asset allocation*. The amount you put in each type of investment (asset class) will affect the long-term performance of your investments.

### Investment Flavors

Stocks, bonds, and cash equivalent (money market) investments are the

three major asset types that may be available in your retirement plan. In the past, stocks have provided the best long-term returns. But stocks also have a higher risk of short-term losses. (Past performance does not guarantee future results.)

Bonds tend to have lower long-term returns than stocks, but usually are less risky. Cash equivalent investments are the least risky, but also have the least chance of earning returns greater than the inflation rate.

Different asset types may react differently to various market conditions. For example, when the stock market declines, bond prices often rise.

So, when you spread your retirement investments out among the different asset types, you spread out your risk.

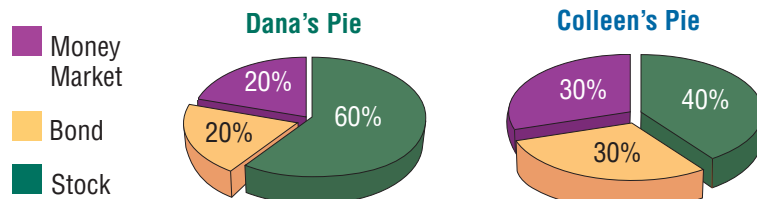
### Slicing Your Pie

Generally, your investment time frame and risk tolerance should factor into how much you invest in the different asset types. The further away from retirement you are, the more risk you probably can handle.

Early in your career you may decide to allocate a larger slice of your assets to stock funds or portfolios to increase your long-term return potential. As retirement draws near, however, you may want a larger proportion of your account in bond and money market funds to help preserve the value of your investments.

## Dessert Sampler

Here's how Dana and Colleen have divided their retirement plan investments. Dana is willing to take more risk to increase long-term return potential.



These are hypothetical examples for illustrative purposes only. The allocations shown here are only samples. The proper allocation for your situation may differ. In applying any allocation to your individual situation, you should consider your other assets, income, and investments (including home equity, savings accounts, and other retirement plans), as well as your investing time frame, needs, goals, and aversion to risk. If any of these factors change, you should review your asset allocation.

Source: NPI

## Get Up to Speed on Your Tax-deferred Savings Vehicle

**W**hen you're saving for retirement, you don't want to fall behind. To get your savings up to speed, contribute more to your employer-sponsored retirement plan.

Contributing more money to your plan *now* could make a big difference in the amount of money you have to live on in the *future*. Plus, making contributions to your plan actually *reduces* the amount of current income tax that you'll pay. So put your pedal to the metal.

### Speeding Up Reduces Your Tax Ticket

You can reduce the amount of federal income tax that is withheld from your paycheck by increasing your retirement plan contribution. Here's how: You don't pay current taxes on any contributions to your plan account. So, if you're in the 25% tax bracket and contribute \$50 a week to your plan, you'll save \$12.50 a week in taxes. And, if you increase your contribution to \$100 a week, you'll save \$25 in taxes. Over a whole year, the tax savings can really add up.

Increased Savings = Bigger Benefit		
Annual Amount Saved in Plan	\$2,600	\$5,200
Number of Years Saved	35	35
Average Annual Total Return	8%	8%
<b>Account Balance after 35 Years</b>	<b>\$448,024*</b>	<b>\$896,047*</b>

\* Amounts are taxable upon withdrawal. This is a hypothetical example used for illustrative purposes. It is not representative of any particular investment vehicle. Your results will be different. Source: NPI

### Tax Detour Gets You to Your Destination

You also are deferring income taxes on the money your retirement plan investments earn. Tax deferral is a lot like a long detour. You won't pay taxes until you withdraw the money, usually after retirement. And, if you speed up your savings, even more of your money can benefit from potential tax-deferred growth.

### Accelerate with Catch-up Contributions

If you're age 50 or over, your plan may allow you to contribute even more than the limit that applies to younger participants (generally \$14,000 for 2005). The maximum catch-up contribution for 2005 is generally \$4,000. Check with your plan administrator to find out how much you can contribute to your plan.

