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Retirement planning is a simple matter of arithmetic

ROB RIKOON

Real Money

This article is directed to all readers out there including me, who occasionally think about how they are going to retire. I often wonder how I can get everything done in my life that I thought I would do when I was a kid. Well, maybe we are all kids at heart, believing and hoping we will have the chance to do something meaningful or fulfilling or just plain fun. What does this have to do with Real Money? Well, most things today have something to do with money, or at least most of the things that we talk about have some relationship to finance.

So, why not think seriously now about our retirement plans? After all, there is no time to waste. The question of achieving our unique brand of self-fulfillment might be a matter of when we can afford to stop working. Or perhaps it is a question of when we can move on from our occupations, which may have turned out to be less glamorous than we thought they would. Readers who belong to the ranks of generation "X" or "Y," as those who follow baby boomers are called, will have help in planning their retirement. Through political influence, baby boomers may whip the Social Security system into shape by privatizing part of it, and refocus the retirement plans of major corporations by creating more flexible benefit formats. Readers over the age of 60, who may have ridden the long wave of prosperity into retirement, are hopefully reaping the rewards of the biggest bull market in history. Unfortunately for us middle-agers, we might have to figure out this issue for ourselves.

You don't have to be a rocket scientist or a mathematical genius to figure out how much money you will need to save in order to retire. In the following paragraphs, I will walk you through one process for figuring out a secure retirement plan. The good news is it is never too late to start. The bad news is that it may involve some sacrifice for your future security. No one said it was going to be easy.

To create a comfortable retirement, the one thing you will need, along with your health, is money. Think about your current situation. You work hard, week after week, and then end up spending most of your take-home pay on necessary bills. Once you retire, you will still have to contend with many of these expenses. Where will the money come from to pay them — Social Security? Savings? Perhaps you will be among those lucky enough to receive an inheritance.

Most people are comforted by the thought that they can

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count on Social Security benefits to provide for their "dream" retirement. By now, it should be clear that to have a great retirement, you have to take matters into your own hands. One good place to begin is first to ask yourself and then answer the following two questions:

- How much money do I need to accumulate for my retirement?
- What is the best way to save for my retirement?

Let's tackle the first question:

Generally, people need somewhere between 60 percent and 80 percent of their pre-retirement income. To determine what you will need, make a list of your annual expenses. Next, estimate how your expenses would be different after retirement. Certain expenses will be less, or even nonexistent, while others may be higher. For example, child-care costs should be much lower and, hopefully, your home mortgage will be paid off. However, you might need additional income to cover travel costs, health insurance, or medical expenses. Divide your estimated annual retirement income by .05. The result is an estimate of the amount of savings you will need by retirement. This retirement-planning model assumes that 40 percent to 60 percent of your portfolio is invested in stocks (for growth) with the balance in bonds (individual ones, of course).

Historically, an asset mix of 60 percent stocks and 40 percent bonds has resulted in an 11.1 percent long-term annualized return (1949-1998). A mix of 40 percent stocks and 60 percent bonds has given 9.5 percent return per year. Your income withdrawals, at 5 percent annually, will be made up of a combination of interest, dividends, and capital appreciation. Let's walk through an example:

$60,000	Annual income need at retirement at age 60
.05	Withdrawal factor (5 percent)
$1,200,000	Savings needed at retirement

So, what is the best way to save for retirement?

One of the best ways to save for retirement is through tax-deferred retirement plans. Not only do you receive a tax deduction for your investment, but you also receive tax-deferred earnings and, in some cases, matching contributions. Please don't confuse this as an endorsement of tax-deferred annuities, as they have very high costs that make them a poor investment choice.

To illustrate how powerful retirement plans can be, let's look at the possible results of a weekly contribution of just $90.

Time:	20 years	30	35	40
Invested:	$93,600	140,400	163,800	187,200

Account values based on these earning rates:

	20 years	30	35	40
7%	$191,859	442,076	646,948	934,292
8%	$214,166	530,165	806,443	1,212,385
9%	$239,429	637,919	1,009,526	1,581,290

If you spend a few minutes studying this chart, you will notice that one of the most important elements in building a large retirement account is time.

The sooner you get started, the easier it is to accumulate a large sum of money. Adding constant amounts of money to a stable, diversified investment is called "dollar-cost averaging." It is also a very good way to avoid the natural tendency to try to time or outsmart the market's fluctuations. Why not start building your "dream" retirement today? Old-fashioned thriftiness, discipline, and patience today will go a long way towards guaranteeing your financial peace of mind tomorrow.

Rob Rikoon is the president of Rikoon Investment Advisors, an investment-management and financial-planning firm in Santa Fe (Tel: 989-3581). His recent book, Managing Family Trusts: Taking Control Of Inherited Wealth *(John Wiley, 1999), is a guide for investors desirous of holistic financial health.*