

Why Even the Joneses Can't Keep Up

A special report about working to achieve your retirement goals and what might be keeping you from getting there.

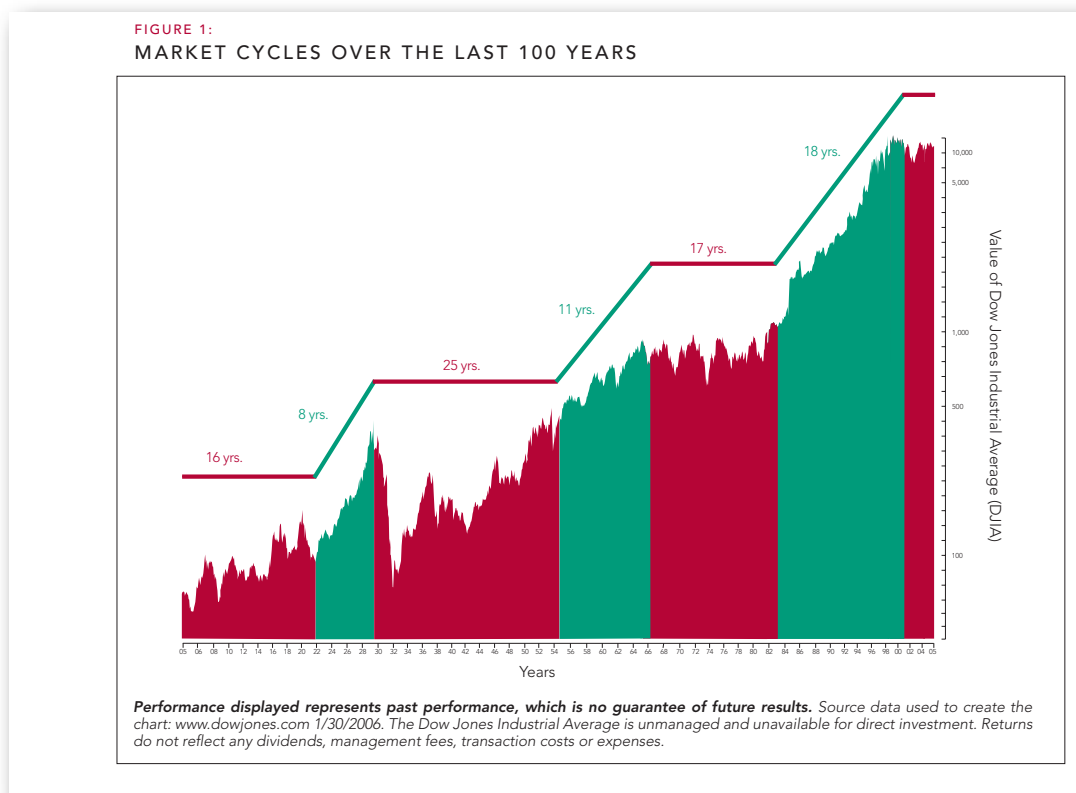
By Charles C. Scott, AIF®

We all know about trying to keep up with the Joneses. It's an adage that's been around for ages. We admire their apparent success. We wish we could be more like them. We may even be a little envious or jealous of what they seem to have. But what if, just maybe, things aren't quite what they appear to be?

Let us take a closer look at Mr. Jones as he navigates the path to retirement success.

Before we get to his story, please look at the following charts. Taking a short historical peek back into the past when looking at the investment markets makes a big difference in trying to put things in the proper perspective.

The first chart gives a 100+ year look at the investment markets. It is from a report titled "Essential Portfolio Theory" from Rydex Investments.



As you can see from the red areas and the green areas, there are times when it looks like “up” is the only direction and other times when the markets go nowhere. It is important to note that the up market

cycles and flat market cycles each last for several years. The term for these kinds of long term market cycles is “secular bull markets” and “secular bear markets.”

It is our opinion that we are currently in a “secular bear market” which started in early 2000. How long it will last is anyone’s guess, but knowing where we are now plays a very important role in helping make the wisest investment choices.

This next chart is from Yahoo Finance and gives a more current look at the prices of the S&P 500 over the last 9 years. It hit a high in early 2000, went down and then up, before topping out in late 2007 and heading down again. This current short-term volatility looks very intense, but when you spread it out over a longer time frame, it takes on a completely different perspective.

As I said in the beginning, having some sort of historical perspective is very important to the rest of this story.



