The Changing Face of Retirement

By

David Ferrucci and Paul Ferrucci

THE FERRUCCI COMPANY

Table of Contents

Challenges of the New Retirement 3
Beyond the Numbers 3
The Three Stages of Retirement 4
Going It Alone 5
1. Overconfidence 6
2. Risk Aversion 6
3. Representativeness 6
4. Regret 7
Concluding Thoughts on Going It Alone 7
The Wealth Strategy Solution 8
Asset Allocation 8
Modern and Post-Modern Portfolio Theory 10
Enter the Wealth Strategist 12
Client Orientation 12
Expertise 12
Management 12
Discipline 13
Process 13
Longevity 13
Finding Your Wealth Strategist 13
The Wealth Strategy Process 14
The Discovery Phase 14
The Investment Plan 15
Making the Commitment 17
Making Progress 18
Pulling It All Together 19
About the Authors 20
About the Ferrucci Company 20

Challenges of the New Retirement

RETIREMENT USED TO BE EASY–OR AT LEAST IT SEEMED THAT WAY. YOU reached age 65, received a gold watch and went off to "rest" on your pension and nest egg.

But that somewhat mythical scenario has become altered beyond recognition, particularly for the affluent and their families. The fact is that retirement is a dynamic period of life with distinct stages, each of which requires its own financial solutions and smooth transitions from one to the next. Retired individuals face new challenges and opportunities that may alter their lifestyle and financial requirements dramatically.

As a nation, we are retiring younger and living longer. Today, the average retirement age in the U.S. is 62, with life expectancies well into the 80s-which means that we have less time to accumulate assets to support a retirement that could stretch into 20 or 30 years. In 1940, notes Neal E. Cutler, a respected researcher in the field of finance and aging, there was a 7 percent probability that a 65-year-old would live to age 90 or longer. By 2000, this probability had more than tripled, to 26 percent. What's more, simple pension benefits have been replaced by a complex web of income sources. Beyond that, the investment marketplace has exploded with a myriad of financial instruments while an entire publishing industry has evolved to try to make sense of them all.

Affluent retirees who wish to achieve the freedom to do what they want, provide for their family and foster some kind of meaningful and lasting legacy have particularly complex financial needs. At the same time, however, they may not wish to involve themselves in the complex details of financial management.

BEYOND THE NUMBERS

The financial side of retirement is intimately entwined with the emotional: Few retirees are satisfied with merely remaining active as long as possible (though that is a prime concern) but often look forward to plunging into new, highly rewarding experiences such as community involvement or a further business venture.

A survey conducted in 2000 by the National Council on the Aging found that only 54 percent of people aged 65 to 75 were completely retired, 25 percent said they were both retired and working full-time or part-time, and another 21 percent said they were not retired. While many of the respondents from this broad sampling continue working out of necessity, a significant number, particularly among the affluent, choose to work because they enjoy it.

Retirement is becoming a richer period in people's lives. We are healthier longer, and few people think of retirement as a time to rest.

Rather, it is a time to connect-or reconnect-with your family, your community and, in many cases, lifelong dreams. In short, it is a time to stay engaged with the world and, where possible, make a lasting difference in the lives of others.

AARP offers this list of objectives for retirement, none of which, by the way, involve sitting on the porch in a rocking chair (although that remains an option!):

* Spend more time with family.
* Travel to new places.
* Devote yourself to volunteer activities or philanthropy.
* Pursue interests that you've stored on your "back burner" for years.
* Start a new career.
* Establish a new business.

The choices you make regarding how to enjoy your retirement define the assets you need to achieve those objectives. "Although retirement and money go hand in hand, planning activities is probably more important," writes Jim Yih, author of Mutual Fundamentals. "What you are going to do with your time will often dictate how much money you need. Far too often, people get this mixed up because they focus on the financial side first."

THE THREE STAGES OF RETIREMENT

Although the style and shape of retirement is as varied as those enjoying it, it is helpful to consider three distinct phases that a retired person might pass through and what issues one should consider when planning for them. As we examine each phase individually, keep in mind that this progression is not a staircase but a slope and that "age" is very much a subjective concept.

1. Active Phase

This represents the beginning of retirement, or even "pre-retirement" (when you may be drawing income from assets while continuing to work). This phase may result in a very high cost of living-maybe even more than before retirement-while you realize those dreams of travel, philanthropy or spending time in multiple homes.

Age range: 50-75

Income Sources: Investment capital, company retirement plan, company stock, business ventures and ownership interests

2. Less Active Phase

This phase results in a comparably reduced cost of living: It tends to last the longest, and it also more closely resembles the historical model in which expenses are lower than they were before retirement. This is also the most predictable phase financially, as income needs tend to vary less than during the active phase.

