Thornburg Investment Management®

Strategies for Building Real Wealth

TP120

The Silver Tide – Are You Prepared?

Jack Gardner, CIMA®
President
Thornburg Securities Corp

TP120

Four Metrics Every Retiree Should Know:

- **Current Spending Amount:** calculated via an endowment spending policy and held as part of a two year cash flow reserve. Breakdown to monthly budgeted amount.
- **Current Spending Rate:** calculated at the beginning of each year as annual spending from the portfolio divided by the current investment portfolio value.
- **Income / Spending Ratio:** how much of the annual spending amount is derived from a growing income stream comprised of dividend and interest income.
- **Amount Spent Since Retirement Began:** in addition to the current portfolio value.

Overview - Retirement Income Process

The information given should not be considered tax advice. Please consult your tax advisor for personal tax questions and concerns.

Following these strategies does not assure or guarantee sustainability of a retirement portfolio, better performance, nor does it protect against investment losses.

Monitoring the Current Spending Rate

Hypothetical Retirement Parameters

Client Input:

- $1 Million Portfolio
- 30 Years
- 5% Initial Spending Rate
- No Legacy

Financial:

3% Inflation

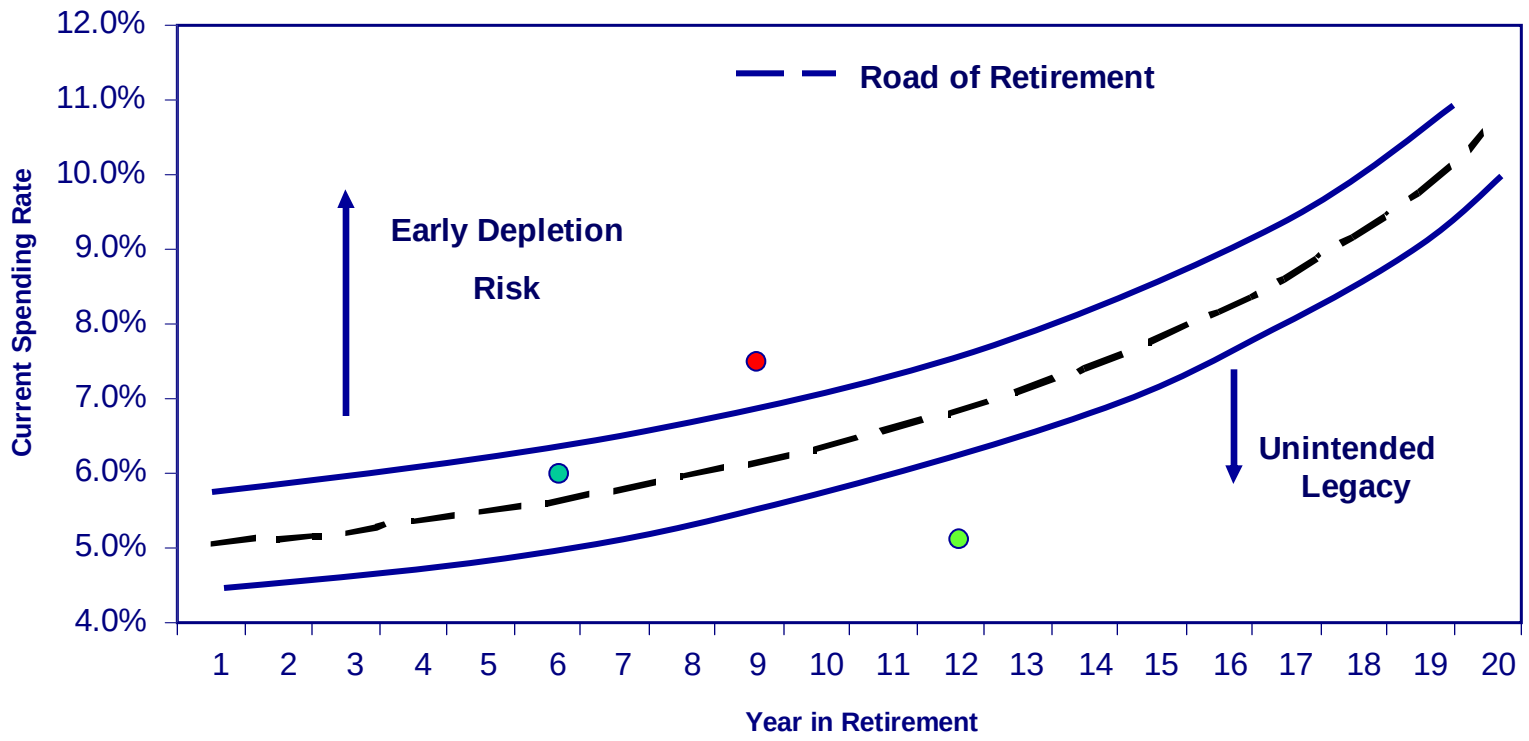
= Annual Return:

5.70% net

	Spend	Account	Spend / Account
1	50,000	1,000,000	5.00%
2	51,500	1,006,983	5.11%
3	53,045	1,012,865	5.24%
4	54,636	1,017,536	5.37%
5	56,275	1,020,882	5.51%
6	57,964	1,022,780	5.67%
7	59,703	1,023,098	5.84%
8	61,494	1,021,695	6.02%
9	63,339	1,018,420	6.22%
10	65,239	1,013,115	6.44%
11	67,196	1,005,607	6.68%
12	69,212	995,714	6.95%
13	71,288	983,241	7.25%
14	73,427	967,981	7.59%
15	75,629	949,714	7.96%
16	77,898	928,202	8.39%
17	80,235	903,196	8.88%
18	82,642	874,427	9.45%
19	85,122	841,613	10.11%
20	87,675	804,449	10.90%

The illustration is hypothetical and not intended to serve as a projection of the investment results of any investment.

Monitoring the Current Spending Rate



The illustration is hypothetical and not intended to serve as a projection of the investment results of any investment.

Source: Thornburg Investment Management

Monitoring the Current Spending Rate

Two Distinctly Poor Eleven-Year Retirement Scenarios

- Retired on January 1, 1973 and January 1, 2000
- 60% Equities and 40% Intermediate Term Gov't Bonds (ITGB)
- Rebalanced Annually
- 5% Initial Spending Rate Indexed to Inflation

Analysis used Broad Equity Portfolio versus a Dividend Growers Portfolio.

Analysis based on the assumption that the Broad Equity Portfolio performed similarly to the S&P 500 Index and the Dividend Growers Portfolio performed similarly to the S&P 500 Dividend Aristocrats Index. Investors may not make direct investments into any index.

For illustration purposes only.

Source: Thornburg Investment Management

Monitoring the Current Spending Rate

Two Distinctly Poor Eleven-Year Retirement Scenarios

	1973 – 1983	2000 – 2010
Annual Inflation Rate[1]	8.21%	2.47%
S&P 500 Index – Nominal/Real	8.07% / -0.12%	0.41% / -2.01%
S&P Top 100 Dividend Paying Stock Index – Nominal/Real	15.68% / 6.91%	9.00% / 6.37%
Barclays ITGB Index – Nominal/Real	8.32% / 0.11%	5.59% / 3.05%

[1]Based on CPI-U

Individuals cannot invest directly into an index.

Nominal = nominal return which is the rate of return on an investment without adjusting for inflation.

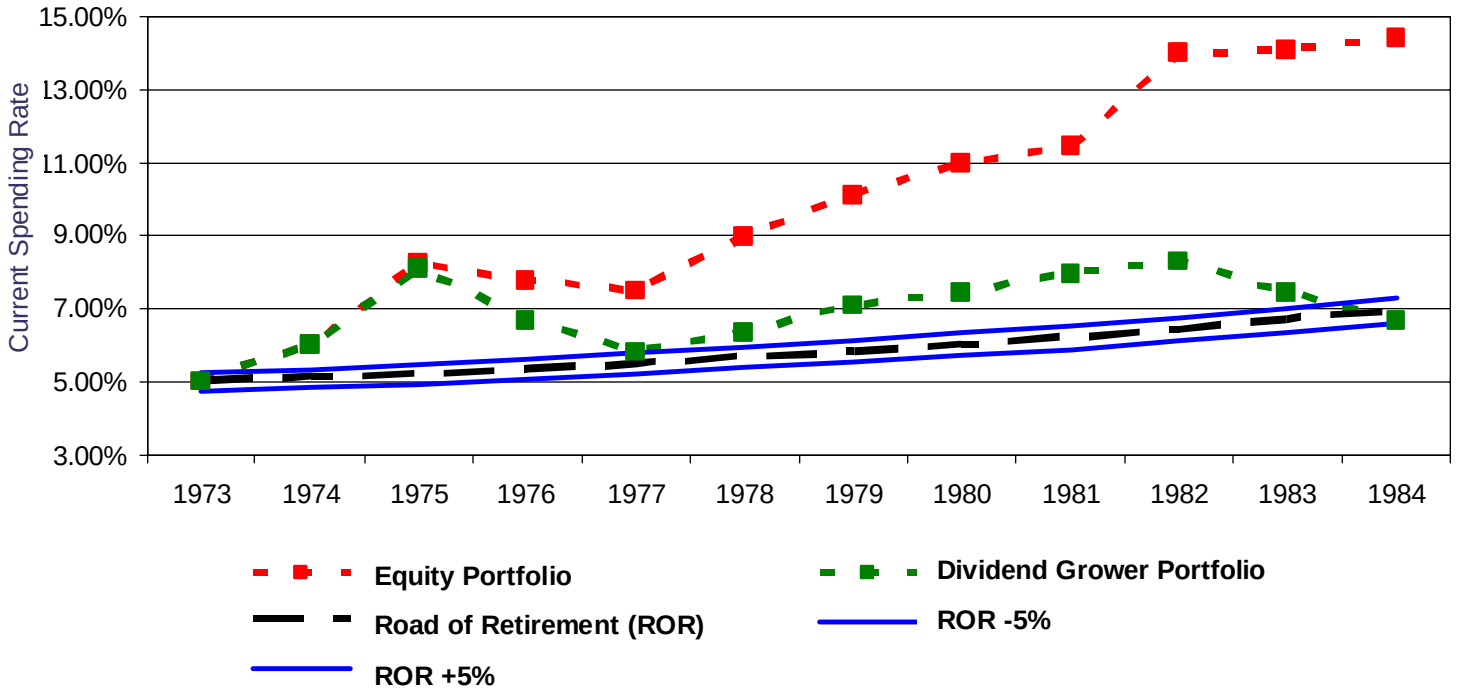
Real = real return which is the return after deducting the effect of inflation.

