Investors' Edge

An Exclusive Newsletter for RBC Wealth Management Investors

SECOND Quarter 2012

INSIDE THIS ISSUE

Planning for Retirement Income? Consider All Your Options

When you're nearing your retirement years, and even when you've recently retired, you'll probably have a lot of questions related to your finances. But the most important thing you can ask yourself will likely be this: How can I be confident that I won't outlive my money?

As you might expect, there's no simple answer to this question — although many people are certainly thinking about it. In fact, in one recent survey, 61% of respondents said that they were more afraid of outliving their assets than they are of dying.*

Fortunately, you can take a variety of steps to help yourself feel more confident about your future financial security. Here are a few suggestions for retirement income planning:

- **Plan for Inflation.** Some people rely on certificates of deposit (CDs) and other fixed-rate investments to help provide income during their retirement years. Yet, if you were to retire today, when short-term interest rates are at historically low levels — and are likely to remain near zero until late 2014, according to the Federal Reserve — the income you receive from your CDs

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would not even keep up with the mild inflation rate we've been experiencing. Consequently, during your retirement years, you'll want to consider the interest-rate environment when you make investment choices.

- **Build a "Ladder."** Even if interest rates are low when you retire, you can still make good use of fixed-income vehicles in your retirement income planning by building a "ladder" with bonds or CDs of varying maturities. Once you've constructed your ladder, you could gain some advantage in various interest-rate environments. When market rates are low, you'll still have your longer-term bonds or CDs earning higher interest rates, thereby paying you more income. And when market rates rise, you can reinvest your maturing short-term bonds and CDs at the higher rates.
- **Seek Sources of Rising Income.** As mentioned above, inflation is a source of concern for you during your retirement. In fact, if inflation averaged just 3% a year, you could lose about half your purchasing power in 25 years — and given the advances in health care and longer life span, you could certainly spend two, or even three, decades in retirement. You can help overcome inflation by owning dividend-paying stocks — in particular, stocks that generally raise their dividends year after year. (Keep in mind, though, there are no guarantees, as companies can reduce or discontinue dividends at any time.) Incidentally, if you were to retire this year, you might have an abundance of possibilities, as corporate balance sheets could see double-digit increases and dividend payouts should be strong.
- **Don't Be Too Conservative.** Many people fear taking any chances with their money during their retirement years. Yet, as we've seen, so-called "safe" investments, such as CDs, carry purchasing-power risk, and individual bonds are subject to interest-rate risk — the risk that their prices will fall as interest rates rise. During your retirement years, you should consider devoting a portion of your portfolio to growth-oriented investments, such as stocks and stock-based mutual funds. And you may be able to ramp up your income somewhat by owning a small percentage of "aggressive income" vehicles, such as high-yield bond funds or emerging market bond funds.

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- **Determine a Sustainable Withdrawal Rate.** Once you're retired, you may have to draw on all your assets, including the money you've accumulated in your 401(k), IRA and other investments. To make these accounts last as long as possible without lessening your quality of life, you'll need to follow a disciplined withdrawal strategy. The percentage of your portfolio that you withdraw every year should be based on your total investment assets, your other sources of income and your individual lifestyle.
- **Create an Income Stream That You Can't Outlive.** In addition to investing in an IRA and your 401(k), you might want to consider purchasing a fixed annuity. Similar to a traditional IRA and a 401(k), a fixed annuity offers earnings that can grow on a tax-deferred basis. Also, fixed annuities generally offer some type of guaranteed rate of return over the life of the annuity contract. And perhaps most importantly, you can structure your annuity to provide you with an income stream you can't outlive.**
- **Consider Delaying Social Security.** You can typically start collecting benefits as early as age 62, but you'll get substantially larger monthly checks if you wait until your "full retirement age," which is between 65 and 67, depending on what year you were born. You'll get even greater monthly benefits if you delay collecting them until you're past your full retirement age, and your benefits will peak once you reach 70. Your decision on when to take Social Security should be based on your family's history of longevity, your personal health

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"Bucket" Strategy Can Pay Off Now... and Later

When you're managing your finances, you might create various "buckets" to meet different needs. For example, in one bucket, you might keep a savings or checking account for your day-to-day expenses, while in another bucket, you might maintain a separate checking account to pay your mortgage. If this system works well for you, you might be interested to know that you can also employ it to manage your investments.

