“The Retirement Distribution Portfolio”

How to turn your 401(k)/403(b)/457 into a Modern Day Pension

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President, Foresight Capital Management Advisors, Inc.

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Content Research: Nathan Wilber, Patrick Carney CFP®, AIF®, Samuel Sheeran, Justin Littleton, and Noah Whitfield

WARNING AND DISCLAIMER

This book is intended to provide general information regarding saving for retirement. It is not intended as a substitute for the investor's own research, or for the advice of a qualified financial specialist. The author shall have neither liability nor responsibility to any person or entity with respect to any loss or damage caused, or alleged to be caused, directly or indirectly, by the information contained in this book.

ABOUT THE AUTHOR

Laurie Stegenga is President and founder of Foresight Capital Management Advisors, Inc., (FCMA) a fee-only Registered Investment Advisory firm. Her past financial work experience has spanned 37 years of managing and accounting for billions of dollars in investments. In 1983, Laurie began her career in big eight accounting, auditing large publicly traded corporations and performing audits and taxes for small entrepreneurial businesses. Five years later she joined Midwest Microwave, Inc. a defense manufacturing company as Chief Financial Officer and Human Resource Director.

In 1993, Laurie joined Alexander Hamilton Life Insurance Company as Manager of Investment Valuation and Statutory Reporting for their $7.3 billion portfolio. Several years later Laurie became a Divisional Director of Accounting and an international finance consultant for Thomson Publishing, Inc.

Then she joined Tisch Investment Advisory, Inc., a regional midwest Registered Investment Advisory firm in 1998, to form and develop their retirement plan division. During her nine years, as Vice President, with the firm she assisted in growing the retirement plan division to a $140 million portfolio, which represented about forty percent of the assets under management for the firm.

Laurie's expertise is in retirement plan services, providing on-site education and one-on-one personal financial planning for the employees, fiduciary consulting, and all aspects of personal wealth planning for the individual and family office. In 2008, she ventured out on her own and established Foresight Capital Management Advisors, Inc. FCMA was featured in the June 2010 issue of *Forbes Magazine - Michigan Financial* and the September 12th 2016 issue of the *Wall Street Journal*. She was listed as a top-ranking RIA in the July 2016, 2017, and 2019 issues of *Financial Advisor Magazine* and has been named a Detroit Five Star Wealth Manager in *HOUR Detroit* and *DBusiness* for six consecutive years, 2016 – 2021.

In 2020 Laurie became a Certified Exit Planning Analyst (CEPA) and the firm now offers complete business transition planning for companies as owners reach retirement.

"THE RETIREMENT DISTRIBUTION PORTFOLIO"

How to turn your 401(k)/403(b)/457 into a Modern Day Pension

HOW TO CREATE A DISTRIBUTION PORTFOLIO AND HARVEST YOUR DIVIDENDS AND INTEREST FOR A BOUNTIFUL RETIREMENT

Authored by: Laurie S. Stegenga CPA, CFP®, PFS, AIF®, CEPA

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Workplace retirement plans are evolving, and individuals are now responsible for funding their own retirement. This is a big change from the retirement plans of the past, which relied on pensions to provide retirement income for workers and their families. To fund a retirement pension, companies would contribute to a defined benefit pension fund as well as with the earnings of the employees. Workers would be pooled together in one pension fund and actuaries would be needed to assess the funding level and risk within the pension plan. This has since changed, and defined contribution plans, such as 401(k) and 403(b) plans, are now the prominent retirement savings vehicles for workers. This shift in retirement savings, in addition to social security which is only designed to cover about 40% of your pre-retirement income, has required a change in the mindset amongst successful retirees (Social Security Administration)[1].

Luckily, there are strategies and financial tools that individuals can use to help them prepare for a healthy retirement. With pensions becoming a thing of the past, it is important to understand how and why successful retirees are saving and preparing for retirement. There are now two phases of retirement; one is saving for retirement during your working life which is the "**Accumulation Phase**" and the other begins in retirement when one is no longer working, but

In this booklet, we will discuss strategies to save for retirement by accumulating wealth and then ways to live into retirement with peace of mind knowing you have created a distribution portfolio that will sustain your lifestyle for the rest of your life. Many people do not realize that the investment portfolios you build during the accumulation phase actually need to be ***transformed*** into distribution portfolios as you near retirement. This booklet will describe the difference between an accumulation portfolio and a distribution portfolio and how to transform your portfolios and why it is critically important that you do so.

WHAT IS A PENSION?

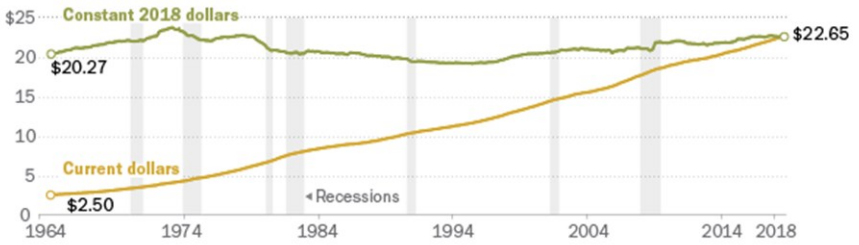
Pensions used to be common with most employers; an employee would work for a company for 30-40 years and when the employee retired, they would receive monthly payments up until they passed away. What is going on behind the scenes? Does a company simply keep the employee on the payroll and pay the retired employee from their current revenues? The simple answer is no. A pension implies that the employer is contributing a certain amount of money annually into the pension fund on behalf of each employee involved within the fund and investing the contributions to grow over time. The future amount of the contributions that have compounded over time are what the employee receives in retirement. The employer continues paying the retired employee with money from the pension investments for the continued duration of the retired employee's life.

WHAT IS REQUIRED TODAY?