Age range: 70-85

Income Sources (in addition to above): Tax-advantaged assets

3. Care Phase

The third stage of retirement is the result of a gradual or sudden decline in health to the point where long-term care is required, and can result in the highest cost of living overall. Lifestyle expenses continue at their same rate, however, a long-term care situation can easily add $50,000 or more per year of additional expenses per person.

Age range: 85+

Of course, it bears emphasizing that everyone is different: Your active phase may extend longer, or you may never need the additional assistance

that some people require. Nonetheless, it is worth planning adequately for each of these stages. As we've already mentioned, planning starts not with the question, "How much money do I need?" but rather, "What do I want to make of my retirement?" That's why it is important to consider retirement as a lifestyle issue, rather than simply as a financial matter.

Jim Yih calls this Life Retirement Planning, encompassing eight areas:

1. Health and Fitness
2. Financial Comfort
3. Social Relationships
4. Home and Location
5. Leisure Interests
6. Mental and Emotional Health
7. Intellectual Spirit
8. Spirituality

Notice that financial issues are only mentioned once, though it's plain to see they are intricately tied to every one of the eight areas. The phrase "financial comfort" is instructive, as well: It reflects the importance not of money per se, but of how you feel toward your money.

GOING IT ALONE

As a sophisticated investor and steward of your family's financial well-being, you may feel the responsibility of managing your retirement on your own. After all, the individual investor has never had so much access to information, or such a broad range of financial products from which to choose.

But that daily bombardment of information can actually be an impediment to careful planning and decision making. For instance, when a financial magazine touts "The Ten Hottest Stocks" of the moment on its cover, is the motive to promote a solid financial strategy individually tailored to help you reach your life goals? Of course not. Simply put, it is to sell magazines.

That's not to say that information is valueless. Quite the contrary-high-end research and analysis is a critical component in creating a plan focused on achieving your goals. Institutional investors such as pension funds and endowments, with billions of dollars to invest, know this. That's why they employ teams of portfolio strategists composed of analysts, academics and other experts. These strategists select the most appropriate asset classes to invest in, determine the optimal mix of these classes and, perhaps most important, select and monitor the investment managers who oversee those asset classes. Until recently, however, even affluent families had no access to these sophisticated resources. But that, as we'll see below, is beginning to change.

The onslaught of information isn't the only peril that investors face. The others come from simple human nature. In fact, a whole branch of science has evolved to study the interaction between human behavior and economics. The field of behavioral finance applies psychology to the investment process. Two of its pioneers, Daniel Kahneman and Vernon Smith, received the Nobel Prize in 2002 in recognition of their work.

What Kahneman, Smith and others have learned is that as humans, we tend to act in ways that are not necessarily in our financial best interest. Instead, we respond irrationally, guided

by emotions such as fear and greed. These manifest themselves in multiple ways, of which four traits are particularly significant:

1. Overconfidence

Overconfidence refers to the tendency of human beings to think we're smarter or more able than we really are. This tendency comes to the fore in the practice of market timing: trading stocks or other investment vehicles in an attempt to outperform the market.

But the market turns out to be extremely efficient in determining a stock's actual value. Any public information about a stock has already been compensated for in its current price. This is the basis of the Efficient Market Theory, developed by Eugene Fama of the University of Chicago in the 1960s.

Numerous studies have shown that efforts to beat the market actually have the opposite effect over the long term. Take the technology bubble of the last decade, in which millions of investors saw their portfolios shrink by 50 percent or more: In 2000, according to the Wall Street Journal, investors continued to pour $4.1 billion into tech investments for six months after the NASDAQ peaked. What's more, anyone trying to outpace the market will likely trade frequently, which has also been shown to be a futile-and costly, both in commissions and in tax liability-practice. In fact, research indicates that only 2 percent of actual long-term return is derived from timing the market-and that even the choice of individual stocks nudges long-term return a mere five percent. Later, we'll explore the crucial strategic element that lies behind the remaining 93 percent of an investment's return: asset allocation.

2. Risk Aversion

Another critical component of behavioral finance is risk aversion-which might better be described as loss aversion, since it occurs even when risk is a neutral factor. Kahneman and Amos Tversky found that investors place different importance on gains and losses. In one famous experiment, the researchers presented groups of subjects with various hypothetical situations. They found that their subjects responded differently to a situation with the same monetary result, depending upon whether it was framed as a gain or a loss. In short, they learned that we are more upset by a loss than we are happy with an equivalent gain. It stands to reason, then, that investors will do more to prevent loss than they would to achieve gain, even if the results are the same. By extension, an investor seeking to minimize loss may, in fact, reduce the opportunity for gain.