### Race To Receive Tax Credit

Contributing to your retirement plan also may allow you to receive a tax credit on your plan contributions. Whether or not you qualify for the saver's credit depends upon your adjusted gross income (AGI) and your tax filing status. If you qualify, the maximum annual contribution eligible for the credit is \$2,000, and the credit percentage rate is 10%, 20%, or 50%, depending upon your income. So, for example, if you contribute \$2,000 and qualify for a 50% credit, you could save \$1,000 in taxes.

Increased Savings = Reduced Taxes		
Weekly Contribution	\$50	\$100
Annual Amount Saved in Plan	\$2,600	\$5,200
Federal Income-tax Rate	25%	25%
<b>Annual Tax Savings</b>	<b>\$650</b>	<b>\$1,300</b>

Amounts saved in the plan are taxable upon withdrawal. Source: NPI

## ANY QUESTIONS?

**Q.** *I know that paying for health care is a problem for many retirees. How can I prepare for this potential retirement expense?*

**A.** When planning for retirement, some people forget about health care expenses. Instead, they focus on having time for hobbies and traveling. Some automatically assume that their living expenses will be lower once they retire. But health care costs could mean *higher* expenses during retirement. If you don't plan ahead, paying for health care could put a big dent in your retirement savings. Here's how to prepare:

### Plan on Paying

If you plan to retire early, health insurance premiums could be an issue since Medicare won't kick in until you've reached age 65. In 2002, nearly half of retirees ages 55 to 64 didn't receive employer-based health insurance. By the time you retire, that number could be much higher. And, if you have to pick up your entire health insurance tab, the costs could be significant.

Even if you or your spouse have employer-provided coverage, you still should plan on paying some of the cost. In addition to premiums, there could be deductibles and co-payments that you'll have to pay out of pocket.



Keep in mind that medical costs tend to rise faster than the inflation rate. In 2002 (the most recent year for which data is available), the annual growth rate in health care spending was 9.3%. By the time you retire, costs could be a lot higher.

### Gaps in Medicare

While Medicare will provide coverage starting at age 65, it won't take care of all of your health care needs. Many people buy supplemental insurance to help cover their costs.

### Save for Out-of-Pocket Costs

Contributing more to your retirement plan can help you prepare

for *all* your retirement expenses, including health care. Even a small increase in your monthly savings could make a big difference by the time you retire.



## Total Return — An Investment's Bottom Line

When you get your plan statements, pay attention to the section that provides *total return* information. It's important because it gives you the bottom line on how well an investment fund or portfolio is performing.

### The Basics

In investing, the word *return* refers to the amount you earn on the money you've invested. For example, if you invest \$100 and earn \$15 of interest, your return is \$15 or 15%.

To calculate your *total return*, you also need to include how much the investment gains or loses in value. So, if that same investment lost 5% of its initial value, its total return would be 10%.

*Average annual total return* takes compounding and the length of time you hold an investment into account.

### Inside Fund Returns

An investment fund's total return has three components:

**Share Appreciation/Depreciation** — the increase or decrease in the market value of the fund's shares.



**Income** — any interest or dividends earned by fund investments.

**Capital Gains** — the profits earned from the sale of investments in the fund's portfolio.

### Comparing Total Returns

Knowing an investment's total return (or average annual total return) helps you compare that investment to other

investments. You also can compare an investment's return to a benchmark index, such as the S&P 500\*, that tracks the performance of similar investments.

Investments may have periods when they do not perform as well as similar investments or a relevant index. However, that doesn't mean that you should immediately get rid of an investment just because it's had one down period. Take a look at other factors that may affect performance, such as the economy as a whole or a decline in one industry. The investment may soon recover. If an investment does take a long-term turn for the worse, however, it may be time for a change in your portfolio.

So, the next time you receive a plan statement, take a look at your total return to get to the bottom line on how well your investments are performing.



\* Standard & Poor's 500 (S&P 500) Index tracks 500 industrial, transportation, financial, and utility company stocks.