Sources: Barclays and Standard and Poors

Past performance does not guarantee future results.

Monitoring the Current Spending Rate

Hypothetical January 1973 Retirement Date

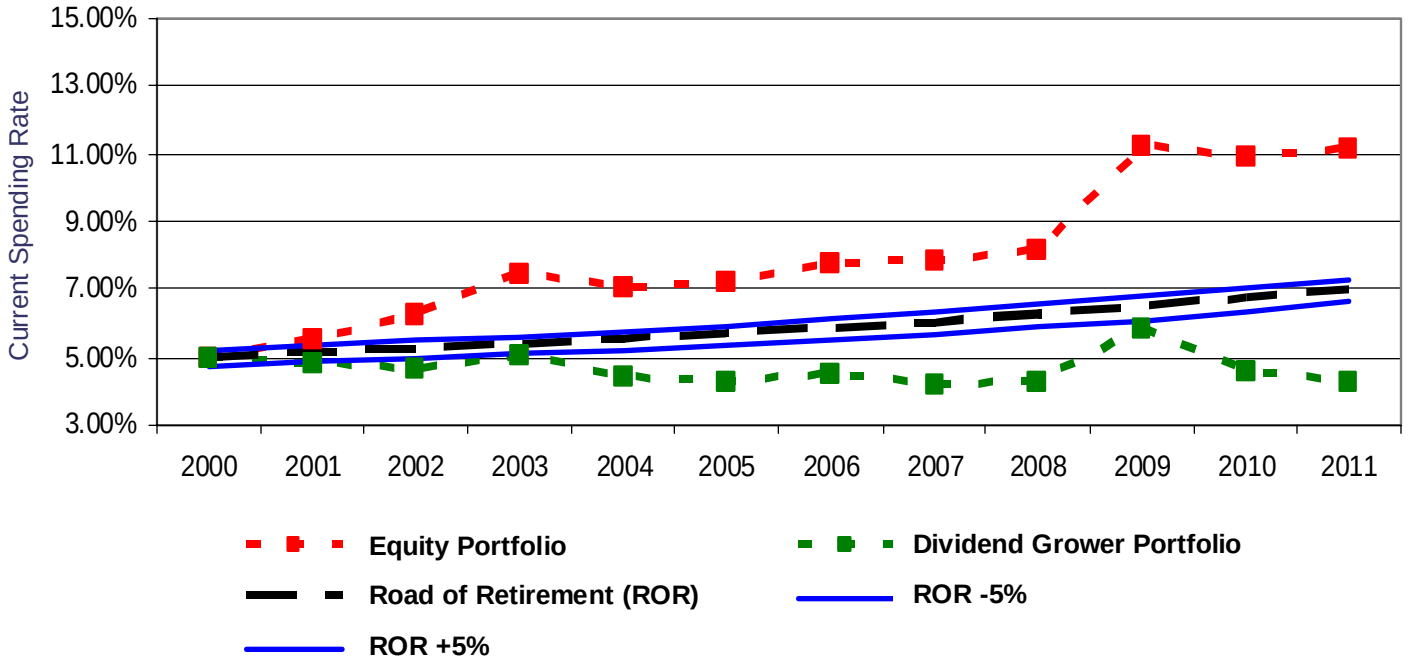


We've assumed the Equity Portfolio performed similarly to the S&P 500 Index and the Dividend Grower Portfolio performed similarly to the S&P Top 100 Dividend Paying Stock Index.
Investors may not make direct investments into any index.

For illustration purposes only.
Source: Thornburg Investment Management

Monitoring the Current Spending Rate

Hypothetical January 2000 Retirement Date



We've assumed the Equity Portfolio performed similarly to the S&P 500 Index and the Dividend Grower Portfolio performed similarly to the S&P Top 100 Dividend Paying Stock Index. Investors may not make direct investments into any index.

For illustration purposes only.

