The FINANCIAL SUCCESS Library

Money Minute

Financial Planning & Investing Newsletter

"Smart Ideas for Secure Finances"

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Inside This Month's Issue:

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FEATURE

Is an Annuity the Solution to Retirement Income Needs?

In the August issue of this newsletter, I examined a handful of strategies for creating income during retirement. Last month, I took and in-depth look at one of my favored investment vehicles for creating income during retirement: high-yield bonds and bond funds. While I do use these investments extensively for many of my clients, using high-yield bonds to create income during retirement represents a relatively aggressive approach...as I illuminated in detail last month. This month, I will take a closer look at what is perhaps the most conservative approach to creating retirement income: an immediate annuity.

Immediate Annuity Basics

Whether you are currently retired or 25+ years away from retirement, the details surrounding this topic (retirement income) are of tremendous importance as far as financial planning topics are concerned. The word "annuity" is used in many contexts, but in the case of an immediate annuity, it represents an income stream to the recipient of the annuity. After accumulating a lump sum of cash, a person can purchase an immediate annuity from a life insurance company and, essentially, trade that lump sum of cash for monthly payments.

-For example, a 65 year-old male could make a $100,000 premium payment in exchange for monthly payments of $561 for his lifetime.

Once the $100,000 premium is paid, the man cannot access his initial investment from the insurance company. At the same time, the insurance company cannot decide to stop making payments and refund the money at any point.

Annuity Payout Options

The most obvious risk for the male in the above example is the risk of dying after only a few years of payouts. For example - if he dies at age 68, he would receive a mere $20,196 in payments for his $100,000. As you might expect, there are a host of payout options designed to protect the man:

-The man can specify a life with 10-year or 20-year guaranteed payout period,

(Continued on page 4)

QUOTE OF THE MONTH

"Education is a progressive discovery of our own ignorance."

~ Will Durant
Writer

(1885 - 1981)

DID YOU KNOW ?

Drug companies Bristol-Myers Squibb and Ono Pharmaceuticals recently launched a cancer-fighting drug called Opdivo in Japan, which will cost $143,000 per patient.

Source: Wall Street Journal

Potpourri ---Stock, Company & Market News and Notes---

Home Depot Suffers Customer Data Breach, Tesla Factory Decision, etc.

Home Depot (HD) announced it suffered a massive data breach that compromised the credit and debit card information of roughly 56 million customers. The breach dated back to April of 2014 and was discovered in early September. The company is offering customers whose payment information was compromised a free year of credit monitoring. **Target (TGT)** suffered a similar breach late last year, which affected roughly 40 million people.

The company's stock price fell roughly 5% following the news but has since recovered. The company has been on a tear since 2011, seeing shares rise from the low $30s to the low $90s amidst a housing market recovery and increased sales as Americans once again open their wallets to improve, renovate and upgrade their homes.

Apple (AAPL) sold a record 10 million units of its newly-introduced iPhone 6 during its first week of sales. Supply constraints likely dampened those figures somewhat according to CEO Tim Cook. The company is projecting a staggering $37 - 40 billion in sales during the 4th quarter of 2014, and shares are now back to previous highs set back in September of 2012 - just over $700 per share then, and just under $100 per share now after a 1 for 7 stock split. Rival Samsung pushed its release date ahead for its updated Note 4 phone-tablet hybrid, a.k.a. "phablet."

Tesla Motors (TSLA) announced it has chosen a site in Nevada for its yet-to-be-built battery factory. The factory will be a joint venture with Panasonic and will cost an estimated $5 billion. The new factory will have ready access to lithium, a key raw material in the batteries used in its automobiles. The company's Model S all-electric sedan currently carries a base price of $71,000, but Tesla announced plans for a new, more mainstream Model III sedan costing somewhere around $35,000. Reducing the cost of the batteries is key to achieving this price point, and the factory is scheduled to be completed by 2017. Arizona, California, Nevada, New Mexico and Texas had all been competing for the factory and had offered as much as $500 million in incentives to Tesla.

General Electric (GE) announced it sold its appliance division to Swedish company Electrolux for $3.3 billion. GE has grown into an industrial powerhouse by building aircraft engines, locomotives, medical imaging equipment and turbines over the past two decades, and these higher-margin businesses have far greater growth potential and importance to the company compared to the relatively low-margin, low-tech appliance business. The company posted $146 billion in revenue in 2013, with just $5.7 billion of that coming from the appliances division. Shares were down less than 1% on news of the deal. Electrolux will still sell appliances under the GE brand. Electrolux already owns the Frigidaire, Westinghouse and Kelvinator brands of appliances.

