

Are You a **STOCK** or a **BOND**?

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QUESTION:
Which Number is Less Predictable?
(i.e. more volatile)

1. Total **stock market** return during next decade.
2. Total years you will **live/spend** in retirement.

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Historical U.S. Market Equity Returns

Decade	\$1 Growth During Decade	Annualized
1940s	\$1.249	9.6%
1950s	\$5.336	18.2%
1960s	\$2.216	8.3%
1970s	\$1.801	6.1%
1980s	\$4.687	16.7%
1990s	\$5.245	18.0%
2000s	\$0.968	-0.3%
Average	\$3.250	10.7%
Variability	\$1.796 (=55%)	

Source: Ibbotson/SBBI Total Value Weighted Return (2010 edition, page 92)

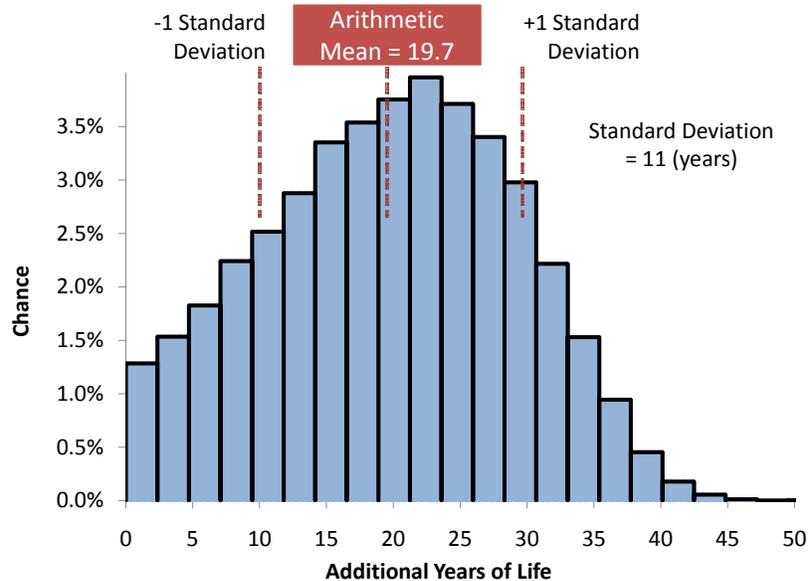
Remaining Life for 65 year-old:

- Arithmetic Mean = **19.7** years
- Standard Deviation = **11.0** years
- Variability of **56%**

Read the Obituaries: How Many Years in Retirement?				
20.8	2.3	12.1	9.0	34.2
4.3	20.1	30.3	27.5	23.4
20.7	4.7	11.4	20.4	35.6
4.9	20.3	30.2	30.2	33.9
34.5	29.1	19.6	20.9	28.8
18.8	24.3	18.7	19.9	28.3
21.0	30.2	40.5	34.2	17.0
10.3	6.2	4.2	24.0	17.5
8.5	36.3	24.7	11.8	0.3
26.3	5.9	26.2	19.2	14.4

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Remaining lifetime for 65 year-old:



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Longevity in the U.S.

Number of Americans...	
> Age 90	2,000,000
> Age 100	73,000

Source: U.S. Fed News (5 September 2007)

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FOCUS RETIREMENT SECURITY: INCOME PLANNING

To Insure Longevity Risk Or Not: That Is The Question

BY DENNIS L. CARR

THE GOAL OF RETIREMENT income planning is to convert the client's nest egg into a stream of inflation-adjusted income that will last the client's lifetime. This involves 3 major unknowns:

- ▶ Investment returns and their pattern by asset class.
- ▶ Inflation rates.
- ▶ Lifespan (or the planning horizon).

