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Seniors: Safe Investments vs. Stock Market Risk!

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On July 1, 2009, it will be halfway through a frightening 2009. After the 2008 Wall Street Crash, the stock market reached its 12-year low in March 9, 2009 and then rebounded by 30-40% (depending on whether one looks at the Dow-Jones, S&P 500, or Nasdaq Index). On 10/9/07, the Dow Jones Index reached its peak of 14,164; on 6/25/09 it closed at 8472. Despite the recent rally in the stock market it's still a 40% drop from the peak. Seniors face the dilemma of low interest rates in most safe investments vs. stock market risk.

Typical case study: At the peak of the stock market in October, 2007, the portfolio was worth \$1 million. Today, it's worth \$600,000. Assume that the married couple is 70, retired, and has \$35,000/year of Social Security and/or pension income. They are currently spending \$70,000/year. Before the crash, they thought there would be no problem in obtaining the extra \$35,000/year of income from their investments. On 6/25/09, Bloomberg.com lists these current rates:

CD's: A 5-year CD averages 2.65% and a 1-year CD pays 1.78%. If their entire \$600,000 was invested in CD's, they could get \$10,680-\$15,900 of annual income. As long as your CD is covered by FDIC insurance, your principal is safe.

U.S. Treasuries: A 10-year Treasury note yields 3.57% and a 30-year Treasury bond yields 4.35%. Their annual income would be \$21,420-\$26,100. Your principal is safe, backed by "the full faith and credit of the U.S."

Municipal Bonds: Average yields are 3.54% for a 10-year bond and 4.86% for a 30-year bond. The annual income would be \$21,240-\$29,160. However, if future interest rates increase, the principal price of the bond will drop.

Stock Market: Because the 3 investment options listed do not generate enough income, many seniors leave their money in the stock market. I ask seniors who see me to imagine they have a bag of cash that contains their whole life savings. Then I ask them: If a taxi dropped you in front of a Las Vegas casino or on Wall Street, what percentage of your life savings would you want to risk losing? The typical answers range from 0-25%.

Unfortunately, many seniors say: "I've lost so much money in the last 1.5 years that I have no choice but to leave all or most of my money in the stock market and pray that it recovers to its peak." They are risking 70-95% of their life savings because stocks represent such a high percentage of their entire liquid assets, and it scares them silly.

Cash Flow Accounts: This fairly new concept may be a reasonable compromise. For a 70-year-old investor, they typically pay 6-7% of immediate cash flow. If one can delay taking income, the lifetime income goes up by 6-8% each year. This is modeled after the Social Security concept, where for each year one waits (after age 62) to take benefits, one's lifetime income increases by 6-8% per year.

The cash flow accounts guarantee income for life and one is guaranteed to not lose principal. If one dies, any



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remaining principal in a cash flow account is available for one's spouse or kids. In contrast, after one takes lifetime income from either a company pension or an old-fashioned annuity, the entire principal disappears and there's nothing left for one's heirs. This is a major difference.

In conclusion, low yields on CD's, U.S. Treasury's, and municipal bonds influence many seniors to take much more risk than they want to in the stock market. Cash flow accounts may offer a safe option to consider.

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