Alibaba (BABA), the Chinese equivalent of eBay, PayPal, and Amazon rolled into one, recently completed an initial public offering of common stock on the New York Stock Exchange. The stock closed up 38% on its first day of trading, valuing the company at $231 billion. The IPO was the biggest in U.S. history, as the company raised $21.8 billion dollars. The company is - for the moment - the 12th largest company listed on an American stock exchange.

Bond investing legend **Bill Gross** left his post at **PIMCO** (Pacific Asset Management). Gross founded the firm and ran its flagship Total Return bond fund, which held north of $250 billion at its peak, but poor performance in recent years saw outflows from the fund and the firm, which is owned by German insurer Allianz AG. PIMCO manages a mind-blowing $2 trillion in assets but is expected to see that figure decline amidst Gross' exit. Gross had earned as much as $200 million in recent years and has a sterling track record dating back to the early '90s, but he made incorrect bets over the past two years that led to poor performance for the fund. $10 billion of redemptions occurred on the day of the announcement alone, and analysts expect $200 - $500 billion will eventually flow out. PIMCO's funds are ubiquitous inside of 401(k)s and other retirement plans.

Market and Economic News

-Economic growth (measured by gross domestic product (GDP)) for the 2nd quarter of 2014 was once again revised upward to +4.6% (from +4.2%). The first reading for the 3rd quarter will come later this month

-The U-3 unemployment rate dropped to 5.9% in September from 6.1% the previous month, its lowest reading in over 6 years. 248,000 non-farm payroll jobs were added last month, a solid reading from last month's disappointing 142,000 (revised to 180,000).

-Global stock markets sold off sharply in early October and retreated from all-time highs. The pullback is threatening to erase the modest 2014 market gains in major indices.

At a Glance...
(as of October 7) **DJIA** – 16,719 **S&P 500** – 1,935 **NASDAQ** – 4,385 **10-yr T-note** – 2.35%

Readers' Q&A

Questions? E-mail Brad@R1FinancialGroup.com

Q. "Why do financial companies often say you need to save so much money to retire ($2+ million)? Those amounts seem very high for most people."

-Jeremy – Fort Worth, TX

A. The amount you should save for retirement is very dependent on your current income and what lifestyle you'd like to live during retirement. As a rule of thumb (which I hate using in most cases), a ballpark figure of 15-25 times your current gross annual income is probably not far off for most people. Here are a few reasons these projections may seem high:

-**Inflation** - a dollar will buy fewer goods and services in the future than it will today. For example, if you are 40 years old now and want to retire in 25 years, be aware that $1.00 in the year 2039 may buy less than half of what $1.00 buys in the year 2014. (That is assuming a 3% annual rate of inflation.) This is the biggest reason why future projections of how much you'll need to retire comfortably often seem so large. Also, remember inflation will continue throughout your retirement, which could last 25-30+ years.

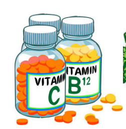
-**Health care costs** - most projections anticipate needing a sizeable cushion of cash to pay for anticipated health care costs.

-**Low interest rates** - current projections you see may be relying heavily on today's unusually low interest rates. A more normal interest rate environment could reduce how much you need to save, depending on what assumptions and methods will be used to create income.

-**Conservative outlooks** - some projections likely estimate high due to uncertainty in the level of social security payments in the future, as well as uncertainty related to life expectancy for a given retiree. Others may simply over-estimate and encourage you to save more than you may actually need (which is probably not a bad thing).

One thing that is clear: if you want to retire comfortably and not alter your current lifestyle (this last part is key), you will almost certainly need a lump sum of somewhere in the range of 15-25+ times your current gross annual income. Those who can taper back their lifestyles and expectations can probably make do with less. As daunting a task as it sounds, accumulating a large sum is achievable if you start early, save / invest regularly and achieve decent returns over time. I'll highlight some facts and figures related to accumulating a sizeable nest egg in next month's feature story.


YOUR HEALTH




Low Sodium Diets: Do They Do More Harm than Good?

