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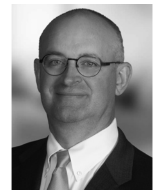

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Should You Retire Early?

Not so long ago, most working people wanted to retire early. But the prospect of retiring at a young age and depending on your investments for income for decades is suddenly a scarier thought. Should you even think about retiring early?

Much will depend on your definition of early retirement. If your definition means to quit working completely so you can travel extensively and pursue expensive hobbies, then you might want to postpone those plans for a while. However, if your definition means to change careers to work part time at a less stressful job, cut back on your living expenses, and only take minimal amounts from your retirement savings until Social Security and pension benefits kick in, then your early retirement plans might still be feasible. If you want to seriously consider early retirement, review these tips:

✔ **Make sure you know what you're going to do with your time.** When you're working full time, it seems like you could fill all your waking hours with the things you don't have time to do. But if you're used to a fast-paced life, can you really expect to spend the next 20 to 40 years of your life just puttering around the house and golfing? Make sure you have concrete plans to fill your days, so you don't get bored early in retirement. If possible, ask your employer to give you a short sabbatical. That way, you can see how well you'll adjust to retired life. If you like it, you can go ahead and retire. If you find yourself quickly bored, you haven't given up your job.

✔ **Calculate your numbers carefully.** You want to be sure your retirement savings and other income sources, such as Social Security and pension benefits, will support you for what could be a very lengthy retirement. When calculating how much you need for retirement, be very conservative. Bump up your expected expenses by 5% to 10%, add a few years to your life expectancy, reduce

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Bonds – AKA Fixed Income

I wrote the article that follows six years ago. At that time, I had never seen yields consistently increase during my entire career! This has changed. The silver lining of this otherwise negative market development is that going forward, clients can now earn a meaningful return on the bond component of their portfolio.

In 1984, I was a rookie stock broker for Merrill Lynch. Broker was an appropriate term because I really was new to the business with no advice to offer, only investment products to sell. But I had a finance degree from Lehigh University, so I had learned a little bit.

One of the things I realized was that interest rates were very good so I decided to sell bonds. In fact, I wanted customers to buy long bonds, the longer the better. Treasury rates were over 15%. "Lock that rate in," I kept saying, but you could not believe how hard it was for people to commit to long term bonds. Why lock in when you can get a short-term rate for the same 15%?

I countered that rates were historically high but my customers had experienced rate increases for the last 10 years. Why would they stop going up? In fact, I even lost an account because the accountant told the client that they were crazy to lock in 15% for 10 years, as they did with the bond I sold them.

Looking back, it seems crazy. But you know what, it has been happening nonstop for my entire 32-year career. I now consider myself an advisor because I don't work for commissions anymore and because I have earned several designations and a very uncommon Masters in Financial Planning. So at this point, I get paid whether clients buy a long bond or a short one, but no one ever wants to buy a long bond.

Perhaps it is because people struggle so much with bond math. When you buy a bond, you can sell it at any time, like a stock. You lock in the income from the bond (why we call it fixed income) but the price of the bond will fluctuate,

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Should You Retire?

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your expected return by a couple of percent, and increase your inflation expectations. Don't expect to draw more than 3% to 4% annually from your retirement investments. Now, can you really afford to retire early?

✔ **Cut back on your standard of living.** Unless you're very wealthy, you probably won't be able to retire early and afford fancy cars, expensive homes, and other luxuries. Cutting back your expenses now will serve two purposes. It will provide more money to save for retirement and it will reduce your living expenses now and during retirement. Don't just look at obvious ways to cut back, such as reducing how often you dine out or taking your lunch to work. Look at more drastic measures, such as moving from your current home to a smaller one or comparison shopping for items like auto and home insurance.

✔ **Work at least part time during retirement.** Even a small amount of income after retirement can go a long way in helping to fund your retirement expenses. Consider working at a less stressful job, starting your own business, or turning hobbies into a paying job. This can give you time to pursue travel, hobbies, and other interests, while helping to fund a long retirement.

✔ **Move to a less expensive city.** The cost of living in different cities across the country and in different countries can be vastly different. If you live in a city with a high cost of living, moving to a different location can dramatically lower your living expenses. However, this is not just a financial decision. You need to consider whether you'll be happy living somewhere else, away from family, friends, and other ties.

While retiring early certainly seems more challenging than it did even a few years ago, that doesn't mean it can't be done. But you do need to make sure your plans are realistic before retiring. Please call if you'd like help developing a plan for early retirement. ❍❍❍

Raising Financially Responsible Children

Although you'll have to wait a good while before they'll thank you for it, teaching your children to be financially responsible is one of the best gifts you can give them. Fortunately, most of the lessons can begin while they are still very young.

Lesson #1: Appreciation for the value of money — Money has to be earned — and when it is, they better appreciate its value. Those of us who had a job like babysitting or mowing lawns in the summertime might remember when a new video game was no longer just $50 of Mom and Dad's money, but the equivalent to 10 hours of work. Perhaps you recall hesitating to purchase a soda for $1.50 and opting to visit the water fountain because you were saving your allowance. Prices are just abstract numbers until time and effort has been spent to generate those coins and bills.