In recent years, several studies have addressed the question of what is a safe withdrawal strategy. These

TABLE A: BASE CASE

\$500,000 Systematic Withdrawal Program (SWP)				
		Initial Withdrawal Rate	Initial Annual Income	Guaranteed Annual Income Floor
Male	Age 65	4.40%	\$22,000	-
	Age 70	4.75%	\$23,750	-
	Age 75	5.45%	\$27,250	-
Female	Age 65	4.05%	\$20,250	-
	Age 70	4.60%	\$23,000	-
	Age 75	5.15%	\$25,750	-

flation-adjusted income was fully maintained in 90% of the 2,000 scenarios.

The base case utilizes a systematic withdrawal program (SWP) for the entire \$500,000 nest egg. Today, SWPs are the most common method for drawing income from a nest egg. Calculations were done for 6 client variations—male and female; ages 65, 70 and 75 (see Table A). In each variation, the system solves for the initial annual withdrawal amount that

Source: National Underwriter, August 6, 2007

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In the past most retirees had Defined Benefit pensions to “hedge” this risk



Are You a Stock on a Bond?

You just got hired by one of the
100 largest companies in the U.S.

Did they offer you a D.B. Pension?

Year 1985	Year 2002	Year 2010
89	50	16

*Source: Watson Wyatt, Reported in J.F.P. Sep 2006
The IFID Centre, Calculations January 2010.*

Main Takeaway:

- For many clients approaching retirement, you are now their personal pension fund manager.
- Learn to identify their hidden liabilities in addition to their financial assets.
- So, lets take a closer look at the personal balance sheet...

Personal Balance Sheet of YOU Inc.

Assets

- Bank Accounts
- Housing
- Stocks & Bonds
- Car & Vehicles
- Small Business Equity
- PV of Pension

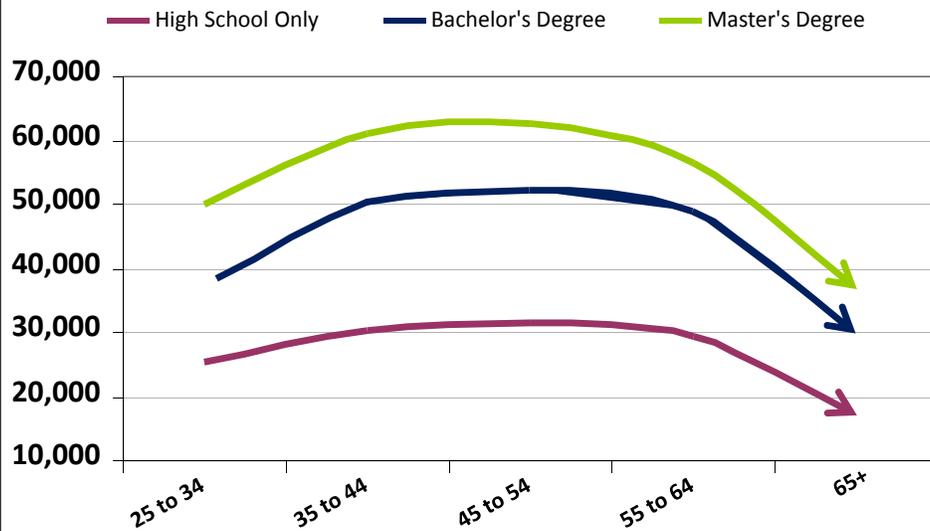
+ HUMAN CAPITAL

Debt + Liabilities

- Mortgages
- Consumer Loans
- Credit Cards
- Student Loans

• Net Worth

Median Earnings Over the Life-Cycle (USD)



Source: U.S. Census Bureau, 2008

Are You a Stock on a Bond?