Long-standing recommendations for low-sodium diets are under heavy scrutiny after results from a comprehensive study suggest low-sodium diets actually pose health hazards. Guidelines from the American Heart Association, the World Health Organization and other agencies suggest daily maximums of 1,500 to 2,300 mg of sodium intake per day, and the average person in the U.S. consumes about 3,400 mg. A recent study, whose findings appeared in the New England Journal of Medicine, tracked over 100,000 people from 17 countries over a three year period and found that those consuming fewer than 3,000 mg per day had a 27% higher risk of death or serious event such as heart attack or stroke compared to individuals who consumed 3,000 - 6,000 mg per day. Sodium is one component of salt and is a nutrient that is key to many cellular functions. Too little sodium can trigger hormonal responses from the body that actually increases blood pressure. Very low sodium was associated with a higher concentration of lipids in the blood stream, a risk factor for cardiovascular disease. Current guidelines are based largely on studies showing that a low-sodium diet can reduce blood pressure in individuals already suffering from hypertension, a.k.a. high blood pressure.

All do not agree with the study's conclusion. Researchers at Harvard's School of Public Health estimate that there were 1.65 million deaths in the year 2010 due to cardiovascular issues associated with high sodium intake. On average, roughly 75% of sodium intake comes not from individuals adding salt from a salt shaker but from salt already added to processed foods and restaurant food. It is estimated that fewer than 1% of Americans are currently in compliance with current American Heart Association sodium intake recommendations. *Source(s): Yahoo Health, New England Journal of Medicine

Money Minute
Trivia Question

What organization has recently become the target of U.S. military air strikes after it beheaded westerners and broadcast its exploits on the internet?

A) al Quaida *B) ISIS* *C) SMC* *D) Free Syrian Army*

Last Month's Question – A police shooting of an unarmed 18-year old man has sparked protests and social unrest in the city of Ferguson. Ferguson is located in what U.S. state? A) Kansas ***B) Missouri** C) Nebraska D) Oklahoma

High-Yield Bonds Offer Income for Risk-Tolerant Investors

(Continued from page 1)

where he could name a beneficiary to receive payments should he die before that 10- or 20-year payout period ends.

-Another option is for the man to elect to receive payments for life and receive a lump-sum refund payment should he not receive at least $100,000 in monthly payments before dying. For example, if the man dies after three years and receives only $20,196 in cumulative payments during his lifetime, his beneficiary(ies) would receive a lump sum of $79,804.

Both of these options add a level of guarantee for the recipient of the annuity payments and will alter the monthly payout from the insurance company accordingly. Here is a sample payout grid for these options from www.ImmediateAnnuities.com:

Male, 65 years old, $100,000 premium payment

Annuity Payment Option	Monthly Payment
Single Life Only	**$561**
Single Life with 10 Years Guarantee	**$553**
Single Life with 20 Years Guarantee	**$506**
Single Life with Premium Refund	**$524**

As you might expect, the single life only option, though risky for the purchaser, pays significantly more than the life with 20-year certain option. There is a $55 per month difference between the two payout amounts, which may not sound like much but adds up to $13,200 over 20 years.

You may be wondering if there is any difference in payout rates for women. The answer is yes. Women have longer life expectancies, hence the payouts are slightly lower. For a 65-year old female, here are the numbers from www.ImmediateAnnuities.com:

Female, 65 years old, $100,000 premium payment

Annuity Payment Option	Monthly Payment
Single Life Only	**$526**
Single Life with 10 Years Guarantee	**$514**
Single Life with 20 Years Guarantee	**$482**
Single Life with Premium Refund	**$493**

For couples who want to create an income stream for the duration of both of their lives, a joint life immediate annuity can be purchased. Since it provides a payout until both spouses are deceased and covers two lives, payout rates are lower than for immediate annuities that cover only one life. Here is a sample payout grid for the various payout options:

Male and Female, both 65 years old, $100,000 premium payment, joint life annuity

Annuity Payment Option	Monthly Payment
Joint Life Only	**$464**
Joint Life with 10 Years Guarantee	**$462**
Joint Life with 20 Years Guarantee	**$454**
Joint Life with Premium Refund	**$457**

In all cases, payout amounts will be higher if the annuitant(s) is (are) older than 65 and less if the annuitant(s) is (are) younger than 65. Also - keep in mind that these are sample payout rates from one carrier. Payout rates can vary greatly from one company to another. These numbers should only be used as a guide to illustrate concepts.

Benefits vs. Drawbacks

On the plus side, the safety, predictability and security of these products is extremely high. The products are fixed in nature and immune to interest rate fluctuations. They are issued by life insurance companies, a very tightly-regulated industry, and the income stream is guaranteed by the claims-paying ability of the company. They require no thought or management after purchase, and if a person is healthy and lives longer than expected, he or she will continue to enjoy payments for life and increase the return on investment.