So let’s meet Mr. Jones at the start of the year 2000. He’s a 45 year old, successful professional who would like to retire at age 65. He currently has a half million dollars (\$500,000) in his company 401(k) plan. He consistently contributes \$15,000 per year to the plan and is assuming a modest 11% return in the future on his retirement funds based on what’s been happening in the “markets” for the last few years.

Using these assumptions, his portfolio should be worth about \$4.5 million at retirement age. He’s planning to conservatively withdraw 3% of this retirement fund every year in order to give him a “salary” from his retirement funds of about \$136,000 a year.

All of this makes sense, seems conservative based on then-recent history, and puts Mr. Jones on a comfortable path. That is, until the “secular bear market” hits in the spring of 2000. Lacking the proper historical point of view, Mr. Jones continues to invest from his “offensive playbook” only, maintaining the “buy and hold” philosophy he’s been told is the way to invest.

As we visit him at the end of 2008, he is 53 years old and only 12 years away from his desired retirement. For the past nine years he has added his \$15,000 (totaling \$135,000). However, the “market” has taken much of those contributions away. His account is worth approximately \$412,000.

Take another look at the performance table of the S&P 500 on the preceding page.

Mr. Jones “bought and held” and rode the market down from 2000 to 2002 but had the intestinal fortitude to hang on and ride it back up from 2003 into 2007 and now through 2008.

Beginning of 2000:	
<u>Current Situation:</u>	
Age:	45
Expected Retirement Age:	65
Account Value:	\$500,000
Expected Annual Rate of Return:	11%
Average Annual Contribution:	\$15,000
<u>At Retirement (Age 65):</u>	
Projected Account Value:	\$4,500,000
Annual Withdrawal at 3%:	\$136,000

Current Picture 2008:	
<u>Current Situation:</u>	
Age:	53
Expected Retirement Age:	65
Account Value:	\$412,000
Expected Annual Rate of Return:	11%
Average Annual Contribution:	\$15,000
<u>At Retirement (Age 65):</u>	
Projected Account Value:	\$2,000,000
Annual Withdrawal at 3%:	\$60,000

If Mr. Jones had just kept his money in cash, without earning any interest, he would have about \$635,000 today.

However, today his retirement outlook is drastically different.

His projected account value is now approximately \$2,000,000, or less than half of what he had planned on. Instead of drawing a professional’s “salary” from his portfolio, he will be receiving only about \$60,000 per year.

Mr. Jones is now faced with some difficult choices. If he wants to get back on track to attain his retirement nest egg of \$4,500,000 he’s going to need to make some drastic changes.

One thing he could do is increase his annual contributions to more than \$160,000 per year. That’s obviously more than is allowed to go into his 401(k).

Or he could leverage his account and shoot for investment returns of over 20% per year. That’s crazy!

Or he could increase his retirement age to 74 and work the extra 9 years he has probably wasted by not getting out of the way of bad investment markets.

Alternatively, he could take a new job in “retirement” at age 65 with a \$75,000 salary to supplement his shortfall from his original plan.

None of these alternatives is particularly appealing. After getting over the initial shock that he’s not going to be able to afford a “Ritz-style” retirement, he is coming to terms with the idea of a more “Days Inn-style” lifestyle. First and foremost for him should be the idea of making sure he doesn’t lose any more ground. It’s also important to understand that Mr. Jones hasn’t done anything wrong. He’s been saving and investing the way the mainstream media has advised. However, that way of investing does not always work. Unfortunately, these are times when it isn’t working.

If this story hits home in any way, perhaps it’s time to take a look at a different way to manage the investments in your 401(k) plan. We may be able to help. We would love to talk to you about it, but before we do that, please take a few minutes and go through the following steps:

- 1) check your 401(k) balance as of 1/1/2000,
- 2) check your 401(k) balance as of 12/31/2008,
- 3) subtract out your own contributions over that time,
- 4) subtract out the matching funds from your company for the same time period, and
- 5) calculate how much you are up or down from start to finish.

This will give you the results of the performance of the investments that you have chosen over the last 9+ years.

We have no idea what the results might turn out to be, but if you are not happy with the answer, we can help. We provide personalized, pro-active, professional advice for participants in retirement plans. We are a fee-only firm. We do not sell any products. We have no hidden agenda. We would love to talk to you about this if you feel it is appropriate.

Thank you for taking the time to read this report and we hope that you have found it helpful. We would like to extend a special thank you to Dorsey Wright and Associates for introducing us to Mr. Jones and his retirement reality.

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