How to Value Human Capital (approximately)

Human Capital

$$= \frac{45,000 \times (1 - 27\%)}{(1 + 4\%)^1}$$

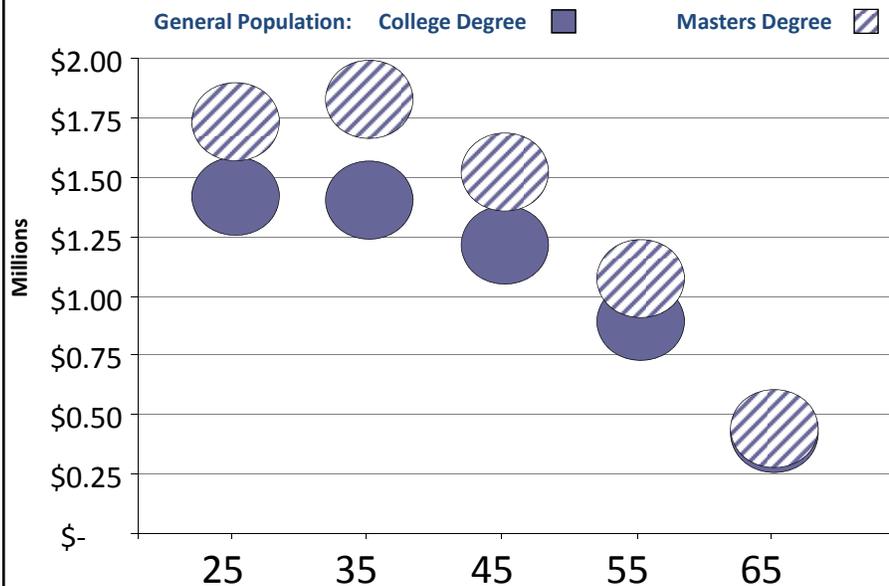
$$+ \frac{46,350 \times (1 - 27\%)}{(1 + 4\%)^2}$$

+ ...

$$+ \frac{\$142,516 \times (1 - 27\%)}{(1 + 4\%)^{40}}$$

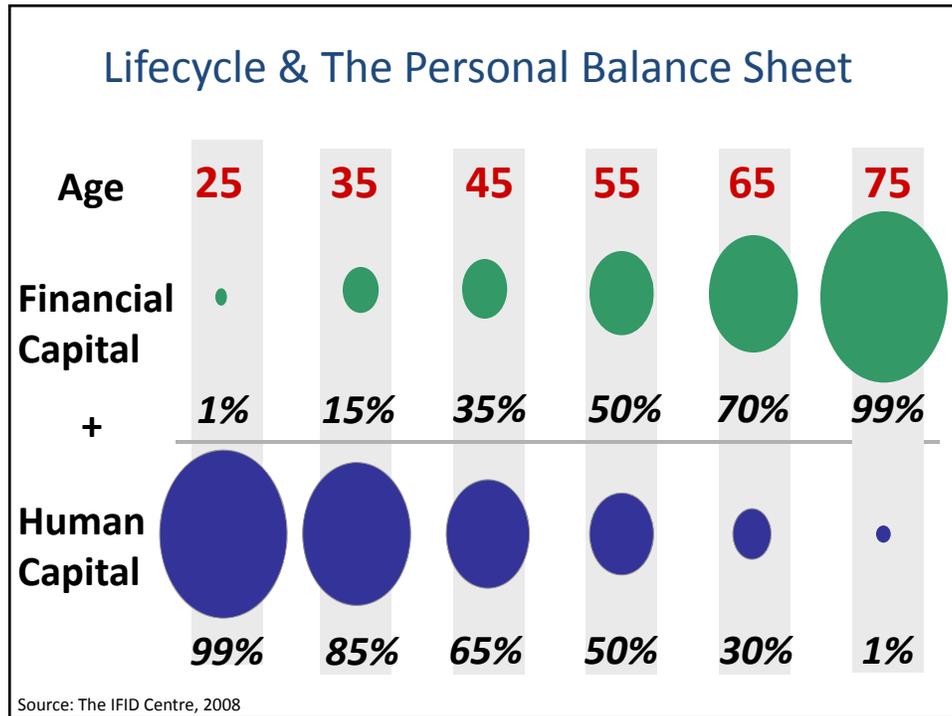
= \$1,053,017

Estimated Median Value of Human Capital:



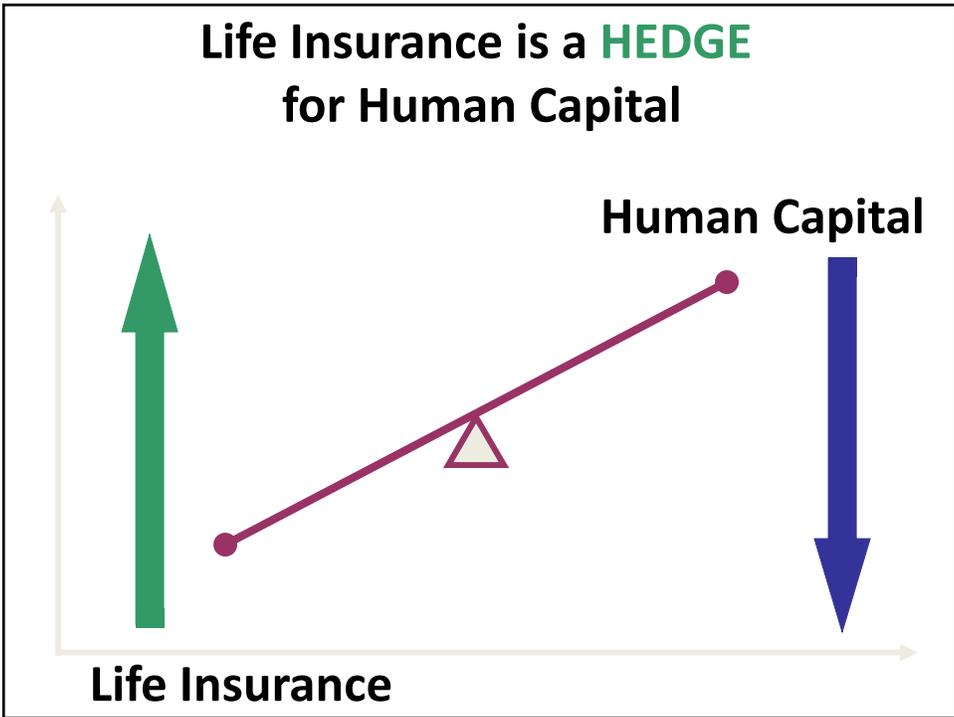
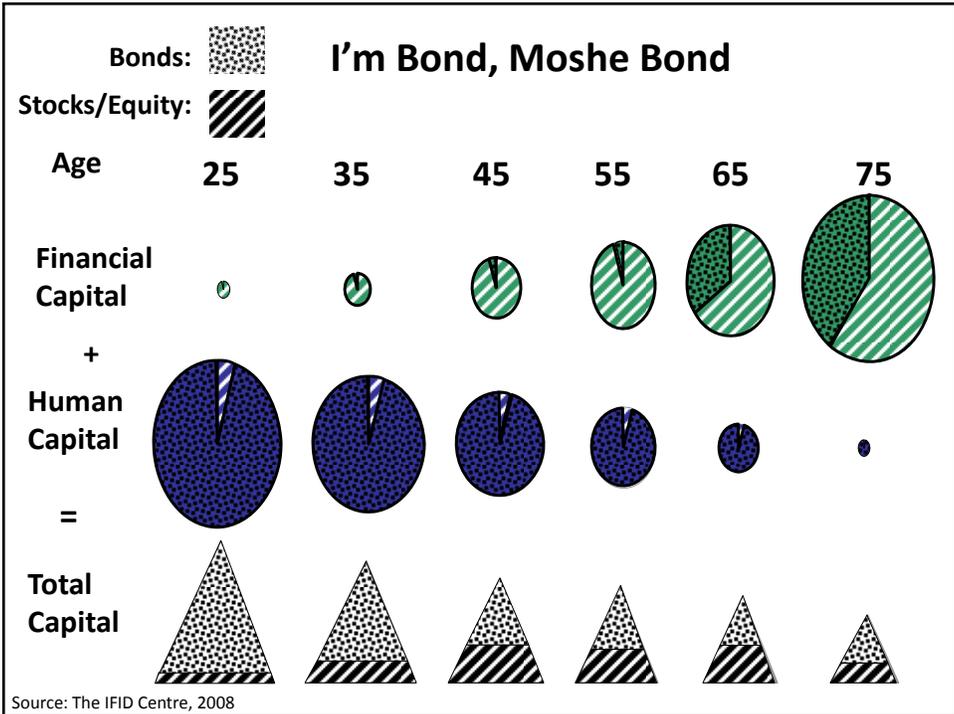
Source: U.S. Census Bureau, Current Population Survey, 2008; IFID Centre calculations