Now that most employers no longer are offering pensions, an employee is required to save on their own, which is perfectly ok! Remember, an employer was contributing money on behalf of each employee to invest into the pension. Now that employers are not deducting money out for pensions, employees' paychecks are nominally larger than previously throughout history. This means employees just have to deduct an amount from their own paychecks and contribute it into their own retirement account so it can grow over time. They can then set money aside from their own paycheck and contribute to their own self-generated nest egg and create their own "pension". But how do you create your own "Self-Made Pension?" or "Modern Day Pension"?

Americans' paychecks are bigger than 40 years ago, but their purchasing power has hardly budged

Average hourly wages in the U.S., seasonally adjusted



Source: U.S. Bureau of Labor Statistics.

Pew Research Center

TWO PHASES OF THE MODERN DAY PENSION

PHASE ONE: SAVING AND ACCUMULATING WEALTH

Saving for retirement should begin as early as possible. As soon as you get your first full time job and can start saving, you should begin putting money away and letting it grow until retirement. Now, there is no magic number that should be saved for retirement, but there are some general rules to follow. Here are some basic concepts to follow for a successful savings pattern. At age 35, you should have approximately 1x your salary saved, at age 45 you should have about 3x your salary saved, at age 55 you should have about 5x your salary saved, and at age 67 you should have about 8x your salary saved. For example, if you have a salary of $30,000, you should have the following amounts saved at the corresponding ages: $30,000 at age 35, $90,000 at age 45, $150,000 at age 55, and $240,000 at age 67. Talking to a financial advisor can help determine how much is needed to save for retirement. A tool called a ***Monte Carlo Simulation*** (Palisade, "What is Monte Carlo Simulation?")[2] can help determine the amount needed to save for a successful retirement. A good rule of thumb for saving for retirement is to save 15% of your gross income for every working year. Also, the earlier you start saving, the easier it will be! The images on pages 4 and 5 are a sample of a Monte Carlo simulation and also a chart displaying investment growth under different time horizons as

Monte Carlo Simulation for Sample

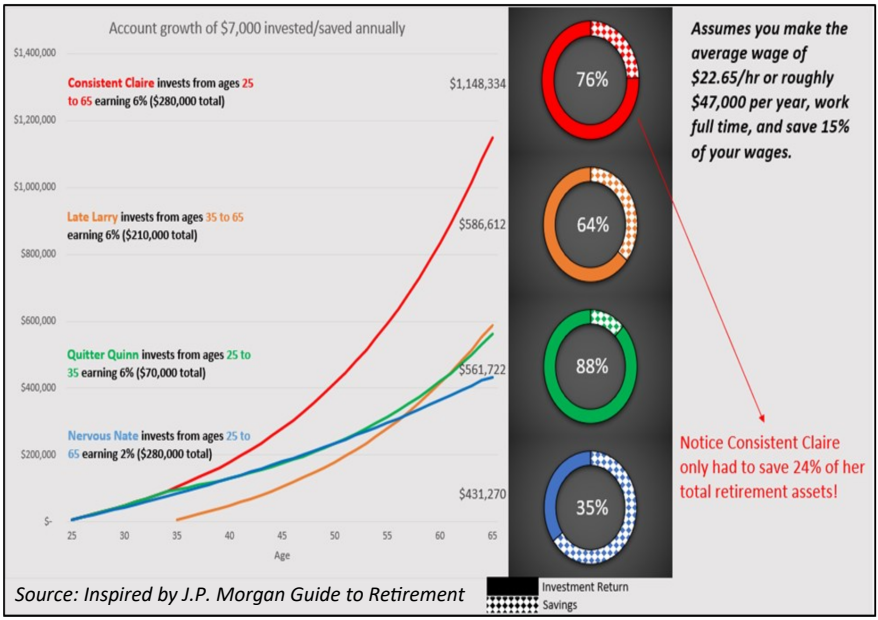
Scenario 1: Income goal of $37,600 ($33,088 net of taxes), in addition to healthcare expenses in retirement. This scenario assumes a moderate growth portfolio earning on average 7% per year. Sample person starts taking social security at age 67 upon retirement in 2037. This scenario also has the individual saving $7,000 per year until retirement. Conclusion: This scenario is recommended because there is a 92% probability of success at age 90 and a 88% probability of success at age 95 for having money throughout retirement without running out.

Assumptions:		Moderate Growth					
RoR	7%	Beginning Savings	$ 414,000	Retirement Income Goal	$ 37,600	$ 33,088	80% replacement of working salary which was $47,000 per year
Std	12%	Social Security at 67	$ 23,089	Retirement Age	67		
Inflation	3%	Annual Savings	$ 7,000	Social Security Age (SS)	67		
SS Inf	2%						
SS Std	1%			Mortality Age	90	95	
Health Inf	4%			Probability of Success	92%	88%	High likelihood of success
Health Std	1%						