Source: Thornburg Investment Management

Tax Efficient Withdrawal Strategies

- *In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®*
- Roth's, Tax Deferred (e.g. 401(k)) and Taxable Accounts
- Implications for Asset Location, Allocation and Withdrawal Strategies
- Tax Efficient Withdrawals Can Improved Retirement Portfolio Sustainability by 1 – 5 Years.

The information given should not be considered tax advice. Please consult your tax advisor for personal tax questions and concerns.

Following these strategies does not assure or guarantee sustainability of a retirement portfolio, better performance, nor does it protect against investment losses

Tax Efficient Withdrawal Strategies

Key Concept #1 - Treat Tax Deferred Account (TDA) Like a Partnership.

- Assuming a 25% Future Tax Rate in Retirement, the Investor Owns 75% of the Principal and Government Owns 25%.

- Purchasing Power - $1.00 in a TDA Has Same Future Purchasing Power as $.75 in Roth.
  - Assume Both Double in Value, Worth $1.50 After Tax.

- AFTER TAX VALUE of TDA Grows Tax Free to Investor.

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Key Concept #2 - Taxable Accounts Least Tax Efficient

	Bonds*	Stocks
Roth	0%	0%
TDA	0%	0%
Taxable	1-Current Tax Rates (Ord)	1-Current Tax Rates (CG or Ord)

* Assume taxable bonds

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Investor's Share of Principal, Return & Risk

	Principal	Return	Risk / Losses
Roth	100%	100%	100%
TDA	1- Future Tax Rate (Ord)	100%	100%
Taxable	100%	1-Current Tax Rate (CG or Ord)	1-Current Tax Rate (CG or Ord)

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Implication #1 – Asset Location

Roth and TDA	Taxable
Bonds / interest bearing assets	Assets with capital gain returns
Real estate investment trusts	Undeveloped real estate
Tax inefficient stock funds	Tax-managed equity funds / stocks
Hedge funds	High dividend stock funds

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Implication #2 – Asset Allocation

Pre-Tax	After-Tax
$100,000 in Bonds – Roth	$100,000 in Bonds – Roth
$300,000 in Bonds – TDA	$225,000 in Bonds – TDA
$600,000 in Stocks – Taxable	$600,000 in Stocks – Taxable
$1,000,000 - Total	**$925,000 - Total**
60/40 Allocation	**65/35 Allocation**

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Implication #3 – Withdrawal Sequence- General Rule

1. Required Minimum Distribution (RMD), when applicable, from TDA
2. Bonds and then stocks held in a Taxable Account
3. Stocks then bonds held in a Roth IRA
4. Stocks then bonds held in TDA

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tax Efficient Withdrawal Strategies

Implication #3– Withdrawal Sequence- Exceptions

- TDA - withdraw whenever in an unusually low tax bracket.
- Three years where taxable income might be low include:
  - Before RMD's Begin.
  - Large Charitable Deductions.
  - Large Deductible Medical Expenses.

Source: In The Presence of Taxes: Applications of After-Tax Asset Valuation – William Reichenstein, Ph.D., CFA®

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Tangible Investing in Retirement

We define tangible investing as an investment strategy that cultivates a substantial and growing cash flow via dividend and interest income.

This can be an attractive solution for retirees who are trying to balance present income needs with future purchasing power.

Following this strategy does not assure or guarantee sustainability of a retirement portfolio, better performance, nor does it protect against investment losses

Tangible Investing In Retirement

FEATURE

Tangible Investing in Retirement Using a Global Dividend Income Strategy

By Jack Gardner CIMA®, AIFA®

As financial markets continue to mend following the disruption of 2007–2009, many investment consultants are rethinking how to help baby-boomer clients build sustainable retirement plans. For clients who are within five years of retirement, investment consultants would be wise to heed that well-known value investor Benjamin Graham, who said, "The investor will do better if he forgets about the stock market and pays attention to his dividend returns and to the operating results of his companies." I believe that a tangible investment strategy that cultivates a substantial and growing cash flow via dividend and interest income can be an attractive solution for retirees who are trying to balance present spending needs with future purchasing power. The combined focus on a rising income stream plus acceptable risk-adjusted total return may help keep retirees on plan during difficult markets.

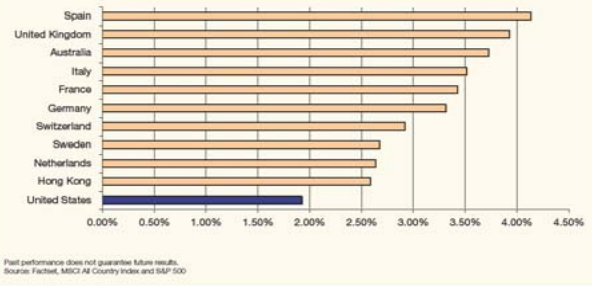
> "The cornerstone of such a tangible investment strategy for retirement includes the use of equity dividend income derived via a global investing strategy."

The cornerstone of such a tangible investment strategy for retirement includes the use of equity dividend income derived via a global investing strategy. This article will review how to structure, allocate, and monitor the results of such a tangible investment strategy for retirees.