The drawbacks of immediate annuities are fairly obvious. First and foremost, the loss of access to ones principal is certainly not desirable. The other major drawback is that the rates of return associated with these products are generally very modest. Similar rates of return are available in other fixed income investments without the drawback of the loss of access to ones principal, though none of these alternatives carry any sort of guarantee.

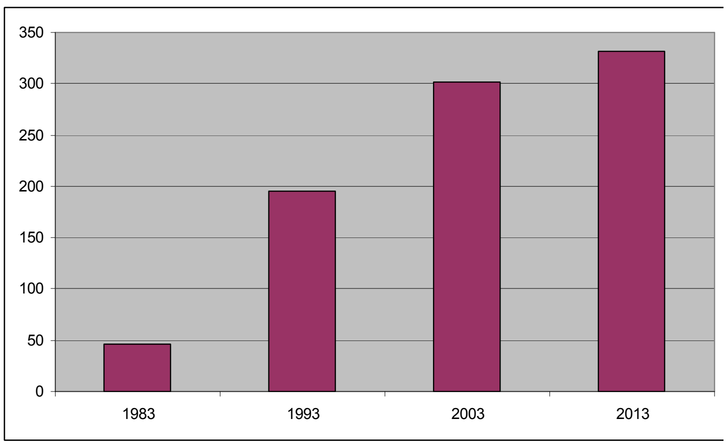
Overall, I believe that immediate annuities are a valid option for creating retirement income for more risk-averse individuals who value the guarantees associated with these products. More risk-tolerant individuals who are comfortable with some fluctuation in monthly income will likely not be interested. Of course, the choice does not have to be an "all-or-nothing" proposition, but those who do choose to use immediate annuities must be sure to maintain ample liquid assets aside from what they invest.

As always, consult your financial and tax advisors before making any investment decisions.

CEO Pay Relative to Average Worker Pay Continues to Climb

The Occupy Wall Street movement, legislation proposing a raise in the federal minimum wage to $10.10, stagnant wage growth and media coverage of growing income inequality statistics all reflect the unbalanced nature of this economic recovery. Justified or not, you can be sure that these topics will be mentioned frequently during this election season, particularly by Democratic candidates. One related issue that has drawn ire from the left is that of executive compensation relative to the wages of average workers. The median compensation for a CEO of a Fortune 500 company in 2013 was $11.7 million. This sum represents 331 times as much as the average worker in these companies made in 2013. The charts below show the trend of rising CEO pay relative to workers, along with the selected pay of CEOs at 10 well-known companies compared to the average worker's hourly wage.

Ratio of CEO-to-Worker Pay
(1983 - 2013)



Source(s): AFLCIO.com, Nerd Wallet

Selected CEO to Average Worker Earnings Comparison (2012)

		CEO Hourly Compensation[1]	Average Worker Hourly Wage[2]	CEO Pay Multiple
1	McDonald's	$9,247 [4]	$7.73	1,196
2	Starbucks	$9,637	$8.79	1,096
3	Dollar General	$7,720	$7.67	1,007
4	Gap	$8,209	$8.67	947
5	TJ Maxx	$7,256	$7.85	924
6	Target	$6,882	$8.35	824
7	Walmart	$6,898	$8.86	779
8	CVS Caremark	$6,777	$8.81	769
9	Best Buy	$6,517	$9.78	666
10	AT&T Wireless	$7,412	$13.28 [5]	558
	Median	$7,334	$8.73	874

[1] Calculated by dividing CEO's total compensation from the company's annual proxy statement by 60 hours a week times 50 weeks per year.
[2] Equals the average non-executive employee wage as obtained from www.glassdoor.com.
[3] Calculated based on hourly overtime rate equal to 1.5 times the average hourly wage, an eight-hour workday and 22 working days per month.
[4] Compensation is for the former CEO who retired June 30, 2012 as detailed in most recent proxy.
[5] Hourly wage is for the retail sales consultant position.

Dating back even farther, chief executives earned just 20 times as much as their average employee back in 1965. Furthermore, the average compensation for the top 200 earning CEOs of public companies in 2013 was $20.7 million, which represented 270 times their average employee. Despite increased transparency and tracking, pay packages have shown little in the way of leveling off in recent years.