3. Representativeness

Representativeness is a fancy, multisyllabic term for that caveat familiar to anyone who has read an investment prospectus: "Past performance is no indication of future results." But we as humans always use past experience to try to predict the future. We look for recent patterns in an attempt to determine a trend-that is, in part, a definition of intelligence. It works pretty well for evolution: "That bison is charging. I'd better throw the spear or get out of the way." But it doesn't help much with investments.

Investors often look at short-term events-a run-up of technology stocks, for instance-as that charging bison. (Got to buy!) This becomes manifest in the bandwagon mentality: If the market (or a particular hot stock) is going up, up, up, we don't want to miss out on the party. The only problem is, by the time we've heard about it (that is, discovered an upward trend) the moment to invest has passed.

This characteristic can also lead an investor to hold on to a winning stock longer than is prudent. Some investors develop an emotional attachment to an investment that has served them and their family well with strong returns over the years. (In many cases, it may be an investment in their own company's stock.) But stocks don't reward loyalty. Just because an investment has done well in the past doesn't mean it will do so in the future.

4. Regret

Another crucial human trait that impacts investing is that we're very quick to judge ourselves if the outcome of our decisions aren't immediately positive. So we might unload an investment after a decline, even if we bought it originally for a good reason (as part of an asset allocation strategy, for instance). Equally, some researchers feel that fear of regret can lead to bad decisions: holding on to a loser too long for fear of owning up to having purchased it in the first place.

CONCLUDING THOUGHTS ON GOING IT ALONE

So there you are, looking forward to or already enjoying a rich, active retirement in which your financial needs evolve all the time. You are faced with an overabundance of financial information-which, by its nature, emphasizes short-term returns-and a nearly infinite choice of investment vehicles, not to mention other choices to make-regarding estate planning, taxes, business valuation and other areas-closely tied to your financial well-being and that of your family. Overseeing this complex web of issues could easily be a full-time job, and it still wouldn't provide the best-in-class service you would want for yourself and your family. There ought to be a better way.

The Wealth Strategy Solution

RECENT DEVELOPMENTS IN THE FINANCIAL SERVICES INDUSTRY OFFER a unique solution to the dilemmas that affluent investors face: a holistic approach that draws from best practices in a variety of fields to fulfill the needs of investors as completely and efficiently as possible. That may involve a diverse range of offerings, including investment management, retirement, estate planning, tax planning and asset protection.

According to Russ Alan Prince, a leading expert on the private-wealth industry, this broad approach is a three-part equation: **brokerage** (financial transactions), **investment management** (the types of services you'd expect from a typical financial planner) and **advanced planning.** It is this third component that truly distinguishes wealth strategy from more traditional forms of financial service. Prince breaks this item down into four main components:

Wealth Enhancement: Tax management strategies to reduce the bite on investment proceeds.

Wealth Transfer: The complex issues surrounding estate planning

Asset Protection: Strategies to safeguard your objectives from family-changing events, such as disability and death (This would also include developing plans to minimize your risk from third parties.)

Charitable Giving: Handling your philanthropic initiatives in a way that helps you and those you wish to benefit

Simply put, this approach helps you find solutions to the challenges you face, no matter what traditional areas of finance they fall into. It can encompass everything from valuating a private business to setting up charitable trusts, and it often draws upon the expertise of not one but many professionals in a number of fields.

That is not to minimize the value of investment management, only to say that your invested assets make up one slice of the pie. Nonetheless, a successful wealth strategy begins with sound investment management. For that reason, it bears a bit more examination.

ASSET ALLOCATION

The foundation of investment management is financial analysis: simply put, a thorough examination of your current financial situation, your tolerance for risk, your goals and the appropriate mix of asset classes you must hold to achieve them. There are three basic components to financial analysis: your goals (for example, to retire with 100 percent of your current income), the horizon (the length of time you have to achieve your goals) and the amount of capital you must have to reach those goals. At the same time, you should be minimizing risk

to increase the probability that you will achieve your goals. Financial analysis is a no-nonsense approach that makes no promises about the future. It is, instead, a measure of the probability that these three components-goals, horizon and investment-will produce the desired results.

The result of this analysis is the creation of a portfolio that mixes asset classes in such a way as to maximize the probability that you will achieve your goals while keeping risk within a tolerable range. This is known as asset allocation. While we'll elaborate more below, suffice it to say that by combining asset classes according to certain criteria, you can create a portfolio that will grow at a rate to meet your goals with a high degree of probability.