Are You a Stock on a Bond?

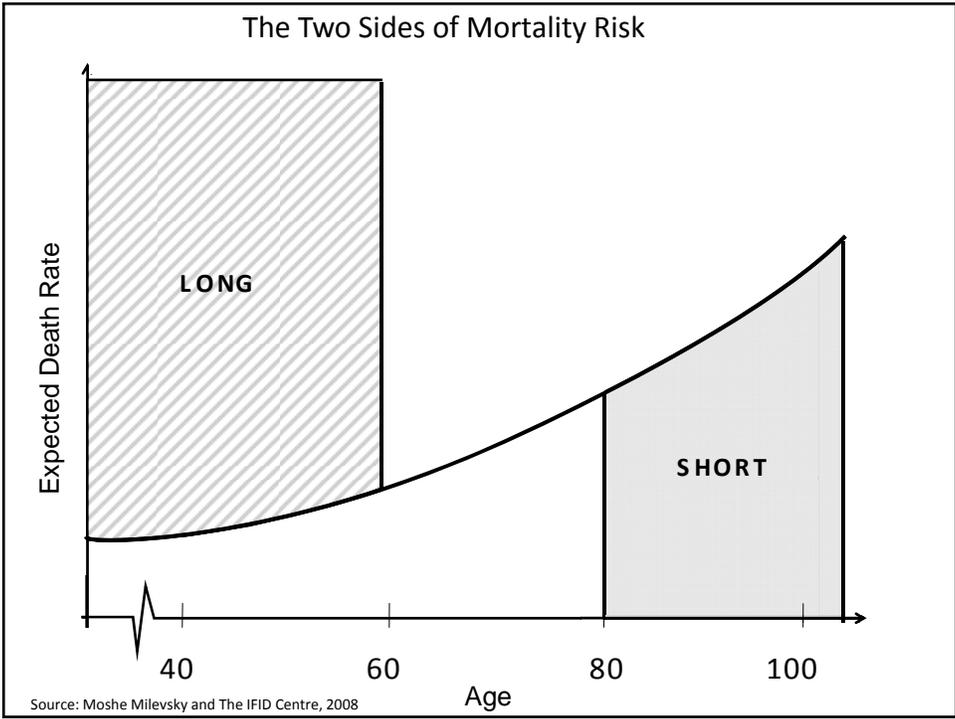


**Human Capital is the Most Valuable
Asset Class on the Personal Balance
Sheet for Most of Your Working Life**

So, are You
a **STOCK** or a **BOND**?