Different investment theories have identified different numbers of buckets. But one popular approach is the three-bucket model:

Bucket 1: This bucket is designed to help you meet short-term, unexpected needs, such as a major car repair, a new furnace, a large bill from the doctor and so on. This bucket contains liquid, low-risk vehicles, such as CDs, money market funds and U.S. Treasury bills.

Bucket 2: In this bucket, you'll want to keep investments that can provide you with income in the near future, perhaps five to 10 years, for goals such as college for your children or grandchildren. This bucket might contain a mix of mutual funds, including those specializing in both small- and large-capitalization companies and those with an international component. It might also contain short-term bonds and some types of exchange-traded funds (ETFs), which look like mutual funds but trade like stocks.

Bucket 3: This third bucket is for those investments that, ideally, you wouldn't touch for 10 years or longer — in other words, it's designed to provide you with money that you might need in retirement (assuming that's at least 10 years away) or that you may want to include as part of your estate. Given its longer time horizon, this bucket contains investments that will fluctuate more in the short term, but, in exchange, can provide more long-term growth potential. These types of investments may include both growth and value stocks and growth-oriented mutual funds.

While buckets present a visually interesting way of thinking about your various investment needs and goals, it's important to keep in mind that you can achieve the same effect by integrating the three buckets into one comprehensive, diversified portfolio. Still, the idea of the three buckets may serve to remind you that different investments have different objectives — and you need to always be aware of why you own different investment vehicles and what you can expect from them. ■

2012 Could Be Good Year to Establish Dynasty Trust

Estate planning can be complex and time-consuming. Fortunately, however, you don't have to do it all at once. But if you have a high net worth, and you'd like to maximize the benefits of one potentially important estate-planning tool, you may find that 2012 is the year to take action.

Specifically, you may want to consider establishing a dynasty trust, which is designed to provide income to future generations of your family. By placing your assets in a dynasty trust, you can help protect these assets from estate taxes and from the consequences of divorce, the actions of creditors and the uncontrolled spending of any of your heirs.

Your contributions to a dynasty trust are considered taxable gifts, but you can minimize or even avoid gift taxes by applying your lifetime gift tax exemption, which, in 2012, is $5.12 million. At the same time, gifts to generations beyond your children — such as your grandchildren or great-grandchildren — are considered a generation-skipping transfer (GST) and are subject to the generation-skipping transfer tax. However, you can make a transfer up to the GST exemption amount, free of GST taxes — and, in 2012, this exemption amount is also $5.12 million.

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2012 Could Be Good Year to Establish Dynasty Trust, Continued

In fact, the federal estate tax exemption is also $5.12 million through the end of 2012. These exemption amounts — for gift, GST and estate taxes — are the highest they've been in decades. Plus, married couples can combine their exemptions and transfer up to $10.24 million before being subject to taxation. But in 2013, without a change in tax laws, these exemptions are all scheduled to revert to $1 million, and the maximum estate and GST tax rates will increase from 35% to 55%.

Of course, Congress may act to alter these figures for 2013 and beyond. But given the country's current and projected fiscal conditions, the estate, gift tax and GST exemptions may not be this high for quite some time — and maybe never again. And that means that 2012 may be the perfect year to establish a dynasty trust.

Dynasty trusts are complex and irrevocable, so you'll need to consult with your legal and tax advisors before taking action. Don't wait too long, though, because 2012 will be over before you know it.

To learn more about establishing and funding a Dynasty Trust, please call soon, as this is a time-sensitive opportunity that will expire at the end of 2012. ■

It's Never Too Soon to Start Funding Your IRA

You may have just finished your taxes a few weeks ago. And if you're like many people, you made some "11th hour" contributions to your IRA for the 2011 tax year. Now, you've got until April 15, 2013, to contribute to your IRA for 2012 — but why wait?

You could have started contributing to your IRA for 2012 on January 1. And if you fully fund your IRA each year in early January, as opposed to waiting until mid-April of the following year, you'll give your money 15 extra months of growth potential. If you factor in all the years you'll be contributing to your IRA before you retire, those extra months of growth opportunities, repeated over decades, could provide you with a significant amount of extra cash when you start tapping into your IRA at retirement.