Consider forming an allowance-for-chores policy to teach your children about money management early on. You pay for the basics, but if they want the extras, they will have to save up and use their own money. It's an important lesson on its own but will also help them focus their priorities and feel a sense of pride in accomplishment.

Lesson #2: Saving the money they earn — Teach them to save a portion of what they earn from the get-go. This habit will make it much easier for them to not spend their entire paycheck as well as leave their savings intact when they are on their own. You may need to encourage them firmly at first, with a fixed percentage or minimum amount. As they grow older and their savings increase, they will need less guidance as they come to appreciate the readiness of available funds for a special purchase.

Lesson #3: Setting goals and staying on track — Helping your children set short- and long-term goals is a key part of getting them to stick to a savings strategy. Most children are not that excited by slowly rising dollar amounts, but when a certain dollar amount represents a desperately desired new toy, their focus sharpens considerably. Make a chart to show them how much they would need to save over a specific amount of time to have enough for their goals… and make sure to reward them when they stay on track.

Lesson #4: The nitty-gritty of a balanced budget — Show your children the day-to-day workings of adult finances. Go through the line items on your budget (with real or simplified amounts) and reveal your own percentage of savings for short- and long-term goals. You can explain the benefits of autopay, managing a bank account online, minimum balances and fees, and even how to fill out a check (some landlords and city utilities still require checks for bill payment). It may seem mundane to you, but depending on the child's age, the desire to be grown up could increase their interest level and make abstract concepts more understandable.

Lesson #5: Understanding debt and loans — When young adults are first exposed to credit cards, they may not understand that purchasing things on credit or taking out a loan ends up costing more money. Explaining how interest can work for you (in a savings account) and against you (in a loan or on credit) can keep them from making bad decisions. Above all, modelling financial responsibility in your own life can help them form the basis for a lifetime of good money habits. ❍❍❍

10 Ways to Boost Savings

Saving money doesn't have to be hard. By embracing some simple lifestyle changes or taking full advantage of tax perks and other savings incentives, you can easily boost the amount of cash you save. Here are some ideas to get you started.

✔ **Take advantage of savings perks:** If you contribute pretax earnings to a 401(k) plan or IRA, you're saving money beyond your actual contribution amounts. Say your monthly gross pay is $5,000 per month. You currently don't contribute to a 401(k) plan. You decide to start saving 3% each month (or $150) into your employer's 401(k) plan. This $150 comes out of your paycheck pre-tax, which means that even though you're saving $150, your paycheck only shrinks by $112 — in other words, you've saved $38 a month on taxes, or $456/year.

Another way to save? Make sure that you're contributing enough to get your employer match, since this is a great way to increase your savings without actually shrinking your take-home pay.

✔ **Get your benefits:** Your employer may offer benefits that could save you money. Flexible spending accounts are common benefits that allow you to set aside pretax income for out-of-pocket medical expenses. Also common are programs for commuters that let you pay for parking or public transit on a pretax basis. Some employers even offer discounts on gym memberships or other services. Take the money you save by participating in these programs and use it to boost your savings.

✔ **Cut recurring expenses:** Monthly subscription boxes, streaming entertainment services, gym memberships that you don't use — these regular costs can add up. While some may be worthwhile, trimming the fat in the area of recurring expenses can help you save more. Keep what you use and drop the ones you don't use.

✔ **Buy generic:** Do you always buy the name-brand version of the product? If so, you might be wasting money. In many cases, the generic version of a product is just as good — if not identical — as the pricey, branded version.

✔ **Make it automatic**: Not sure where your money goes each month? Automate your savings so that you don't have to think about setting aside extra cash.

✔ **Be generous:** If you itemize your taxes, make sure you're keeping track of all your charitable donations — from checks you write to the value of goods donated.

✔ **Cut one habit**: Do you indulge in daily soda or an expensive coffee drink? Cut the habit (or, if that's too hard, limit it to two or three times a week). Set aside the money you would have spent.

✔ **Repair, don't replace:** It's easy to toss a slightly worn or damaged item and buy a new one to replace it. But many of the items we throw out can actually be repaired. By purchasing quality items and taking good care of them, you'll likely save yourself money in the end.

✔ **Use coupons:** Clipping coupons may seem distinctly old school. Fortunately, you can now take advantage of coupon savings without having to spend an entire Sunday morning sorting through newspaper inserts. When shopping online, always do a quick search for online promo codes. Or sign up for your favorite grocery store's rewards program.

✔ **Review your insurance premiums:** Raising deductibles or bundling policies could save you a bundle. Also, make sure you actually need the insurance you have — cell phone insurance and warranties are often a waste of money. Finally, make sure you're getting all the discounts you qualify for, like car insurance premium reductions for being a safe driver or homeowners insurance discounts for having an alarm system.

Please call for help analyzing your budget and identifying ways to cut your expenses and save more of what you earn. ❍❍❍

Bonds – AKA Fixed Income

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like a stock. If we ignore details like call features and assume that the issuer is solvent, then the only variable is the coupon rates on bonds like the one you bought.