Again, the term "probability" is key here. Sound investment strategy does not attempt to predict the future in the way that market timing does. Attempting to time the market assumes that you will know the exact right time to buy and sell an individual investment vehicle-in other words, that you'll know how it will behave in the future. Instead, asset allocation takes into consideration that the future is unknowable, and that the best we can say about it is that given the long-term history of different asset classes, we can calculate the probability of their movement under certain market conditions and their overall performance in the long term. For retirees or those looking forward to retirement, this translates into greater peace of mind.

In the same way that many investors begin their retirement planning with the question, "How much do I need?" most people instinctively ask their financial advisors, "What stocks (or other vehicles) should I buy?"

But that's not the most important question, either. Consider, instead, "How will I allocate my assets among the major asset classes to maximize my chances of achieving my goals?" It is that allocation-and not the individual stocks or funds you own-that will determine your portfolio's ability to deliver the results needed to achieve the goals you've set for yourself. As we'll see below, there are only a small number of financial professionals who are positioned to answer that question in a way that is aligned with their clients' interests. How important is asset allocation? Well, if you recall, security selection represents five percent of performance variability, while market timing represents two percent. By contrast, asset allocation has been shown to produce a full 93 percent of the variations in returns.

The question of how to distribute your investments over various asset classes is not something you ask once and then forget about. Even though asset allocation is a long-term strategy, it is hardly static. For one thing, your situation and goals could-and often do-change. And as you approach and enter retirement, your investment horizon becomes a moving target. For instance, your horizon for purchasing a vacation home or establishing a philanthropic trust won't be the same as that of providing for your and your spouse's long-term care. In fact, as you pass through each stage of retirement, your time horizon will continue to shift, and your asset allocation should reflect those changes.

And even if your goals don't change prior to

retirement, your portfolio most certainly will. As your portfolio grows, it will become "unbalanced." Those asset classes that grow faster will take up a disproportionate share of the portfolio, while the slices of the pie represented by slower-growing assets will shrink.

To keep this from happening, you must systematically rebalance your portfolio-that is, sell some of the faster-growing assets and acquire more of the slower ones. Doing so has been shown to keep risk in check (by reducing volatility and exposure to overvalued areas) and enhance overall wealth (by enabling you to systematically "buy low and sell high," since you sell those classes that have increased in value and buy those that are lower in value).

MODERN AND POST-MODERN PORTFOLIO THEORY

The point, as you've probably gathered already, is not to beat the market (we've already shown that's nearly impossible to do) but to increase the probability that you will achieve those goals that are most important to you. This is the basis of Modern Portfolio Theory (MPT), created in 1962 by Harry Markowitz, another Nobel Prize winner (1992). Maury Seldin, of the Homer Hoyt Advanced Studies Institute, explains that MPT "holds that diversification of assets may increase returns at given risk levels, or alternatively, may provide the same returns at reduced risk levels."

Modern Portfolio Theory is built on three components: historical returns, historical risk and correlation coefficients. While the truism "past performance is no indicator of future results" still holds true, Markowitz found that different types of investment vehicles, when examined over a long period of time, do exhibit predictable long-term returns and risk levels (i.e., volatility). What's more, each asset class responds differently to different market conditions. When stocks rise, for example, bonds tend to decrease in value.

> *The relationship between these classes is their correlation coefficient. Two classes with a correlation of +1 (perfect positive correlation) rise and fall in perfect harmony, while two with a correlation of _1 (perfect negative correlation) go in exactly opposite directions. The purpose of diversification then is to combine classes with low correlations, to minimize risk. They do not have to rise and fall in complete opposition, but only respond differently to various market environments. Over the long run, for example, equities deliver returns of about 5 percent in excess of inflation (real return), while bonds produce 1 percent to 2 percent. Cash produces zero real return.*

The operative phrase here is "long run." Between 1926 and 2002, the S&P 500 has had an average growth rate of about 10 percent. Yet only four times in all those decades did it actually grow anywhere close to that rate.

Recently, a highly technical refinement of modern portfolio theory has taken hold. Labeled Post-Modern Portfolio Theory, it is based on the fact that risk and return are not perfectly symmetrical. The theory attempts, then, to identify an optimal mix of assets to reduce downside volatility without limiting upside potential.