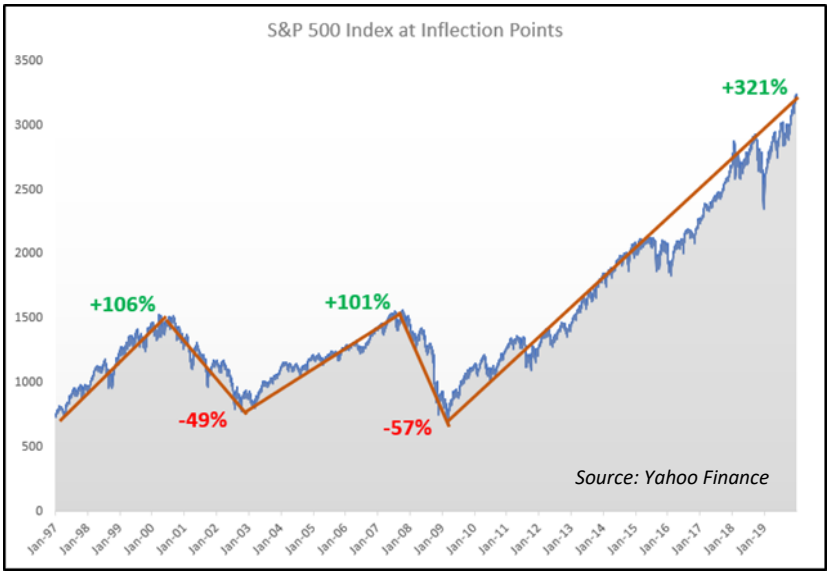
	Year	Age	Retirement Income Goal Adjusted for Inflation	Invest Pool	Social Security	Annual Savings	Healthcare Expense
37,600	2020	50	$ -	414,000	$ -	$ 7,000	$ -
38,439	2021	51	$ -	483,110	$ -	$ 7,000	$ -
39,964	2022	52	$ -	534,803	$ -	$ 7,000	$ -
41,232	2023	53	$ -	617,734	$ -	$ 7,000	$ -
41,873	2024	54	$ -	589,002	$ -	$ 7,000	$ -
42,276	2025	55	$ -	565,643	$ -	$ 7,000	$ -
43,401	2026	56	$ -	638,526	$ -	$ 7,000	$ -
43,938	2027	57	$ -	499,575	$ -	$ 7,000	$ -
45,475	2028	58	$ -	562,092	$ -	$ 7,000	$ -
46,892	2029	59	$ -	568,892	$ -	$ 7,000	$ -
48,649	2030	60	$ -	501,493	$ -	$ 7,000	$ -
49,810	2031	61	$ -	634,337	$ -	$ 7,000	$ -
51,339	2032	62	$ -	732,902	$ -	$ 7,000	$ -
52,743	2033	63	$ -	851,585	$ -	$ 7,000	$ -
54,703	2034	64	$ -	868,384	$ -	$ 7,000	$ -
55,895	2035	65	$ -	1,050,102	$ -	$ 7,000	$ -
56,963	2036	66	$ -	1,156,227	$ -	$ 7,000	$ -
58,632	2037	67	$ 58,632	1,155,943	$ 23,089	$ -	$ 5,863
60,714	2038	68	$ 60,714	1,165,234	$ 25,440	$ -	$ 6,071
62,110	2039	69	$ 62,110	1,202,289	$ 26,017	$ -	$ 6,211
63,215	2040	70	$ 63,215	1,262,006	$ 26,446	$ -	$ 6,322
65,518	2041	71	$ 65,518	1,134,164	$ 27,416	$ -	$ 6,552
66,905	2042	72	$ 66,905	959,295	$ 28,243	$ -	$ 6,690
68,706	2043	73	$ 68,706	1,172,790	$ 28,694	$ -	$ 6,871
70,795	2044	74	$ 70,795	1,134,598	$ 29,654	$ -	$ 7,080
73,070	2045	75	$ 73,070	953,495	$ 30,107	$ -	$ 7,307
74,614	2046	76	$ 74,614	842,283	$ 30,339	$ -	$ 7,461
76,166	2047	77	$ 76,166	752,113	$ 30,771	$ -	$ 7,617
79,464	2048	78	$ 79,464	729,844	$ 31,364	$ -	$ 7,946
82,688	2049	79	$ 82,688	710,353	$ 32,215	$ -	$ 8,269
84,498	2050	80	$ 84,498	779,771	$ 32,869	$ -	$ 8,450
87,113	2051	81	$ 87,113	736,363	$ 33,410	$ -	$ 8,711
90,317	2052	82	$ 90,317	731,011	$ 33,802	$ -	$ 9,032
90,882	2053	83	$ 90,882	539,266	$ 34,909	$ -	$ 9,088
93,162	2054	84	$ 93,162	526,270	$ 35,353	$ -	$ 9,316
96,568	2055	85	$ 96,568	510,195	$ 36,551	$ -	$ 9,657
97,367	2056	86	$ 97,367	583,376	$ 37,634	$ -	$ 9,737
100,486	2057	87	$ 100,486	601,361	$ 38,269	$ -	$ 10,049
102,617	2058	88	$ 102,617	690,432	$ 39,279	$ -	$ 10,262
104,750	2059	89	$ 104,750	615,019	$ 40,344	$ -	$ 10,475
107,481	2060	90	$ 107,481	603,579	$ 40,457	$ -	$ 10,748
111,072	2061	91	$ 111,072	677,875	$ 41,541	$ -	$ 11,107
113,550	2062	92	$ 113,550	642,978	$ 43,005	$ -	$ 11,355
117,311	2063	93	$ 117,311	520,390	$ 43,877	$ -	$ 11,731
122,276	2064	94	$ 122,276	482,842	$ 45,476	$ -	$ 12,228
123,515	2065	95	$ 123,515	459,426	$ 46,465	$ -	$ 12,351
125,281	2066	96	$ 125,281	447,354	$ 47,415	$ -	$ 12,528
127,753	2067	97	$ 127,753	439,541	$ 48,510	$ -	$ 12,775
133,345	2068	98	$ 133,345	365,893	$ 49,809	$ -	$ 13,335
135,274	2069	99	$ 135,274	281,340	$ 50,317	$ -	$ 13,527
140,272	2070	100	$ 140,272	214,275	$ 51,281	$ -	$ 14,027

Source: Palisades Risk

well as different investment rates of return. Even if you were to start later than age 25, you can make up for this difference with an aggressive investment strategy. It gets more difficult to reach your goals the later you start saving. Even if someone were to start at age 40, they still would not be touching their retirement for at least 20 to 30 more years. This long period will allow them to weather any recessions and make a positive return over the long run.



For example, after the market dropped -57% in the 2008 great recession, it rose about 321% over the next 11 years. Meaning, if you did not sell in 2008, you would have netted around an 81% return over the next 11 years. This return is simply if you put your money into an S&P 500 index investment. There are many thoughts on the best way to invest your money, but a risk-managed, diversified and a blended approach between active and passive investing is likely the best approach over the long haul.