If you bought a 10-year Treasury, its market value on any given day is impacted by the direction of rates on new 10-year bonds. If rates subsequently increase, who would want to buy the bond you have that has a lower rate? You would have to lower the price to get a buyer.

Conversely, if rates go down, now your bond looks like a good deal. You can raise your price and sell it for a profit. Bond math is that simple. The income (coupon) is fixed, the price and the yield are not fixed. If the bond is held to maturity and the issuer does not default, the yield over the time you owned it will be exactly what you signed up for. But if you sell before, the price and the yield change.

Let's now consider if you should sell that bond when the price goes up. If the price has gone up, your yield has gone down. This is the part where everyone always loses me. You locked in a certain income when you bought, not the price. Yield is just the income divided by the value. If the value goes up, your yield goes down.

Let's say you bought a 10-year bond for $10,000 at 4%. Lucky you. You get paid $400 per year. Now two years go by and 8-year bonds are yielding 2%. Why compare to an 8-year bond? Because that's what it has become after you hold it for two years. Your bond is now worth quite a bit more. It would be worth about $11,600. Since it is still worth $10,000 at maturity in eight years, you have to figure that your yield has gone lower for two reasons.

First, the $400 per year divided by $11,600 yields less than it did when the bond was worth 10,000. Yield is $400 divided by $11,600. That is what is called the current yield. It is not that meaningful because we have to consider the second reason why the yield is less than 4%. The second reason is that the $11,600 bond is going to be worth $10,000 in eight years when it matures. That is, it will lose almost 2% per year in price.

Year	Bond Value	Interest Earned	Total Return	Yield Earned
1	$10,000			
3	$11,600	$800	$2,400	11.56%
10	$10,000	$4,000	$4,000	4.00%

Note that over the last eight years, returns were a lot less than 4% after making 7.36% in the first 2 years. Examples of what can go wrong are illustrated below.

Combining the two concepts, current yield and the loss of capital that will occur, gets you the yield to maturity. Yield to maturity (unless the bond is callable) is the only yield that matters. It tells you what the real yield is on your bond.

Back to the question, should you sell your bond, the bond that started with 4% and is now worth quite a bit more? The yield to maturity on your bond going forward is 2%, the same as rates for new bonds. Your yield changed because your price changed. You may want to sell the bond if you can find something that yields more than 2%. Perhaps you would consider a longer bond or a different type of bond? But you have to first accept that your yield is no longer 4%, that it is 2%.

If you remember one thing from this, it should be that the income is fixed, the yield and the price are NOT.

Bond Strategies

Assuming you are looking at bonds of similar quality or rating (the major rating agencies are Moody's and Standard & Poor's), then maturity becomes the focus for bond buyers. Bonds come in maturities from a few days to 30 years (there are a few rare exceptions that are even longer). For the vast majority of time, the longer the maturity, the higher the rate, all things being equal. If you knew rates were going to stay the same or go down, you would buy the longest bond you could find because you want the higher rate. But we don't know that rates are going to stay the same or go down. If they go up and you want to sell, you will have to take a loss. One of the reasons we tend to like 10-year bonds is that we typically get almost as much yield as a 30-year bond but for much less risk.

Let's look at an historical example.

If you bought a 10-year treasury in January, 1966, you would have gotten 5.13% yield. Two years later 8-year rates were 6.13%. Your bond would have gone from $10,000 to $9,353 for a loss of $647. You would have made money because your income would have been over $1,000 for the two years. You could hold it for another eight years to get the $10,000 or you could sell it for the loss.

Year	Bond Value	Interest Earned	Total Return	Yield
1	$10,000			
3	$9,353	$1,026	$379	1.93%
10	$10,000	$5,130	$5,130	5.13%

You also could have purchased a 30-year treasury for about 9%. Two years later, a 28-year bond would yield about 11%. Your bond would now be worth $8,273. Your loss would be $1,727. You would have lost about as much as you made. It would have been better to have purchased the first bond.

Year	Bond Value	Interest Earned	Total Return	Yield
1	$10,000			
3	$8,273	$1,800	$10,073	0.36%
10	$10,000	$9,000	$9,000	9.00%

These were real life examples. The point of this is to show that buying a 10-year bond in a rising rate environment was not nearly as good as buying a 30-year bond.

Another reason that we like 10-year bonds is that they tend to go up in value if rates stay the same. How is that possible? If you buy a 10-year bond and hold it two years, you now have an eight-year bond. Since eight-year bonds tend to yield less than 10-year bonds, and because bonds appreciate if the comparable bond has a lower yield, all things being equal the bond would go up in price if 10-year bonds stayed the same and if 8-year bonds stayed the same.

They call the strategy of trading a bond back out to its original maturity, "Riding the Yield Curve." I learned it in college 33 years ago. The idea would be to go back to the 10-year maturity after holding for a number of years (usually more than two).

In full disclosure, investors have to be aware that there may be trading costs and trading costs may make it impractical to ride the yield curve.

Let us know if you would like to discuss bonds further, or discuss any investments in your portfolio.

Sincerely,

John B. Burke

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Financial Advisor