Sound investment management begins with

choosing asset classes that have low correlation coefficients in relation to one another, but it certainly doesn't end there. Each investor, with his or her own financial situation, goals, horizon and risk tolerance, needs his own particular mix of these assets. Additionally, as we have seen, portfolios must occasionally be rebalanced in order to operate at optimum efficiency. Portfolio strategists for institutional investors may rebalance in two ways: strategically or tactically. Strategic rebalancing, described above, means keeping the portfolio within the confines of its original design, that is, the proportions of the various asset classes within it. In strategic allocation, then, the portfolio's target asset weightings stay more or less consistent.

Tactical allocation, on the other hand, establishes permissible ranges for each asset class and seeks to shift the target mix whenever opportunities arise that might boost overall returns or reduce overall risk. This requires a high degree of discipline. That's why it is crucial to set permissible ranges for each asset class and not exceed them.

Enter the Wealth Strategist

SO FAR, WE'VE FOCUSED ON JUST THE INVESTMENT PORTION OF comprehensive planning, to the exclusion of other elements. That is because of all these areas, investing is the one that even affluent investors might tackle on their own. (After all, you can't very well insure yourself or draw up complex legal documents on your own.) But while portfolio analysis would seem to address all the downsides of individual investment, it ignores the elephant in the living room: time. The research, analysis and implementation required for a sound wealth strategy actually requires more, not less, time than the typical approach. What's missing is one trusted advisor to manage those personal assets that you absolutely do not want to lose while getting the risk-adjusted return necessary to achieve your goals.

The ideal Wealth Strategist would be able to bring to the table expertise from multiple sources, institutional-level research and strict discipline. This manager should be entirely focused on the well-being of the client, a commitment that is reflected in both a compensation structure and outlook. Let's take a closer look at each of these elements:

Client Orientation

Wealth Strategists are first and foremost oriented toward their clients. This is different from other types of financial services professionals, whose compensation structure may lead to a conflict of interest. Brokers, for example, are transaction or product oriented. They are usually paid by commission, either on each transaction or, sometimes, on particular investment products. Additionally, brokers (and mutual fund managers) are often judged by-and sometimes compensated based on-the quarterly or annual returns they generate. At first glance, this seems only fair, except when you consider that short-term returns are of far lesser significance than long-term strategy.

Unlike Wealth Strategists, these professionals may not have a defined process through which they take their clients and may not offer wealth-planning services that include tax and estate planning. They also may not have a profile of the people who benefit most from their services. As a result, many top brokers end up with hundreds of clients, large support staffs and an inability to meet with their clients on a regular basis.

Expertise

A Wealth Strategist serves as the quarterback for a team of experts, from lawyers to insurance agents to portfolio managers. The Wealth Strategist's focus remains on the client, while he takes advantage of best practices by delegating details to other experts, who can focus 100 percent of their time on their areas of expertise.

Management

The asset management portion of wealth strat-

egy involves preparing a client's Investment Policy Statement (more on that below) and includes tax optimization, rebalancing, reporting and administration.

Discipline

In his seminal work, Manias, Panics and Crashes: A History of Financial Crises, economist Charles Kindleberger offers this scenario of the typical market tumble:

> *What happens, basically, is that some event changes the economic outlook. New opportunities for profits are seized, and overdone, in ways so closely resembling irrationality as to constitute a mania. Once the excessive character of the upswing is realized, the financial system experiences a sort of "distress," in the course of which the rush to reverse the expansion process may become so precipitous as to resemble panic.*

This might sound familiar to anyone who experienced the tech bubble of the late 1990s, but it could also describe the Nifty Fifty of the 1970s, the South Sea real estate bubble in the 18th century or the Dutch tulip craze of the 17th century!

By creating and adhering closely to an Investment Policy Statement, a Wealth Strategist can offer a high degree of discipline when behavioral finance might produce negative results for an individual investor.

Process

A Wealth Strategist is able to maintain a client focus as well as a disciplined strategy by adhering to a documented process of determining his client's needs and goals, creating a plan to meet those goals and reporting regularly on its progress, revising the plan as the goals or the client's financial situation changes. The section below explores this process in greater detail.

Longevity

Finally, a Wealth Strategist is in it for the long haul. A central tenet of the advisor-client relationship is that it is ongoing and built on trust.