DIFFERENCE BETWEEN AN ACTIVELY MANAGED FUND AND A PASSIVELY MANAGED FUND STYLE

There are good arguments for both types of funds, but first, you need to know the difference. A **passively managed** fund is a fund whose investment securities are not chosen by a portfolio manager, but instead are automatically selected to match an index or sector of the market. An S&P 500 index fund is a passively managed fund with holdings and weightings that mimic the S&P 500. An **actively managed** fund is a fund in which a manager or a management team makes decisions. These decisions are about how to invest the fund's money and select the individual securities to add into the investment portfolio. So, which one is better? How does an individual decide on which strategy to implement? Well, there is nothing wrong with passively managed funds, just by putting the money into an index fund can give an investor good returns and help you grow your assets into retirement. An actively managed fund, however, allows for the possibility to maximize returns and minimize losses by actively monitoring the assets inside the fund. For example, in 2008 when the stock market was at its peak, an actively managed account could have switched over to a more conservative portfolio so it could minimize its exposure to the equity market. After the market hit the bottom the portfolio manager then could transition back into a more aggressive portfolio, and add back equities at a cheaper value. Keep in mind, this sounds great but is very hard to accomplish. However, as you accumulate larger amounts of wealth or are nearing retirement, your appetite for risk will naturally reduce and you will likely want to protect your assets and minimize your downside losses. **Active Management** becomes more important as you near retirement. Here are the numbers, assume: If you are 26 years old and have $1,000 saved in your 401(k) versus if you are 61 years old and have $1,100,000 saved in your 401(k) and the 2008 recession hits with a -57% drop in the market.

If both have 100% of their money in an S&P 500 index investment fund, the $1,000 account would reduce to $430 and the $1,100,000 account would reduce to $473,000 during the market drop. Now for the 26 year old with the $430 balance, it would not be that big of a deal because within 4 years, or by 2012, the 26 year old who is now 30 would have redeemed the $1,000 back and still will have 32+ years to grow and accumulate more assets in the portfolio for retirement. On the flip side, the 61 year old seeing their account drop down to $473,000 the year before they had planned to retire at age 62, would experience a very emotional event! It would be so emotional they might decide to pull entirely out of the S&P 500 stock index and decide they now have to work much longer until they get their account back to $1,100,000 utilizing safer investments such as CDs and money market funds. This is why it is so important to work with a financial advisor as you near retirement, usually 7-10 years ahead of time. The financial advisor will assess your risk and design a risk-adjusted portfolio so if a 2008 level recession hits while you're age 61 it will likely not cause a life changing retirement event. Active funds will be utilized with a blend or mix of passive funds to greatly reduce any shock a surprise recession may cause. This is proper financial planning!

PHASE TWO: HOW TO CREATE A DISTRIBUTION PORTFOLIO WHICH IS A SELF-MADE PENSION!

"THE MODERN DAY PENSION"

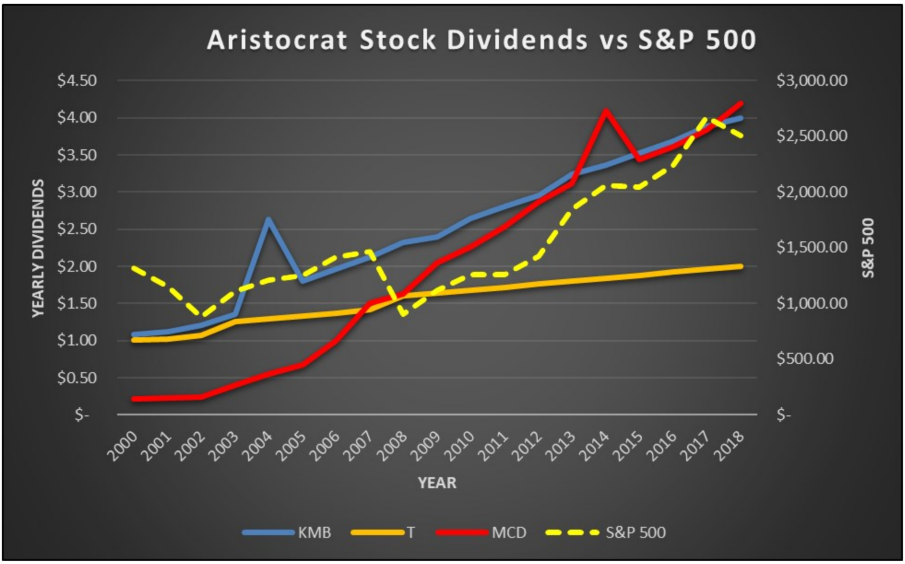
Now onto the important part of retirement, protecting your assets! Accumulating assets for retirement is important, but protecting the principal of those assets and getting the most out of your savings during retirement is the most important part. The transformation from an ***accumulation portfolio*** to a ***distribution portfolio*** is the most important step as you approach your retirement years.

The key part is transitioning away from an aggressive strategy of mutual funds that utilizes growth equities, into a cashflow strategy that utilizes high dividend paying stocks and fixed-income bond investments. **Cashflow can be used to describe investment earnings such as dividends and interest.** To describe cashflow payments are, and how individual investors can utilize them, we will provide certain examples of investments that pay dividends or interest. A dividend is a sum of money paid to shareholders that own a stock. Dividends come directly out of the company's profits. Dividends are typically paid either quarterly or annually. Whichever method is employed to disperse dividends is completely subject to the issuer of the stock. Fixed-income refers to any type of investment, which are normally bonds, where the issuer borrows principal and is obligated to pay a specified number of interest payments on a fixed schedule with a fixed principal payback amount in the future.