It would be easy to conclude that CEOs are grossly overpaid and that the CEO-to-worker pay ratio clearly exemplifies income inequality in America. Alternatively, one could simply conclude that the forces of the free market have led CEO pay to its current state, and, as such, high CEO pay is justified. Before making any conclusion, there are a few different issues to consider here: why is CEO compensation so high, why has it risen so rapidly relative to average workers' pay and how is this high compensation justified? Also, what forces have caused overall wage growth to stagnate over the past 20+ years? I will begin to examine these questions in this month's Editorial (see below).

Editorial: *Is Anger Toward CEO Pay Justified?*

If you have not already read this month's "Up Close" article (above), I recommend you do so before you proceed. Doing so will give you some relevant background information about current CEO pay. That being said, let's get down to business. First, to those who make the argument that no one needs that much money, that it is morally wrong for anyone to earn such large sums of money (especially while there are those who earn relatively little), that those who do should endure the public's anger...I will not attempt to disabuse you of that notion. For those who can, at a minimum, tolerate the free market and believe that individuals should be free to earn as much as they can (legally), the question of whether CEOs specifically deserve the public's ire is a legitimate

Editorial: *Is Anger Toward CEO Pay Justified?*

topic for debate.

First - consider CEOs who have provided vision, leadership, strategy, guidance and/or creativity to start a company, grow sales at an existing company, or turn around a struggling company. It would be hard to say that CEOs instrumental in doing such things are not deserving of such compensation. Some examples:

-Alan Mullaly - former CEO of Ford Motor Co., steered the company through the recession without filing for bankruptcy, brought the company back to record profitability

-Steve Jobs - founder / former CEO of Apple. Company is expected to generate roughly $39 billion in sales during its next quarter. Not much more to say here.

-Jeff Bezos - founder of Amazon.com. Enough said.

-Jeff Boyd - former CEO of Priceline.com - sales at the company increased six-fold during the last six years of his tenure as CEO. Share price up 51% per year annualized during his 11-year tenure.

These CEOs were/are paid handsomely, but they have played a crucial role in their company's success and the creation of wealth for their company's shareholders. On the opposite end of the spectrum, there are those CEOs whose leadership steered companies in the wrong direction:

-Ron Johnson - former CEO of J.C. Penney for just 17 months and was paid $52 million (mostly in stock options) to join the company. His failed turnaround strategy decreased sales by 35%+ and sent the stock price lower by 2/3rds.

-Steve Ballmer - former CEO of Microsoft, failed to capitalize on the shift to mobile technology from personal computers, stock price fell 40%+ over 11 years during his tenure.

These men clearly hurt shareholder value for their respective companies, and some anger for these failures is certainly justified. These examples represent some of the very best and very worst, and overall, CEOs probably get too much of the credit for when things go right and take too much of the blame when things go wrong. This may be an extension of the so-called "Great Man Theory," which contends that history can be explained by the impact of great individuals. Top athletes, sports coaches, actors, directors, musicians, etc. who are viewed as being great command similarly high compensation in their respective fields. For example, in professional basketball Lebron James will earn $20.6 million next season and is worth every penny. With no salary cap in place, I believe James could easily attract a salary of $40-50 million per year. Alternatively, Amar'e Stoudemire, who plays for the NY Knicks, will earn $23.4 million and is widely considered a "bust" for not living up to his huge contract over the past few seasons. For whatever reason, we don't find individuals publicly protesting how overpaid athletes, actors or other highly-paid individuals – whether they are ultimately unsuccessful or not.

Similar examples exist in all of the aforementioned fields and others, and the belief that a "superstar" can bring a team a championship, make a movie into a box office success, or turn a business into a winner is all part of the same phenomenon. With the huge sums of money at stake in global business, the huge compensation associated with these jobs is not hard to understand. Sometimes paying a premium for a "superstar" works out for the team / movie studio / business / etc., and sometimes it doesn't. The common thread, however, is that entities in high-stakes fields are compelled to "pay up" to attract talent if they want a chance at success.

Clearly, CEOs who do a poor job of running their business deserve scorn, criticism and disapproval from shareholders and employees. In fact, any time anyone is paid any job but ultimately fails in some way or does a poor job, some level of anger or disappointment is justified. However, blanket anger specifically directed towards all CEO pay does not strike me as being justified. Disproportionately high pay for "superstars" in any field - whether they eventually "earn" their pay or not – is simply a feature of a competitive free-market economy. A more consistent response would be to extend ones anger to all highly-paid individuals…though this is also not something I agree with either.

Please send comments via e-mail to: Brad@R1FinancialGroup.com

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