FINDING YOUR WEALTH STRATEGIST

The choice of a Wealth Strategist is a critical one. You should be comfortable delegating to him the issues that directly impact your financial security and that of your family. Consider the following criteria. A Wealth Strategist should

- Have been in practice for 10 years or more.
- Have relationships with other professionals, such as lawyers, accountants, insurance experts, business consultants and others who can add value for you.
- Have an intimate knowledge of his clientele's challenges and needs. Many Wealth Strategists specialize in working with identifiable niches-corporate executives or owners of closely held businesses, for example-providing specific groups of people with their ideal Wealth Strategist. His "ideal clients"-those he actively seeks to work with-should be people like you.
- Limit his number of clients in such a way as to allow him the time necessary to build a sound relationship with you and really understand what is important to you.
- Work on a fee-only rather than a commission basis.
- Make it clear that he has the client's best interest in mind.

This last is difficult to quantify, but not difficult to understand. You should go with your instinct. You might consider entering the interview with a list of issues that are important to clients. This could include the following:

* Frequency of contact: How often does the Wealth Strategist meet clients, speak with them on the phone and communicate by email? (Quarterly meetings, at least for the first two years, are recommended.)
* Personal rapport: Do you feel that you can have a good working relationship with the Wealth Strategist? After all, this is the beginning of what ought to become a long-term collaboration.
* Time, patience and attention: Is the Wealth Strategist spending enough time with you, explaining issues and fully answering questions?
* Perhaps most important: Does the Wealth Strategist listen to your concerns, goals and situation?

Because it is the job of a Wealth Strategist to listen carefully, it is the responsibility of the client to voice his or her concerns, wishes, questions and goals. Additionally, in order to prepare a comprehensive plan, a Wealth Strategist must have a clear picture of the client's current situation.

THE WEALTH STRATEGY PROCESS

The Discovery Phase

In the first meeting or two, you should expect a Wealth Strategist to ask a wide variety of questions that might fall into the following six broad categories. Asking is only half the equation, though. Make sure he listens to and understands your answers.

1. **Your values and overarching goals**

   This is at the heart of the discussion. What are your personal and financial goals? What is important about money to you? What do you want it to achieve? What concerns do your goals raise?

2. **Your relationships**

   A Wealth Strategist needs to know about your personal relationships-with your spouse, your children, your extended family and your community. What concerns do you have for them going forward? What goals do they have for the future?

3. **Your Assets**

   This discussion is not only about your investments, insurance policies, real estate and other assets, but also your attitude toward them. Do finances confuse or intimidate you? What is your biggest concern about your portfolio? What was your best investment? Your worst?

4. **Your Advisors**

   As the coordinator of your advisory team, a Wealth Strategist should find out how you prefer to interact with lawyers, accountants or even such informal advisors as family members. This team must work well together. If you do not have a full complement of advisors, your Wealth Strategist should recommend appropriate professionals with whom he has working relationships. Finally, your Wealth Strategist should become your "go-to" person, freeing you of the time-consuming task of managing multiple relationships.

5. **Your Way of Working**

   How often and by what methods do you like

to communicate? How involved do you like to be in the investing process? A Wealth Strategist should present options and recommendations to you for approval to whatever degree you prefer.

6. Your Interests

Finally, a Wealth Strategist should engage you as a person and learn the details that round out your life: what sports you play or follow, what you read, your hobbies, your ideal vacation, which charitable causes you support and, of course, the details of your financial and personal goals. After all, this is how you will want to spend your retirement.

The Investment Plan

Once you have completed the initial discovery process with a Wealth Strategist, you should expect him to follow up with a meeting to present an investment plan tailored to your needs. The investment plan is essentially an agreement on how your money will be managed. Remember that so far, you have not made a commitment to work with the Wealth Strategist and vice versa. This meeting will be an important factor in your decision to proceed.

The investment plan is at the heart of an ongoing advisory relationship: This plan will serve as the road map that will maximize the probability that you will achieve everything that is important to you and your family.

This is a deeply personal relationship, but it is also a professional one. It is important to remember that your Wealth Strategist's job is to be just that: an advisor, not merely a conduit for what you want. (To take a contrasting example, a stockbroker may simply execute a client's orders, without regard to how they may fit into the larger scheme.) The advisory relationship can give you real peace of mind knowing that someone is on your side, looking out for your best interests and those of your family.

You should expect three things from the investment plan meeting:

1. The Wealth Strategist should walk you through the investment plan, step-by-step. Though it can be a technical document, it should be written in terms that you understand and that your Wealth Strategist can easily explain.
2. Your Wealth Strategist should solicit-and address-any concerns or questions you have about the investment plan. You may like some parts of the plan and not others. Be sure the Wealth Strategist understands the modifications you are looking for and incorporates them into a rewrite.
3. The Wealth Strategist may ask you for a commitment to move forward. This is a reasonable request, but one you must consider carefully. Make sure that you've asked all the questions you have about the investment plan, and that they've been adequately addressed. At a later date, depending on your time frame and circumstances, the Wealth Strategist should schedule a "mutual commitment" meeting. Take the time you need to be certain you are comfortable enough to move forward.