PART 1, CHOOSING HIGH DIVIDEND STOCKS

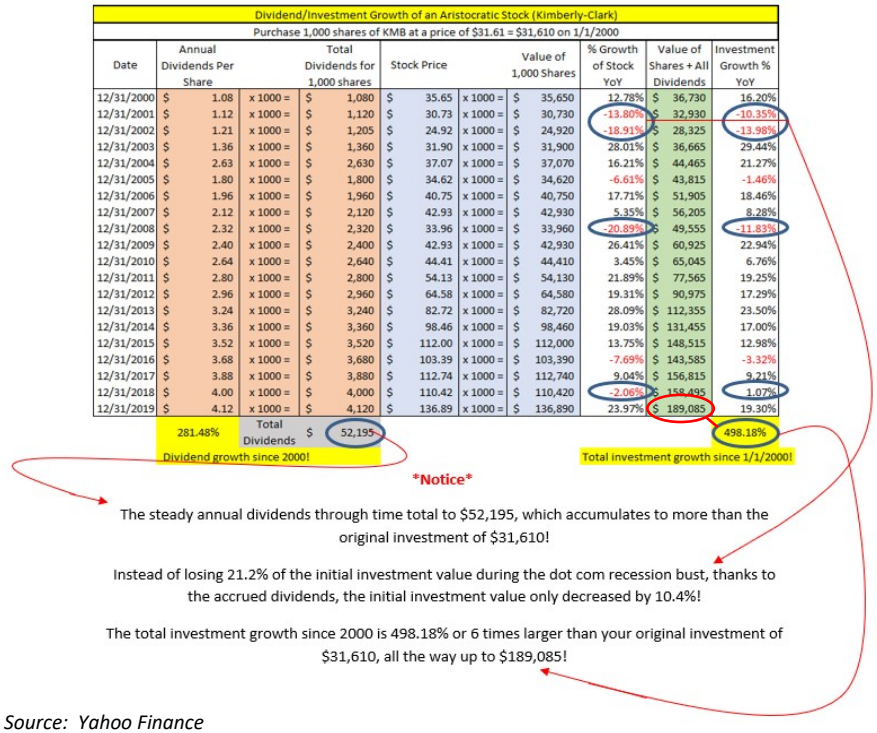
Some companies have consistently paid out dividends throughout history, also some have consistently increased their dividend amount each year. These companies who have a track record of achieving both for at least 25 years are referred to as "Aristocrats" (Wikipedia, "S&P 500 Dividend Aristocrats")[3]. These stocks are great to add into distribution portfolios because investors can be more certain they will receive their dividends throughout the year regardless of what matter what happens to the economy and the stock market. A few examples of companies with aristocrat stocks are AT&T (T), Kimberly-Clark (KMB), and McDonalds (MCD).

The chart on the following page shows how each of these companies have continuously increased dividends over time, no matter what has happened with the economy. You'll notice two separate occasions where the dividend amount spiked during certain years for both KMB and MCD. This can be attributed to those companies paying a special dividend those years.



Source: Yahoo Finance

This chart illustrates how these aristocrat companies continue to increase their dividends no matter what external factors may be working against them during any given year. A key concept to understand is dividends are declared on the number of shares owned, not the price of the stock. Assume a company announces their decision to raise their dividend from $0.40 up to $0.42. If you own 1000 shares of the stock that declared a $0.42 dividend you can calculate your dividend income by taking 1000 shares and multiplying by $0.42 which shows you will receive $420 in dividends for the year! Since dividends are calculated and declared on the number of shares owned it does not matter what the price of the stock is at any particular time. The dividend is paid independent of the what the stock is priced on the day of the payment. It is very important for retirees to understand this concept**. Strategically transforming a retiree's portfolio by building a stock portfolio, rather than holding stock mutual funds or stock ETFs, can create cashflow a retiree can count on in retirement, regardless of what the stock is priced or valued in the portfolio.** As with all investments, there is a level of risk involved with investing in stocks but the Aristocrat high dividend stocks have a steadier ride and history in their favor. The chart on the following page depicts how dividends can impact overall investment growth.



Dividend/Investment Growth of an Aristocratic Stock (Kimberly-Clark)

Purchase 1,000 shares of KMB at a price of $31.61 = $31,610 on 1/1/2000

Date	Annual Dividends Per Share		Total Dividends for 1,000 shares	Stock Price		Value of 1,000 Shares	% Growth of Stock YoY	Value of Shares + All Dividends	Investment Growth % YoY
12/31/2000	$ 1.08	x 1000 =	$ 1,080	$ 35.65	x 1000 =	$ 35,650	12.78%	$ 36,730	16.20%
12/31/2001	$ 1.12	x 1000 =	$ 1,120	$ 30.73	x 1000 =	$ 30,730	-13.80%	$ 32,930	-10.35%
12/31/2002	$ 1.21	x 1000 =	$ 1,205	$ 24.92	x 1000 =	$ 24,920	-18.91%	$ 28,325	-13.98%
12/31/2003	$ 1.36	x 1000 =	$ 1,360	$ 31.90	x 1000 =	$ 31,900	28.01%	$ 36,665	29.44%
12/31/2004	$ 2.63	x 1000 =	$ 2,630	$ 37.07	x 1000 =	$ 37,070	16.21%	$ 44,465	21.27%
12/31/2005	$ 1.80	x 1000 =	$ 1,800	$ 34.62	x 1000 =	$ 34,620	-6.61%	$ 43,815	-1.46%
12/31/2006	$ 1.96	x 1000 =	$ 1,960	$ 40.75	x 1000 =	$ 40,750	17.71%	$ 51,905	18.46%
12/31/2007	$ 2.12	x 1000 =	$ 2,120	$ 42.93	x 1000 =	$ 42,930	5.35%	$ 56,205	8.28%
12/31/2008	$ 2.32	x 1000 =	$ 2,320	$ 33.96	x 1000 =	$ 33,960	-20.89%	$ 49,555	-11.83%
12/31/2009	$ 2.40	x 1000 =	$ 2,400	$ 42.93	x 1000 =	$ 42,930	26.41%	$ 60,925	22.94%
12/31/2010	$ 2.64	x 1000 =	$ 2,640	$ 44.41	x 1000 =	$ 44,410	3.45%	$ 65,045	6.76%
12/31/2011	$ 2.80	x 1000 =	$ 2,800	$ 54.13	x 1000 =	$ 54,130	21.89%	$ 77,565	19.25%
12/31/2012	$ 2.96	x 1000 =	$ 2,960	$ 64.58	x 1000 =	$ 64,580	19.31%	$ 90,975	17.29%
12/31/2013	$ 3.24	x 1000 =	$ 3,240	$ 82.72	x 1000 =	$ 82,720	28.09%	$ 112,355	23.50%
12/31/2014	$ 3.36	x 1000 =	$ 3,360	$ 98.46	x 1000 =	$ 98,460	19.03%	$ 131,455	17.00%
12/31/2015	$ 3.52	x 1000 =	$ 3,520	$ 112.00	x 1000 =	$ 112,000	13.75%	$ 148,515	12.98%
12/31/2016	$ 3.68	x 1000 =	$ 3,680	$ 103.39	x 1000 =	$ 103,390	-7.69%	$ 143,585	-3.32%
12/31/2017	$ 3.88	x 1000 =	$ 3,880	$ 112.74	x 1000 =	$ 112,740	9.04%	$ 156,815	9.21%
12/31/2018	$ 4.00	x 1000 =	$ 4,000	$ 110.42	x 1000 =	$ 110,420	-2.06%	$ 158,495	1.07%
12/31/2019	$ 4.12	x 1000 =	$ 4,120	$ 136.89	x 1000 =	$ 136,890	23.97%	$ 189,085	19.30%
	281.48%	Total Dividends	$ 52,195						498.18%
	Dividend growth since 2000!								Total investment growth since 1/1/2000!