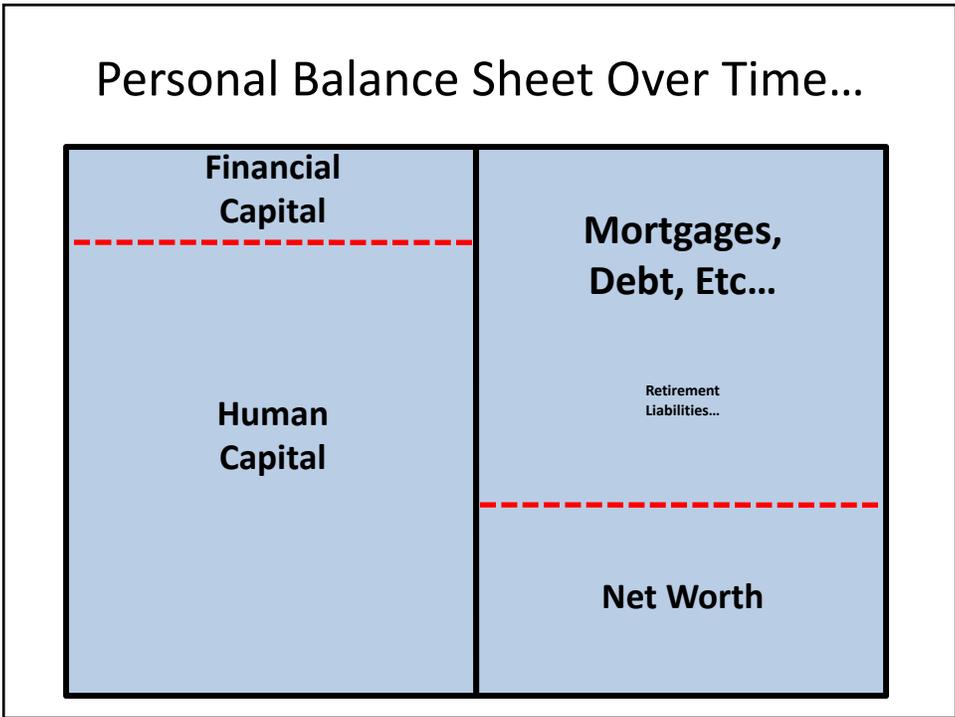
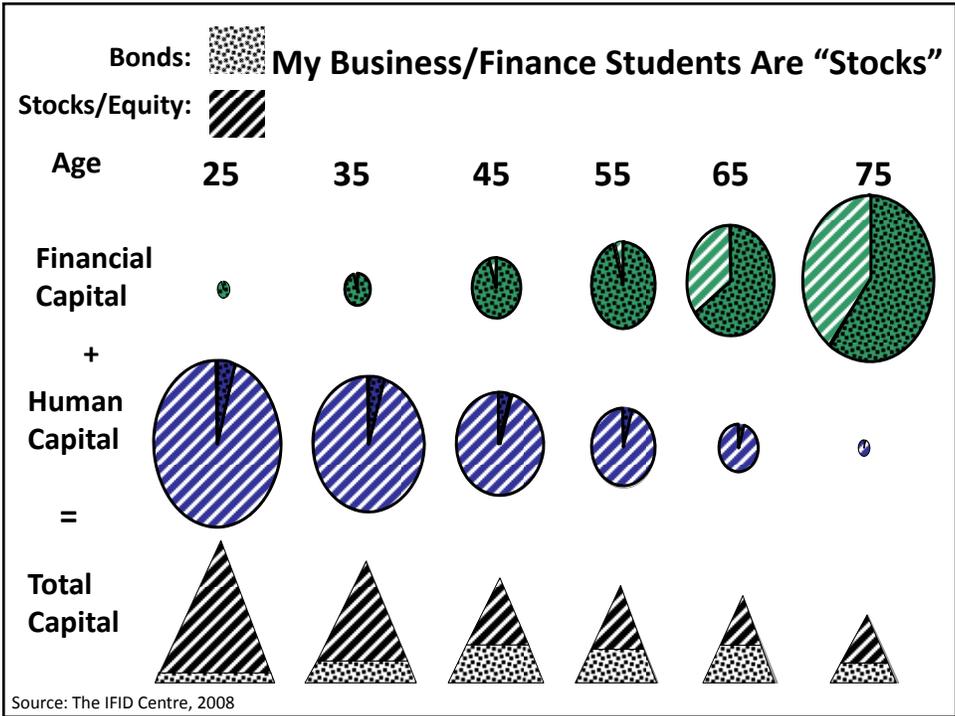