The investment plan defines in writing your financial objectives, the funds available for investment, the investment methodology, the

strategy that the Wealth Strategist will use to help you reach your objectives and the level of risk you're comfortable with. It ensures that your Wealth Strategist understands your goals and objectives, and it serves as a guideline for you to benchmark your progress each year. Perhaps most important, it helps to keep you on a sound long-term course through short-term market "turbulence"-the daily ups and downs, the effects of which can be minimized through the careful allocation of assets.

Components of the Investment Plan

Every investment plan should include the following six points:

1. **State your needs, objectives and values clearly and concisely.**

   Near-term goals may include large purchases early in retirement or income during part-time or volunteer employment. Long-term goals can be anything from early retirement to establishing a sound estate plan. An important goal is ongoing financial security-that is, an investment portfolio that provides the income necessary to maintain or improve your lifestyle into the future.

2. **Establish the expected time horizon for your investments.**

   As we've already seen, an important criterion your Wealth Strategist uses when choosing investment instruments is the time horizon. Equities, for instance, require a minimum investment period of five years to minimize the effect of short-term volatility. A shorter horizon-say, for near-term expenses-would suggest short-term fixed-income investments.

3. **Determine the rate-of-return objective and select the asset classes.**

   Your Wealth Strategist chooses a mix of investment classes using the principles of Post Modern Portfolio Theory. This mix reflects your goals and time frame while minimizing risk.

   Choosing investment classes based on goals versus simply striving for the maximum return (which incurs the maximum risk) is at the heart of planning. It accounts for future uncertainty rather than relying on market forecasts. Yet, even sophisticated investors tend to focus on their rate of return rather than their long-term objectives. Working with a Wealth Strategist provides you the necessary discipline to overcome this natural human tendency.

4. **Define the level of risk involved.**

   Asset allocation and rate of return determine the level of risk that an investment holds. Broadly speaking, risk is directly related to growth: The higher the risk of an investment, the higher the potential growth (and, of course, potential volatility). Risk, then is something your Wealth Strategist must manage, rather than eliminate, in the process of generating the returns necessary to meet your goals. At the same time, you must understand and be comfortable with the level of risk you adopt. The last thing worth losing sleep over is a dip in the market. Adhering to a sound strategy through market volatility means greater peace of mind.

5. **Document the investment methodology your Wealth Strategist uses.**

Simply put, the investment plan should outline the logic behind your Wealth Strategist's investment strategy: how he allocates your assets and why. It should describe both the strategic allocation-the long-term investment strategy based on your goals-and the tactical allocation, which "fine-tunes" the relationship between asset classes.

6. **Establish a strategic implementation plan.**

   Creating an investment road map is an essential step to maximizing the probability that you will meet your goals. But it is only the first step. A trusted Wealth Strategist, responsible to you alone, is in an ideal position to decide how best to implement your portfolio. The investment plan should establish the means for making disciplined adjustments to the portfolio as needed and provide a benchmark to measure results.

Making the Commitment

After the Wealth Strategist presents the investment plan and answers any immediate questions you have, you should consider scheduling a follow-up meeting before implementing the plan. Take the plan home. Reread it at your own pace and in a place comfortable for you. Make a list of any additional questions you may have. This is an important step that should not be rushed. When you meet with your Wealth Strategist again a few days later, fine-tune the plan if necessary and confirm your mutual commitment to working together.

When you sit down for this meeting, be sure to raise those additional questions and ask for any other clarification you feel you need. As before, make certain that your Wealth Strategist answers your questions clearly and to your satisfaction. At this point, your Wealth Strategist will ask you to commit to the investment plan and execute the documents he has prepared for you. If you are satisfied that this is the person you would like to work with, you should do so.

Buyer's Remorse

There's nothing quite like putting your signature to an official document to raise the nagging feeling of "buyer's remorse." This is simply a variant of the regret that can so often derail well-meaning investors.

As we've seen, the most powerful source of buyer's remorse can be the financial news media. It is important to keep in mind that the media is in the business of selling magazines or advertising time on television and radio. They are not in the business of offering sound, personalized financial advice or of being held accountable for what they write.

So as you go out and are exposed to the financial media, try not to pay attention to the "investment pornography" that focuses on headline-grabbing short-term returns ("This Year's Top Mutual Funds!" "The Hottest Stock on the Market!") rather than long-term strategic planning. You might even consider canceling any subscriptions you have to investing magazines. After all, you will have hired your own personal Wealth Strategist who knows your situation, your goals and your resources as well as what's really important to you.