Notice

The steady annual dividends through time total to $52,195, which accumulates to more than the original investment of $31,610!

Instead of losing 21.2% of the initial investment value during the dot com recession bust, thanks to the accrued dividends, the initial investment value only decreased by 10.4%!

The total investment growth since 2000 is 498.18% or 6 times larger than your original investment of $31,610, all the way up to $189,085!

Source: Yahoo Finance

PART 2, ACQUIRING INVESTMENT GRADE BONDS

The next half of a distribution portfolio is the bond and fixed-income holdings. A bond is an agreement between a company or municipality and an investor. Think of this like a traditional mortgage. In this case, the investor is the lending bank and the company or municipality is the homeowner. The investor loans money to the company or municipality and in return, receives their principal back at a specified date in the future and receives semi-annual coupon interest payments. Coupon interest payments are contractually agreed upon interest payments from the issuer to the investor. For example, if an investor owns $10,000 of a 10-year ABC company bond paying 4%, they will receive $200 twice per year for 10 years collecting interest of $400 x 10 years = $4,000 of cashflow to live on in retirement. At maturity, their $10,000 principal would be paid back and if they add their interest to this it would be a total of $14,000. Owning the actual bond opposed to owning a bond mutual fund or

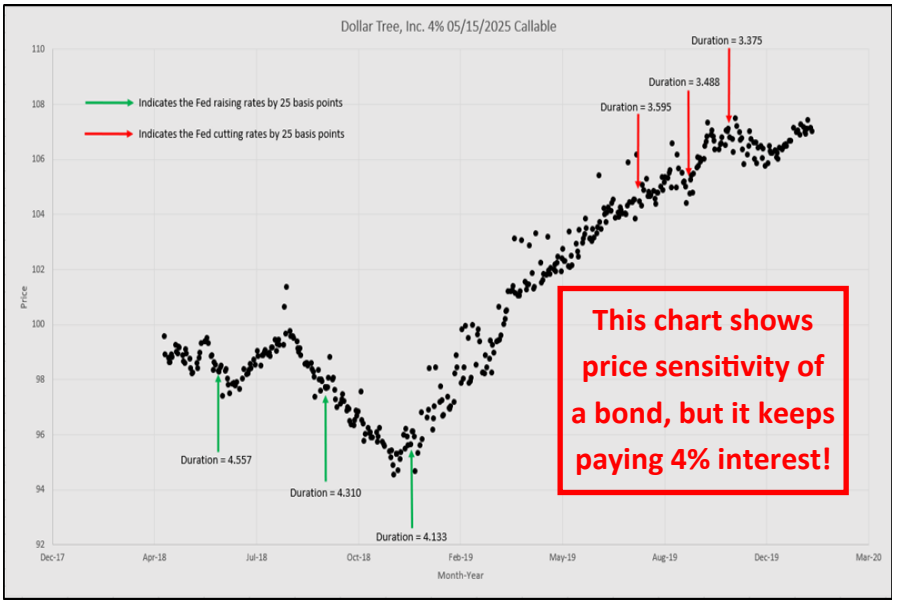
ETF gives investors a steady, reliable and predictable income stream to count on in retirement. As with all investments, there is a level of risk involved with investing in bonds or other fixed-income securities. The risk that a buy and hold bond investor faces is default risk. Companies and municipalities are rated by multiple large ratings agencies on their solvency, ability to repay debt, and likelihood of the company or municipality defaulting. Moody's, Standard & Poor's, and Fitch all rate companies and municipalities and assign these entities bond's credit ratings. The chart below shows the different credit ratings and how each depicts the bonds risk of defaulting.

Credit Quality	Moody's	Standard & Poor's	Fitch
Investment grade			
Prime	Aaa	AAA	AAA
High quality	Aa	AA	AA
Upper medium grade	A	A	A
Medium grade	Baa	BBB	BBB
Not investment grade (Junk bonds)			
Lower medium grade	Ba	BB	BB
Low grade	B	B	B
Poor	Caa	CCC	CCC
Highly speculative	Ca	CC	CC
Not paying/BK	C	C	C
Defaulted	C	D	D

Source: Moody's, Standard & Poor's, Fitch

Bonds are typically seen as a safer investment than stocks because bond or debt obligations are senior to those of equity/stock obligations. Therefore, if a company were to start failing and become bankrupt, debt holders will be entitled to receive full compensation on their investment before equity holders will be entitled to receive any sort of compensation. To put things into perspective of how safe investment grade bonds are, during 2008 there were 3,333 corporate investment grade bonds in circulation. Only 0.42% of them actually defaulted, 14 in total, which has been the most to default in one year over the last two decades (Vazza, Kraemer & Gunter, 2019, p. 3)[4].