Opportunities of a Global Dividend Strategy

Dividends are viewed differently in different cultures. Among many U.S.-domiciled companies, where executive compensation is tied to growing the share price, dividends are a sign of limited reinvestment opportunities. Arnott and Asness (2003) showed, however, that companies with high dividend payout ratios tend to subsequently have higher earnings growth than companies with

FIGURE 1: DIVIDEND YIELDS BY COUNTRY

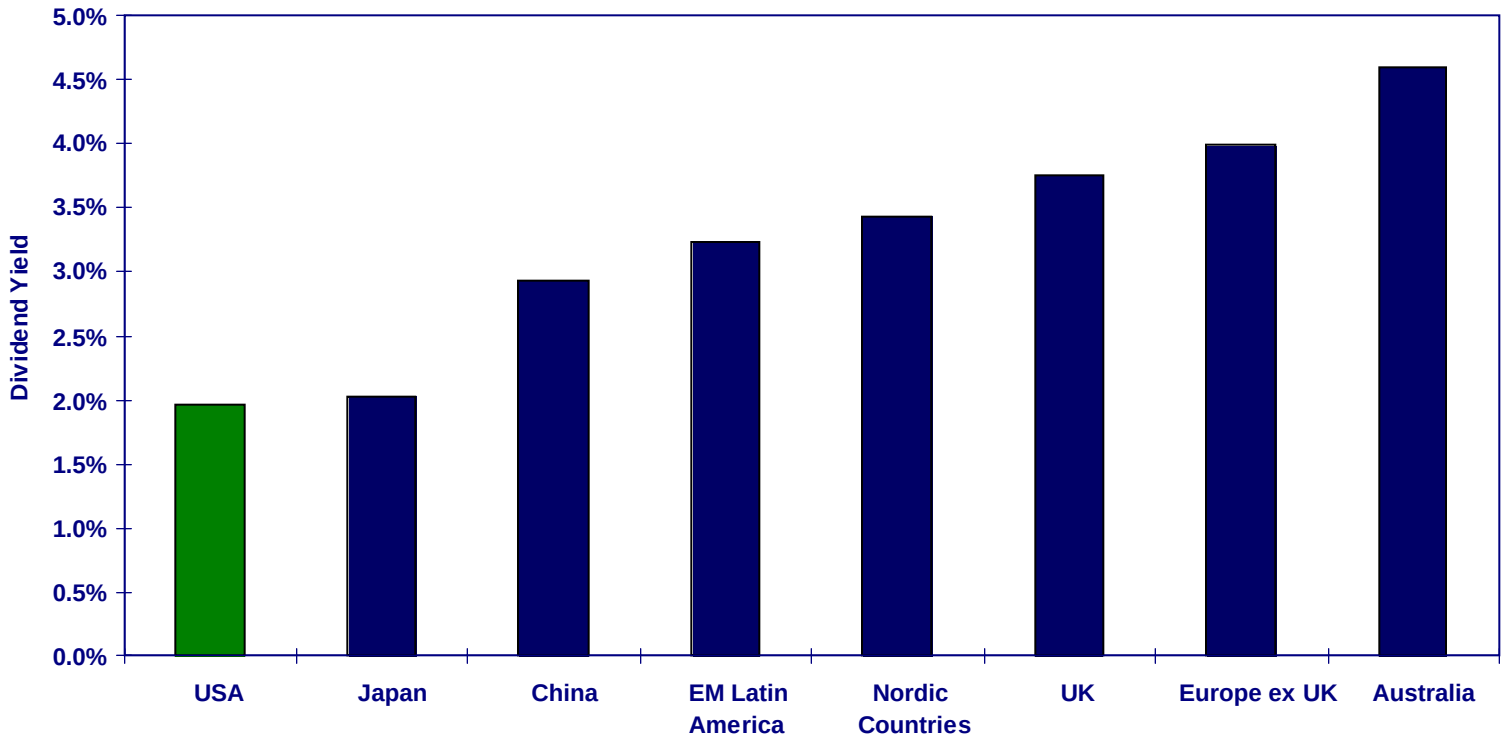


Past performance does not guarantee future results.
Source: Factset, MSCI All Country Index and S&P 500

Following this strategy does not assure or guarantee sustainability of a retirement portfolio, better performance, nor does it protect against investment losses

Tangible Investing in Retirement

Dividend Yields by Country



Past performance does not guarantee future results.

As of December 31, 2010
Source: Factset, MSCI All Country Index.