In 2012, you can put in up to $5,000 to a Roth or traditional IRA, or $6,000 if you're 50 or older. If you can contribute the whole amount at once, consider doing so. If not, here are a few suggestions for helping you fund your IRA as early in the year as possible:

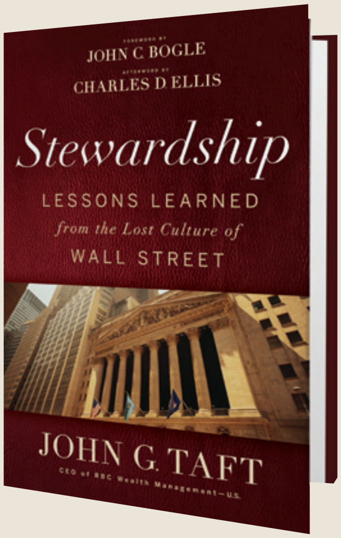
- Use your tax refund. In 2011, the average tax refund was about $3,000, according to the IRS. If you received that amount in 2012, and you applied it toward your IRA, you'd already be more than halfway toward the contribution limit, if you're younger than 50, and you'd be exactly halfway there if you're 50 or older.
- Use dividends or interest payments. Your income-producing events can help you fund your IRA. If you own dividend-paying stocks, and you don't reinvest the dividends, consider putting some of them into your IRA. You can do the same thing with interest payments from bonds. (Keep in mind, though, that you'll need earned income that's at least equal to the amount of dividends or interest payments going to your IRA.)
- Set up automatic investments. As long as you have earned income, you can also have your bank automatically move money each month from your checking or savings account to your IRA. Or use the additional income you receive as a result of the continued FICA tax reduction in 2012.

An IRA is a powerful retirement-savings vehicle. Your earnings grow tax-deferred in a traditional IRA, and tax-free in a Roth IRA, provided you don't start taking withdrawals until you're 59½ and you've had your account at least five years. Plus, you can fund your IRA with virtually any type of investment you choose — stocks, bonds, mutual funds, government securities, CDs and more.

Given these benefits, it's clear that an IRA should be part of your retirement-savings arsenal. And given the added growth potential you'll gain by consistently funding your IRA early in the year, you have an incentive to get started now. ■

“Stewardship” Examines Values-Based Investing

All of us focus a great deal on our individual investment choices and what they mean for our own goals. But it’s also a good idea to step back once in a while and take a look at the big picture. That’s exactly what you’ll get from *Stewardship: Lessons Learned From the Lost Culture of Wall Street,* written by John G. Taft, CEO of RBC Wealth Management – U.S.



Mr. Taft writes that the last four years of economic uncertainty and market volatility may actually impart valuable lessons of hope to investors — lessons that ultimately can help restore investor confidence in the financial system and markets.

In this book, Mr. Taft looks back at the economic crisis of 2008-09 and identifies several causes. Some of them are technical in nature, but others are clearly related to the failure of certain Wall Street firms and their leaders to fulfill their stewardship responsibilities — by putting their own interests ahead of those of their constituencies.

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Also, Mr. Taft reviews the regulatory reforms currently underway and offers practical ideas for investors to explore, with the help of their financial advisors, so that they can prepare for the future of the investment world. And he discusses how investors can use principles of environmental, social and governance investing (sometimes referred to as socially responsible investing) to help achieve their own objectives while simultaneously serving the best interests of society and the planet.

If you would like to gain some added insights into the investment world of which you’re a part, while learning more about prudent, long-term, values-based investing, check out *Stewardship* at your local bookstore or online. All proceeds from the book will be donated to charity. ■

Planning for Retirement Income? Consider All Your Options, Continued

and your other sources of income. You’ll also need to consider your employment status. For example, if you’re between 62 and your full retirement age, you’ll lose $1 in your Social Security benefits for every $2 you earn above $14,640. During the year in which you reach your full retirement age, you’ll lose $1 in benefits for every $3 you earn above $38,880. (All figures are for 2012.) After you reach your full retirement age, you can earn as much as you want without losing any benefits.

The above suggestions aren’t the only ways to boost or manage your retirement income — but they should give you some ideas to think about.

At RBC Wealth Management, we have developed a systematic process to help you manage risk and achieve a reliable, steady stream of income. To learn more about the RBC Retirement Income Planning process, please call. ■

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