Great Gains Come in Spurts

Another source of anxiety for investors is the

market's volatility. To get higher rates of return, you frequently have to take some additional risk, and risk means volatility. (Remember that your investment plan incorporates risk based both on your tolerance of it and on your goals.) It's human nature to be happy when your portfolio is up one month and concerned when it's down the next. As we've seen, this makes it likely that you might even want to sell when you're down or buy when you're up. But the uneven nature of investment gains is an unavoidable part of attaining your investment goals. As an example, just missing the best month out of each calendar year over the past 75 years would have resulted in a drastically lower return than you would have experienced by staying invested throughout the period.

In other words, stay the course. If, on average, the majority of investment returns are concentrated in only one month out of each year, you could spend a lot of time questioning why you've hired a Wealth Strategist. Remember, you've hired him not just to make you money, but also to help you make smart decisions about your money so that you achieve all that you want to achieve in your life.

Making Progress

Finally, your Wealth Strategist should establish a schedule–say, quarterly–for regular progress meetings. These are critical points of intersection for you and your advisor to touch base, where he can review your progress toward your goals, discuss any rebalancing he recommends and keep tabs on your evolving financial situation.

Pulling It All Together

YOU'VE WORKED HARD FOR YOUR RETIREMENT, WHICH YOU deservedly look forward to as a rich, rewarding period of your life. The great news is that we're living longer, healthier lives and remaining more and more active in our later years. The bad news is that the financial marketplace has exploded with a bewildering array of products and services that do little to focus on your specific circumstances and needs.

The solution lies in planning and executing a comprehensive wealth strategy for the various stages of retirement that meets your current needs and maximizes the likelihood that you will achieve your goals and those of your family. It requires discipline, foresight and technical skill.

What it shouldn't require is all of your time and energy. By working with a skilled Wealth Strategist, you can leverage the expertise of a team of professionals while delegating the day-to-day oversight of your financial affairs to a trusted advisor. The result? More time and greater peace of mind to enjoy everything that is most important to you.

ABOUT THE AUTHORS

David L. Ferrucci

David is a managing partner of The Ferrucci Company. He has spent more than 15 years honing his expertise in coordinating successful wealth strategies for affluent families. He is passionate about building lifelong relationships with clients and adding significant value to their families' lives.

David holds a B.A. from Trinity College. He also earned an M.A. from Columbia University, where he focused on the relationship between personal finance and family dynamics. David is currently pursuing a second master's degree, from Trinity College, concentrating on wealth strategies for affluent families.

David lives in Essex, Connecticut, with his wife, Michele, and their children, Madeline, Ella and Nicholas.

Paul V. Ferrucci

Paul is a managing partner of The Ferrucci Company. He has over 15 years' experience in helping families make smart decisions about their money. He has developed expertise in analyzing the full spectrum of a client's financial situation and crafting a personalized plan to help the client pursue his or her overarching goals. As such, he is the chief architect of our clients' investment plans.

Paul graduated from Trinity College and holds a graduate certificate in financial planning. A firm believer in staying abreast of current financial theory, Paul is currently pursuing his M.A., also from Trinity, concentrating on wealth strategies for affluent families.

Paul lives in Essex, Connecticut, with his wife, Jennifer, and their children, Andrew, Ben, Charlie and Hanley.

ABOUT THE FERRUCCI COMPANY

The Ferrucci Company develops comprehensive wealth strategies for affluent families.

The Ferrucci family has been helping clients manage and protect their wealth for three generations. Peter Ferrucci, Sr., was an investment advisor with one of the country's largest financial services firms for over 30 years. With a vision of providing highly personalized and unbiased financial guidance, his son, Peter Ferrucci, Jr., followed him into the business and founded The Ferrucci Company in 1977. Today, Peter Jr.'s sons, David and Paul, own and manage The Ferrucci Company, working diligently to uphold the family's legacy and commitment to helping other families pursue their greatest financial goals.

In general, clients of The Ferrucci Company are affluent families, retired senior executives or successful business owners. In all cases, they are seeking the unbiased counsel of a financial professional to help them work toward the goals that are most important to them.

The Ferrucci Company
2 South Main Street • Essex, CT 06426
800.633.3051 • 860.767.6562 • 860.767.6563 fax
www.ferruccicompany.com
office@ferruccicompany.com

Securities and Advisory Services offered through Commonwealth Financial Network, member NASD, SIPC.
A Registered Investment Advisor.