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THE VIEWPOINT

Spring 2007

When you are evaluating how your investment portfolio performed you should not focus on past annualized returns alone. Those numbers can be deceiving because they tend to smooth out the underlying volatility of the portfolio. This volatility can have a dramatic effect on how much money you have and how long it will last when you are in the distribution phase of your life. You need to pay particular attention to the potential downside risk during this stage. This is not critical during the accumulation phase, although volatile markets can give you a queasy stomach.

The accumulation phase is the period of time when you are adding to savings and building equity. It may have started with the first nickel that you socked away from selling lemonade in front of your house, and it may last from 35 to 45 years or longer. During this phase, time is a luxury. If you invest \$1,000 when you are 20 and your average annual return is 8% per year, it will become \$31,920 by the time you turn 65. On the other hand, if you wait until you are 40 it will be only \$6848. The sooner you get started the better.

The length of the accumulation phase allows you to go through periods with low returns or negative returns like the early 2000's and the aftermath of 9/11. The important part of this phase is having a savings plan and continuing to invest prudently no matter what is happening in the markets. Taking a little extra risk and living with more volatility is okay because time is on your side.

The distribution phase is when you live off the investments you made during the accumulation phase. This phase has become longer as life expectancies have grown. If you live to retirement age you have a 20%

chance of seeing your 90th birthday. If you are married there is a better than 50% probability one of you will reach your 90th birthday. With individuals living longer planning and saving for the distribution phase is more important than ever.

In the distribution phase your portfolio must withstand the ups and downs of the market while providing an income stream for you to live on. This magnifies the effect of market downswings.

As you can see on the chart, the ending dollar amount is virtually the same for the less volatile and more volatile portfolios during the accumulation phase. That is not the case during the distribution phase. Even though the average return is the same, the less volatile portfolio is worth an additional \$4854 than the more volatile

portfolio. Notice also that the less volatile portfolio had lower returns in each period except for one, so don't be overly impressed by big returns in one period.

During the distribution phase, when you are depending on your investments for your living expenses, the volatility of those investments becomes critical. Wide downswings in value are exaggerated by the income distributions thus making it harder to recover. This can seriously undermine how much money you have and/or how long your money will last. It would be better to accept lower upside potential in favor of lower portfolio volatility to protect your portfolio distributions.

<u>Less Volatile Returns</u>		<u>More Volatile Returns</u>	
Accumulation Phase No Withdrawal			
Average Annual Return 8%	Initial Invest	Average Annual Return 8%	Initial Invest
9.12	\$100,000	10.15	\$100,000
2.13	109,120	-22.15	110,150
8.74	111,444	28.62	85,752
11.12	121,184	11.40	110,294
9.09	134,660	19.56	122,867
	146,901		146,900
Distribution Phase \$8,000 Withdrawal Per Period			
Average Annual Return 8%	Initial Invest	Average Annual Return 8%	Initial Invest
9.12	\$100,000	10.15	\$100,000
2.13	101,120	-22.15	102,150
8.74	95,274	28.62	71,524
11.12	95,601	11.40	83,994
9.09	98,232	19.56	85,569
	99,161		94,307

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