Financial planning in uncertain times

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Objectives

Manage volatility

Create an emergency plan

Learn to take advantage of taxes

Create an exit strategy that outlives you

Planning for Uncertain Times

Job Transitions

- Career change
- Job loss
- Retirement

Market Changes

- Corrections
- Recessions
- Bear Markets

Emergencies

- Health issues

Major repairs

- Legal issues
- Accidents
- Pets

The Importance of Financial Fitness

Weathering uncertain times

is not about deciding how to invest your money

It’s having a sound financial strategy that coordinates aspects of your financial life

The five pillars of financial protection

A strong foundation is key to weathering a financial storm. Building one involves:

Protecting against economic crises

Developing tax-saving strategies

Establishing liquidity and control

Creating a lifetime income stream you can’t outlive

Ensuring your heirs receive their inheritance efficiently

L.I.F.E. Design

Lifetime

Inventory

Financial

Evaluation

L.I.F.E Design: Inventory

Salaries

- Take-home vs. gross
- Current vs. future
  - Future: Social Security, pensions, asset withdrawal, etc.

Savings

- Emergency funds, savings, investment accounts, IRAs, 401ks, TSPs (stocks, bonds, mutual funds, CDs, etc.)

Real Estate

- Current home value vs purchase price
- Mortgage interest rate, principal, and interest amount
  - Are you paying PMI Insurance?
- Rental property – current value/depreciation

Debt

- Balances
- Minimum payments
- Interest rates
- Remaining payments

Insurance

- FEGLI – How many times your salary?
  - Are you planning on keeping it into retirement?
- Life
  - Term or permanent
  - Cash value
  - Current benefit vs future
  - Premiums
- Long-term care – premiums and benefits

Wills and trusts

L.I.F.E. Design: Evaluate and Formulate

- Evaluate your inventory for strengths and weaknesses
- Formulate a plan for long-term success that can weather uncertainty
  - This plan should include:
    - A budget – understanding cash flow needs
    - Debt reduction and eliminating interest on debt
    - Improving credit
    - Saving, investing, and earning interest for retirement
    - Estate planning – wills, trusts, longevity planning, etc.

Build Your Budget

How to reach your budget goals

Determine your net income

This is the actual amount of money received after state federal, social security, and other taxes have been deducted

Categorize all expenses

Daily living, monthly, quarterly, and yearly bills and fees

Evaluate your spending

Review all credit card and checking account transactions for at least the past 60 days

Sort by merchant or description and identify where you can reduce or eliminate costs

Standard Guideline:

You need to be living on 70-75% of your net income, and saving 25-30%

Three Phases of Wealth

Contribution

- Having an income
- Saving

The Fragile Decade

- Using time as an asset
- Five years before and after retirement

Distribution

- Creating a stream of income for expenses in retirement

Planning for uncertainty is different in each phase

Contribution Phase

During this phase we are working, earning, saving, and perhaps at the same time, raising children

Maintain flexibility

- Liquidity of money is imperative
- Eliminating debt is crucial
- Utilizing dollar cost averaging is key

Plan for uncertainties that may derail finances

- Job loss
- Health/legal crisis
- Unexpected expenses

Contribution Phase

Eliminate mandatory payments – a best practice

Pay off debt

Make a list of debts, sort them by lowest balance owed, pay off the smallest debt first, and pay the minimum on larger debts

Once the smallest debt is paid off, "snowball" the payments into the next biggest debt

Re-Structure debt

Initiate zero-balance transfers

Refinance your home

Don't be afraid of a 30-year mortgage

You can always turn a 30-year into a 15, but not the other way around

A 30-year mortgage can lower your mandatory minimum payment while offering you the flexibility to save more

Contribution Phase

Save money

Establish an emergency fund

At least six months of mandatory expenses: food, mortgage, etc.

Take out money only for an emergency (job loss, unforeseen expenses)

Keep things liquid

Don’t put all your eggs in one basket

No magic investment will make you rich overnight. Saving money efficiently is more advantageous

Contribution Phase

Key ways to save:

Qualified Accounts: TSP, IRAs, 401ks, etc.

- Take advantage of matching programs offered by the government
  - **Example:** TSP will match 5% after you invest 5%
- Consider looking at other liquid options or a Roth IRA
- Money saved in these accounts have restrictions
  - **Example:** There's a 10% penalty for withdrawing money prior to age 59½
  - **Exceptions:**
    - ROTH IRAs allow you to withdraw the principal penalty for free at any time
    - TSPs/401ks allow you to take a loan up to 50% of the value

Non-qualified accounts: Savings, brokerages, insurance, etc.