Another important metric to understand when investing in bonds is duration. Duration is an approximate measure of a bond's price sensitivity to changes in interest rates. If interest rates rise, bonds will lose value in approximately the amount of percentage of the bond's duration. A simple example is if a bond has a duration of 6 years and the interest rates rise 1% then the value of this bond is likely to drop by 6%. Each 1% of interest rate rise affects bond prices inversely, or negatively by the amount of duration converted to a percentage. This is why you want to hold shorter duration bonds when the Federal Reserve is raising interest rates and hold longer duration bonds when the Federal Reserve is lowering interest rates! Therefore, duration is sensitive to interest rate fluctuations and is measured in years. The key items to understand about bonds is the interest rate coupon the actual bond is paying is not affected by the interest rate changes by the Federal Reserve, only the market value of the bond is affected temporarily until it matures if the Federal Reserve changes interest rates while you hold a bond. So, if you bought a bond paying 4% interest for the next 10 years, to get a nice 4% cashflow to live on, for $10,000 par it will continue to pay you 4% or $400 per year for the next 10 years and at maturity will pay you back the $10,000. (Note: this sounds a lot like dividends that Aristocrat stocks pay stock holders, it does not matter what the market value of the stock is because it keeps paying you the dividend to live off of!) During the next 10 years, the Federal Reserve could raise and lower interest rates and the market value of the $10,000 bond investment will oscillate according to the duration of the bond and what the Federal Reserve is doing to interest rates. **The lesson to learn is to buy prime market bonds to build your distribution portfolio not bond mutual funds.** Then if you are buying a bond for the 4% interest you will want to buy it and hold it until maturity! Once you own a bond, that you plan to hold to maturity, the actual market value of the bond is not important only the interest rate or cashflow it is paying you along the way! The bond, at maturity, will move back to the par price or the original amount you lent the borrower, so you get your original principal investment paid back. Bond prices move inversely in connection with interest rate changes.



Source: Charles Schwab

The chart above shows the impact on a bond's price as interest rates rise and fall. The distribution portfolio is comprised of two major categories of investment holdings which are: high dividend paying stocks and prime market bond holdings that are laddered by maturity with different durations. Foresight recommends transforming your portfolio from the traditional mutual funds and exchange traded funds, found in most 401(k) and 403(b) retirement accounts, to a distribution portfolio as you near retirement. This distribution portfolio does two things: 1) It helps protect against market volatility and 2) it increases the cashflow yield from the portfolio. It stabilizes the cashflow from the portfolio so it is dependable. Remember, it does not matter if the market value or statement value happens to be lower, due to a recession, the portfolio continues to pay the dividends and interest cashflow you designed in the portfolio! Think of the cashflow from the distribution portfolio as a barge in water; the waves may get bigger but the barge does not take on water, it keeps moving gently towards its destination! This is what retirees should strive to create as they enter retirement.

THE IMPORTANCE OF CASHFLOW

When saving for retirement an investor is more concerned about returns, but during retirement an investor should be more concerned about cashflow (the amount of dividends and interest your investments earn consistently each year). The reasoning behind this is that during the accumulation phase an investor is trying to build the principal of the retirement portfolio to get it as big as possible. During the distribution phase, a retiree wants to be able to live off of the portfolio without touching the principal, so cashflow is paramount!

Let's say you buy 100 shares of Coca-Cola for $50 a share. Each share pays an annual dividend of $4, and the current stock price has risen to $80 since you purchased the stock one year ago. The total annual dividends from the investment total up to $400 since you own 100 shares. In order to understand this, you need to know the formula used to calculate the dividend yield. The formula for dividend yield is as follows:

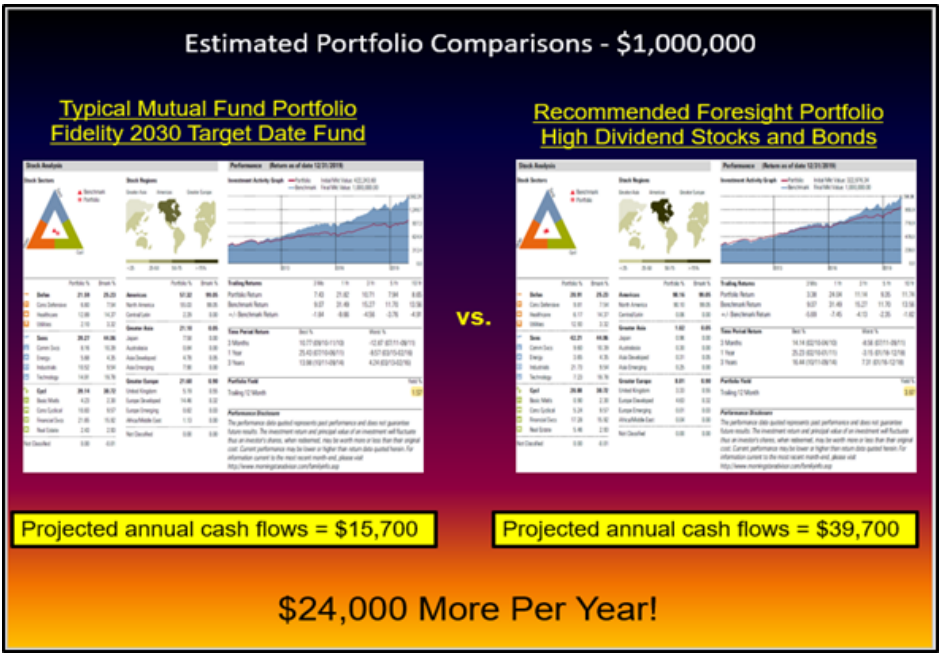
$$\text{DIVIDEND YIELD} = \frac{\text{ANNUAL DIVIDEND \$S PER SHARE}}{\text{CURRENT STOCK PRICE PER SHARE}}$$

Using the formula above, we can calculate the dividend yield by dividing $4 by $80. This gives us a dividend yield of 5%. The price of the Coca-Cola stock will change throughout the year, but you are going to continue getting $4 per share in dividends (or $400) during the year as promised by Coca-Cola. At Foresight, we try to find companies that have consistently raised their annual dividends throughout the history of the company, to increase cashflow in your distribution portfolio.