Tangible Investing in Retirement

Global Dividend Yields by Sector (2011E Dividend Yields),12/31/10

Sector	USA	CHINA	EM LATIN AMERICA	NORDIC COUNTRIES	UK	EUROPE x UK	AUSTRALIA
Index Average	2.0%	2.9%	3.2%	3.4%	3.7%	4.0%	4.6%
Telecommunications	4.9%	3.7%	4.5%	4.6%	5.7%	7.6%	9.8%
Utilities	4.4%	2.7%	5.6%	4.5%	5.4%	5.8%	5.0%
Consumer Staples	3.2%	2.0%	2.3%	2.1%	4.0%	2.9%	5.4%
Healthcare	2.2%	1.1%	NA	2.0%	4.9%	3.8%	3.1%
Industrials	2.1%	2.3%	1.9%	2.4%	3.0%	3.0%	4.3%
Energy	1.9%	3.1%	2.8%	5.4%	4.1%	5.0%	2.5%
Materials	1.7%	2.0%	3.4%	3.0%	1.8%	2.9%	2.2%
Financials	1.7%	3.5%	3.3%	3.9%	3.7%	4.5%	6.5%
Consumer Discretionary	1.4%	2.1%	2.8%	4.4%	3.4%	3.2%	5.8%
Information Technology	0.9%	1.0%	7.3%	4.1%	1.3%	2.7%	2.5%

Best Opportunities

Past performance does not guarantee future results.

Sources: MSCI Country and Regional Indices sourced via Bloomberg, as of 12/31/10

Tangible Investing in Retirement

Components of Return and Standard Deviations, 2000-2010

	Price		Income		Total	
	Return	STDEV	Return	STDEV	Return	STDEV
S&P 500 Index	-1.40%	16.40%	1.83%	0.19%	0.43%	16.41%
S&P Dividend Aristocrats Index	4.74%	14.89%	2.85%	0.41%	7.60%	14.89%
S&P Global Dividend Opportunities Index	4.38%	20.20%	6.57%	1.06%	10.94%	20.42%
Barclays 10-Yr Muni Bond Index	0.80%	1.42%	4.84%	0.02%	5.65%	1.43%
Barclays 5-Yr Muni Bond Index	0.26%	3.38%	4.81%	0.07%	5.07%	3.39%

Past performance does not guarantee future results.

Sources: S&P 500, Barclays, and calculated by Thornburg Investment Management.

Tangible Investing in Retirement

		Hypothetical Yield on Original Cost				
	Spending Rate	S&P 500 Index	S&P Dividend Aristocrats Index	S&P Global Dividend Opportunities Index	Barclays 10-Yr Muni Bond Index	Barclays 5-Yr Muni Bond Index
2000	5.00%	1.12%	2.58%	4.87%	5.24%	5.22%
2002	5.31%	1.09%	2.69%	5.21%	5.20%	4.98%
2004	5.52%	1.32%	2.96%	6.91%	5.10%	4.84%
2006	5.67%	1.70%	3.83%	12.10%	5.02%	4.81%
2008	6.22%	1.93%	4.56%	14.82%	4.95%	4.70%
2010	6.43%	1.52%	4.69%	9.00%	4.96%	4.54%
Cumulative Appreciation		-14%	66%	62%	9%	3%
Purchasing Power		- 45%	36%	31%	-22%	-28%

Past performance does not guarantee future results.

Individuals cannot invest directly into an index.

Sources: S&P 500, Barclays, and calculated by Thornburg Investment Management.

The 2000 Retiree Annual Review

- Hypothetical Retirement Began on 1/1/2000
- Asset Allocation:
  - 5% Muni Money Market Fund,
  - 5% 5-Year Barclays Municipal Bonds Index,
  - 25% Barclays 10-Year Municipal Bonds Index,
  - 15% Dividend Aristocrats Index,
  - 50% Global Dividend Opportunities Index
- Used Cash Flow Reserve, Rebalanced Annually
- 5% Initial Withdrawal Rate Grown at Inflation (CPI)

The 2000 Retiree Annual Review

Hypothetical Income, Balance and Return Sheet

	2000	2006	2008	2009	2010	Since Retirement Began
Income Statement						
Interest Income	17,249	22,143	25,139	16,822	21,240	210,449
Dividend Income	28,218	54,964	62,921	53,414	51,953	495,424
Total Income	45,467	77,108	88,061	70,237	73,194	705,874
Budgeted Spending	50,000	58,660	62,232	64,597	64,339	631,183
Income / Spend Ratio	91%	131%	142%	109%	114%	112%
Balance Sheet						
CAR	9.80%	16.89%	-27.30%	39.63%	7.14%	9.34%
YE Account Value	1,045,837	1,593,436	1,175,771	1,573,391	1,625,381	
Spend Rate* Yr	4.94%	3.80%	5.49%	4.09%	4.02%	

Past performance does not guarantee future results.

* Current spending rate is next year's spending amount divided by the YE account value.

The illustration is hypothetical and not intended to serve as a projection of the investment results of any investment.
Source: Calculated by Thornburg Investment Management.

In Summary

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The Process of Managing Retirement Income

Strategies for Building *Real* Wealth

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The Case for a High and Growing Dividend Stock Strategy in Retirement Portfolios

A reprinted article from November/December 2008

Investments & Wealth MONITOR

IMCA® investment management consultants association

This article received IMCA's 2009 Stephen L. Kessler Writing Award.