- These accounts can be a great way to save for access to money
- First, establish an emergency fund, then designate monthly flow toward investment accounts that can be accessed without penalties

Contribution Phase

Get insured to circumvent emergencies

Types of insurance

- Property and casualty
- Long term care
- Life insurance
- Umbrella

Permanent life insurance – useful in several ways

- The cash value for everyday purchases
- The ability to take a loan against yourself
- Protection in case of death and disability

The Fragile Decade

Your *Contribution phase* strategies still apply once you enter the *Fragile Decade.* In addition:

- Protection becomes even more paramount
  - Consider shelters for your money that have low volatility – specifically TSPs, 401ks, IRAs, etc.
- Set yourself up for the next **30** years
  - Consider long-term care **before** being prone to age-related issues
  - During this phase, economic corrections are a real threat
    - Utilize conservative types of investments
      - Lifecycle funds
      - Annuities (one of the most misunderstood areas of finance)
      - Insurance
      - Volatility controlled indices
  - The last one to two years of savings need to be used efficiently!
    - The last year of savings doesn't make or break retirement – the first 39 do

The Distribution Phase

All planning should have the distribution phase in mind

In this phase, a new set of risks evolve

- The sequence of returns risk
- Long-term care
- Tax and estate planning

The Distribution Phase

The Sequence of Returns

Retiring at the Beginning of an up market			
Year	Investment Value	Withdrawals	Return
0	$100,000	N/A	N/A
1	$103,000	$5,000.00	8.00%
2	$109,330	$5,000.00	11.00%
3	$124,009	$5,000.00	18.00%
4	$136,371	$5,000.00	14.00%
5	$147,735	$5,000.00	12.00%
6	$156,031	$5,000.00	9.00%
7	$168,195	$5,000.00	11.00%
8	$178,332	$5,000.00	9.00%
9	$185,816	$5,000.00	7.00%
10	$190,106	$5,000.00	5.00%
11	$177,502	$5,000.00	-4.00%
12	$158,302	$5,000.00	-8.00%
13	$129,557	$5,000.00	-15.00%
14	$116,783	$5,000.00	-6.00%
15	**$105,944**	$5,000.00	-5.00%

Average Return: 4.0%

Retiring at the Beginning of a down market			
Year	Investment Value	Withdrawals	Return
0	$100,000	N/A	N/A
1	$90,000	$5,000.00	-5.00%
2	$79,600	$5,000.00	-6.00%
3	$62,660	$5,000.00	-15.00%
4	$52,647	$5,000.00	-8.00%
5	$45,541	$5,000.00	-4.00%
6	$42,818	$5,000.00	5.00%
7	$40,816	$5,000.00	7.00%
8	$39,489	$5,000.00	9.00%
9	$38,833	$5,000.00	11.00%
10	$37,328	$5,000.00	9.00%
11	$36,807	$5,000.00	12.00%
12	$36,960	$5,000.00	14.00%
13	$38,613	$5,000.00	18.00%
14	$37,860	$5,000.00	11.00%
15	**$35,889**	$5,000.00	8.00%

Average Return: 4.0%

Despite having the same average annual return, **Investor Blue** has $70,055 more than **Investor Green** due to their sequence of returns.

retireone.com/sequence-of-returns-risk

The Distribution Phase

Consider leveraging of assets

Are you going to spend ALL the money in your TSP and IRA?

Most of us can live off of 4-5% of our assets (The Prudent Person Rule)

If this holds true, a vast majority of the money that is in our accounts will never be touched

This is the money that you want to use to protect against catastrophic events such as large market swings, long-term care, and increased taxes on inherited assets

Long-Term Care

70% of adults need long-term care at some point in their lives

National averages run anywhere between $8,000-$12,000 a month

Incorporate long-term care protection through:

- Traditional insurance – FLTC
- Hybrid insurance
- Asset-based long-term care

Estate Plan

Don't wait - estate planning is for the living

Will

Three parts to a will:

- What happens to your assets
- Who can make financial decisions for you
- Who can make medical decisions for you

Trust

A legal document (separate from a will) that ensures your assets get distributed exactly the way you want

Focus on Good Financial Sense

We can't control market volatility, so control what you can

We can control:

- The way we structure our debt to be efficient
- The way we leverage current assets – especially our mortgage
- Elimination of the sequence of returns risk through financial products
- Estimated guesses of our taxation
- Our exit strategy

Summary

Plan for unforeseen events in these four areas:

- Tax
- Estate
- Insurance
- Assets

Seek guidance from financial professionals

- CPA
- Lawyer
- Insurance
- Money manager

Earning more interest by picking the right investment **is not a strategy!**

RESOURCES

Book

The Money Manual: A Practical Money Guide to Help You Succeed on Your Financial Journey

Tonya B. Rapley, 2019

Websites

Click here for The Institute for Financial Education

Click here for PracticalMoneySkills.com

Click here for MyMoney.gov – Life Events

Articles

Click here for 6 Major Financial Steps of Your Life

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