So, after taking this into consideration, let's amplify the effect. Let's say you have one million dollars in your portfolio. Foresight can transition that money and invest it into a portfolio consisting of bonds and high dividend paying stocks.

The one-million-dollar high dividend stock and bond portfolio can produce a yield much greater than a typical target date fund which is what most employers direct their workers in to within their 401(k) plan.

The chart below illustrates how an average 2030 target date fund will yield around 1.57% totaling $15,700 of cashflow annually compared to a distribution portfolio that has been transformed by Foresight, which can generate a yield around 2.5x greater, totaling $39,700 of cashflow annually.



Source: Morningstar

The "Self-Made Pension" or "Modern Day Pension" produces $39,700 annually or $24,000 more per year in cashflow, in a one-million-dollar portfolio! This cashflow does not fluctuate like the principal does. The principal will fluctuate daily based on how the individual stocks and bond interest rates move, but the yield will consistently stay around 4%. This allows a retiree to be able to rely on consistent cashflows from their investment portfolio, just like you would from a pension! This makes retirement much easier and far less stressful for retirees.

HOW THE YIELD STAYS CONSISTENT

The yield is likely to stay relatively consistent, because the stocks that Foresight purchases for retirees are constant dividend paying companies, like AT&T and Coca-Cola. Foresight also has a trading team that constantly monitors these companies weekly to make sure they are continually working and improving their business practices. On top of that, the trading team is continuously looking for bonds with high credit quality ratings that can be added into distribution portfolios that will consistently pay out their coupon interest payments for cashflow. The trading team also does what is referred to as laddering, which is buying multiple bonds with different interest coupon and maturity dates so that way the portfolio will be generating monthly payments throughout the year, due to the fact that most bonds pay out their coupon interest payments semi-annually.

TYPES OF PLANS TO SAVE FOR RETIREMENT:

401(k), 403(b), AND 457 PLANS

A 401(k), 403(b), and 457 plans are offered by employers to help employees save for retirement, and most employers offer one of these plans. What a 401(k), 403(b), or 457 does is allow an employee to contribute a certain portion of their paycheck into an account, tax free or post-tax Roth savings, until withdrawals start at retirement. Some employers offer matching contributions as well! This simulates the way saving for a pension used to happen, just on an individual basis. Also, a participant is discouraged from touching their 401(k), 403(b), and 457 until they reach the age of 59 ½, making it easier to let the money sit in the account and grow by compounding earnings all the way up until retirement.

INDIVIDUAL RETIREMENT ACCOUNTS (IRA)

An individual retirement account (IRA) is similar to a 401(k) with one key difference; a 401(k) is through an employer, but an IRA is opened by an individual in addition to their employer plan. There are 3 main types of IRAs: Traditional IRA (Pre-Tax), Roth IRA (Post-Tax), and Non-Deductible IRA. Employees are able to max-fund their employer retirement plan and fund an IRA each year. Work with your tax advisor each year to determine which IRA is best for you to fund. The Non-Deductible IRA can be used to fund a "Back-Door" Roth IRA. The "Back-Door" Roth IRA is an advantageous strategy to lower your RMD (required minimum distribution), which now begins at age 72 with the recently passed Secure Act of 2019[4]. Contact Foresight if you want more information on how to accomplish this maximized yearly savings!

SOLO 401(k) OR INDIVIDUAL 401(k) PLAN

A Solo 401(k) is designed for self-employed workers. This plan is very similar to any other traditional 401(k) plan that solely covers a business owner who has no employees. This plan covers only the owner and the owner's spouse with the same rules and regulations as any other 401(k) plan. Solo 401(k)s allow you to choose which type of tax advantage you would like to utilize; Pre-Tax and/or Roth deferrals. You have the option to choose a traditional 401(k) where contributions are not taxed and distributions are, or you can choose the Roth 401(k) option which taxes contributions and allows the beneficiary to grow and withdrawal money tax free. If your spouse earns income from your business, they will be allowed to make elective deferrals into the plan as well. Also, as the employer you can contribute up to 25% of your earnings and your spouse can also contribute 25% of their earnings under the plans profit-sharing initiative. The Solo 401(k) is a great plan for entrepreneurs, small business owners who operate by themselves or with their spouse. Contact Foresight for further information on opening a Solo 401(k) for your small business.

ANNUITIES

Annuities can be a nice investment addition at or near retirement to add cashflow to a distribution portfolio or to utilize later in retirement for healthcare or long term care needs. This booklet does not cover the details of adding annuities to distribution portfolios but Foresight does recommend certain NAPFA (National Association of Personal Financial Advisors)[6] approved annuities to enhance cashflow in later years under certain conditions when needed. The NAPFA organization has recently completed a due diligence project regarding annuities and has recommended annuities that offer reasonable income riders for a fair price, which can be offered by fee-only advisors like Foresight. There are annuities that have income riders that guarantee to double your investment in 10 years and return 7.2% yearly! Contact Foresight if you are interested in learning more about annuities and how to add them to a retirement portfolio.

CONCLUSION:

Retirement used to be a simple process; work until you reach a certain age and once you retire you will have a pension and social security to live off of for the rest of your life. Now-a-days, pensions are becoming more and more rare and social security is shrinking as life expectancies are rising. This sounds scary, but as described in this booklet, it is easily manageable! In some ways it's even better. It used to be that someone would have to work for over 30 years with the same employer in order to receive their pension. Now the "Self-Made Pension" or "Modern Day Pension" is no longer tied to an employer, individuals have more freedom due to the fact that they are creating their own pensions. A financial advisor can help strategically invest the money for you, increasing chances of a successful retirement by assisting with the transformation of your mutual fund portfolios to distribution cashflow portfolios as you enter retirement. Hence, the Modern Day Pension is created!

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