The Case for a High and Growing Dividend Stock Strategy in Retirement Portfolios

By Jack Gardner, CIMA®, AIF®

As a baby boomer, I am amazed by the disparity in the retirement income discussion within the financial advisor community. The discussion ranges from a simplistic comparison of product features to one that is academic and grounded in a holistic financial planning process. For those advisors who take a process approach to retirement income, there is a broad body of academic research regarding spending policies, tax planning techniques, and evolving asset allocation strategies. The goal of this research is to enhance the client's annual spending in retirement and the sustainability of the retirement portfolio for 30, 40, or possibly 50 years.

In my opinion, only a few retirement products that now are available have a place on the market. So many are overpriced or too complicated, and most require loss of control over assets. I know the "retirement income product industry" is bracing for a "tsunami of capital" from baby boomers, but I do not believe it will materialize because the products cost too much and investors are loath to lose control of their hard-earned assets. This reluctance will create an opportunity for knowledgeable financial advisors to assist baby-boomer clients. During this pivotal stage of life, boomers' accounts will need to be consolidated under one advisor to accommodate implementation and monitoring of a retirement income process. To participate in this opportunity, advisors need to know about all the tools available to structure retirement portfolios and be committed to staying abreast of all the academic research that is being done in this area.

Building Sustainable Retirement Income Portfolios

In 1994, William P. Bengen, CFP®, pioneered research into sustainable retirement income portfolios and establishing appropriate withdrawal rates when he published "Determining Withdrawal Rates Using Historical Data."[1] Using historical-returns data, Bengen tested 50 different 30-year retirements that ran from 1926–1955, 1927–1956, 1928–1957, and so on up to 1975–2004. The analysis covered many business cycles and included four major bear markets. A major bear market was defined as one that lasted more than one year and consumed 50 percent of the retiree's purchasing power after factoring in effects of both the S&P 500 Index decline and inflation. Needless to say, major bear markets have a devastating effect on any portfolio, but they especially impact those who also are undergoing withdrawal.

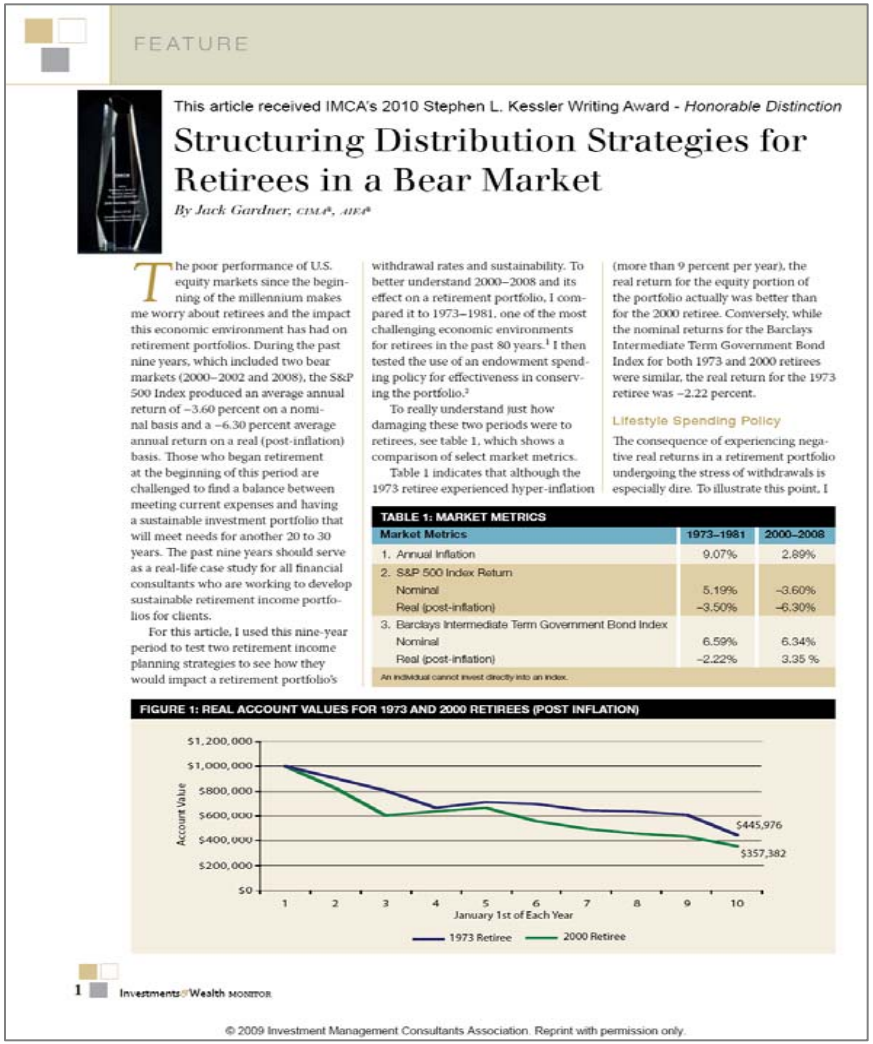
As a result of this research, Bengen is credited with establishing the 4-percent withdrawal rule (or "SAFEMAX," to use Bengen's vernacular), which states that for a retirement portfolio with a beginning value of $1 million, a retiree can spend $40,000, or 4 percent per year, and increase the annual spending amount by an annual cost of living adjustment. Bengen concluded that at this spending level, there was a 100-per-