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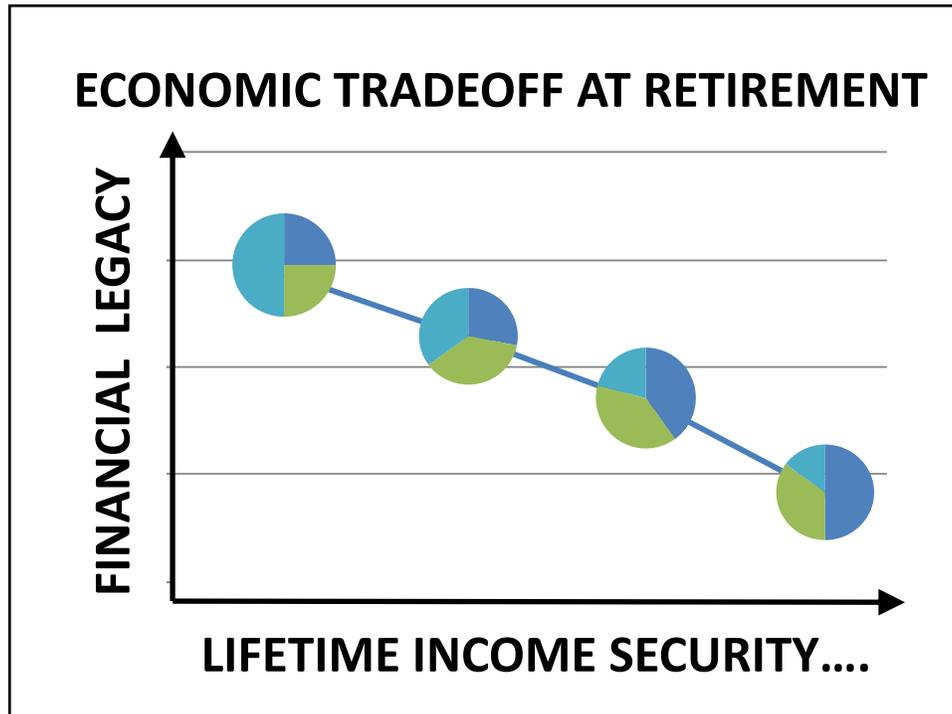


Back to Human Capital:

What about most people without union seniority or tenured jobs?



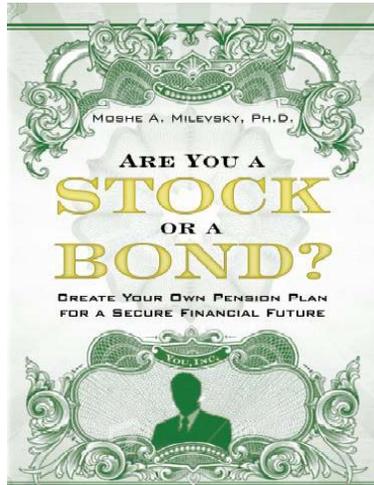
Are You a Stock on a Bond?



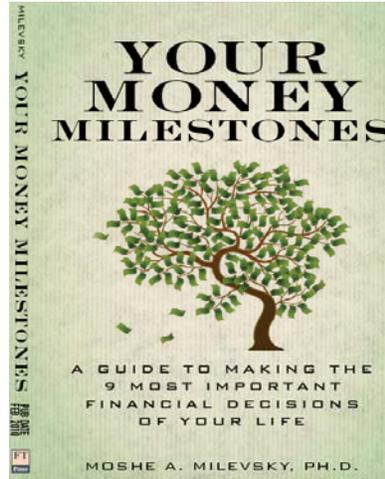
Final Takeaways:

- *Human Capital is the most valuable asset class on the personal balance sheet during most of the working years. Ask yourself and your clients: **Are You a Stock or a Bond?** Invest accordingly.*
- *When your Human Capital has been converted to Financial Capital, the role of **product** – any type of pension income for life -- **allocation** is more important than **asset allocation**.*
- **HEDGE your “retirement income” liabilities, at the lowest possible cost!**

For more information...Read the Books



Published Fall 2008



Published Winter 2010