> "Bengen studied how various asset allocation strategies affect both the withdrawal rate and sustainability of a retirement portfolio in distribution."

This study contains the most current data available at the time of publication. Inclusion of 2008 performance could change results.

Recipient – IMCA's 2009 Stephen L. Kessler Writing Award

Structuring Distribution Strategies for Retirees in a Bear Market



FEATURE

This article received IMCA's 2010 Stephen L. Kessler Writing Award - *Honorable Distinction*

Structuring Distribution Strategies for Retirees in a Bear Market

By Jack Gardner, CIMA®, AIFA®

The poor performance of U.S. equity markets since the beginning of the millennium makes me worry about retirees and the impact this economic environment has had on retirement portfolios. During the past nine years, which included two bear markets (2000–2002 and 2008), the S&P 500 Index produced an average annual return of –3.60 percent on a nominal basis and a –6.30 percent average annual return on a real (post-inflation) basis. Those who began retirement at the beginning of this period are challenged to find a balance between meeting current expenses and having a sustainable investment portfolio that will meet needs for another 20 to 30 years. The past nine years should serve as a real-life case study for all financial consultants who are working to develop sustainable retirement income portfolios for clients.

For this article, I used this nine-year period to test two retirement income planning strategies to see how they would impact a retirement portfolio's withdrawal rates and sustainability. To better understand 2000–2008 and its effect on a retirement portfolio, I compared it to 1973–1981, one of the most challenging economic environments for retirees in the past 80 years.[1] I then tested the use of an endowment spending policy for effectiveness in conserving the portfolio.[2]

To really understand just how damaging these two periods were to retirees, see table 1, which shows a comparison of select market metrics.

Table 1 indicates that although the 1973 retiree experienced hyper-inflation (more than 9 percent per year), the real return for the equity portion of the portfolio actually was better than for the 2000 retiree. Conversely, while the nominal returns for the Barclays Intermediate Term Government Bond Index for both 1973 and 2000 retirees were similar, the real return for the 1973 retiree was –2.22 percent.

Lifestyle Spending Policy

The consequence of experiencing negative real returns in a retirement portfolio undergoing the stress of withdrawals is especially dire. To illustrate this point, I

TABLE 1: MARKET METRICS

Market Metrics	1973–1981	2000–2008
1. Annual Inflation	9.07%	2.89%
2. S&P 500 Index Return		
Nominal	5.19%	–3.60%
Real (post-inflation)	–3.50%	–6.30%
3. Barclays Intermediate Term Government Bond Index		
Nominal	6.59%	6.34%
Real (post-inflation)	–2.22%	3.35 %

An individual cannot invest directly into an index.

FIGURE 1: REAL ACCOUNT VALUES FOR 1973 AND 2000 RETIREES (POST INFLATION)

Honorable Distinction –IMCA's 2010 Stephen L. Kessler Writing Award

Further Reference

- Retirement Income Redesigned - Master Plans for Distribution – Edited by Harold Evensky & Deanna Katz
- Conserving Client Portfolios in Retirement – by William P. Bengen, CFP®
- In the Presence of Taxes: Applications of After-tax Asset Valuations – William Reichenstein, PhD, CFA®

Jack Gardner

Jack Gardner, CIMA®
President, Thornburg Securities Corporation

BS, Stonehill College

MS, Bentley College

Jack Gardner is the president of Thornburg Securities Corporation, distributor for the Thornburg family of mutual funds and a managing director of Thornburg Investment Management, the advisor. Jack has been involved in the investment advisory industry for over thirty years

Jack received the Certified Investment Management Analyst® (CIMA) designation from the Investment Management Consultants Association (IMCA). He is the author of the book *How to Write an Investment Policy Statement* and received IMCA's 2009 Stephen L. Kessler Writing Award and 2010 Honorable Distinction for his *Investments and Wealth Monitor* articles, "The Case for a High and Growing Stock Dividend Strategy in Retirement Portfolios" and "Structuring Distribution Strategies for Retirees in a Bear Market". Jack is a frequent speaker on topics including creating sustainable retirement portfolios for the distribution stage and fiduciary prudent practices. He is also on the Policy Board for the Investment Fiduciary Leadership Council.

Jack holds a BS degree in Accounting from Stonehill College and an MS in Computer Information Systems from Bentley College.