WEALTH
Advisor

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A GRIM OR GOLDEN OLD AGE

Planning makes the difference

One uncertainty strikes fear into the hearts of many Canadians thinking about their retirement savings – no matter what their income or asset level.

How much is enough?

The anxiety intensifies as retirement approaches and after significant equity market volatility.

Defined benefit pensions, where employers pay their retired employees a specific benefit for life, are no longer the norm for private sector employees. Affluent Canadians in particular now look to their own investments as the main source of their future income.

Three threats to your peace of mind

Moshe Milevsky, York University professor, Executive Director of The Individual Finance and Insurance Decisions Centre, and a member of the BMO Advisory Council on Retirement, has identified three significant risks to a prosperous retirement.

Living much longer than anticipated: if you're a 65-year-old couple today, there's a 75-per-cent chance at least one of you will survive for another 20 years, and a 50-per-cent chance one of you will be around to blow out 90 birthday candles.

Unexpected inflation: $1000 shrivels to $610 of purchasing power after 25 years of inflation at a modest two-per-cent per annum. Your own personal inflation rate will likely be higher and is more relevant. It reflects the cost escalation in the pricey goods and services you'll actually consume as you age, including health care. For example, long-term assisted living can total as much as $100,000 annually per person.

Poor portfolio performance in the first few years of retirement: the strategy for preserving and growing your nest egg is as important as its dollar value. You need the right mix of components in your retirement portfolio, which may include traditional investments (stocks and bonds), as well as pension-like products with features that may include downside-protection and/or guaranteed income. The inherent risk, or volatility, of your investment portfolio also plays a vital role. Withdrawing income from a portfolio in a bear market can prematurely exhaust your capital because of the sequence-of-returns effect (see chart on next page).

Retirement Tips
- Moshe Milevsky

- By all means enjoy your retirement; however, try to pace the big-ticket purchases on your bucket list. Spend smoothly over time.
- Before you stop working, pay off high-interest consumer or mortgage debt.
- Set aside an untouchable rainy-day account for extremely unlikely but extremely costly events instead of insuring every small risk in your life.

Prof. Milevsky, a widely recognized, award-winning researcher and innovator in the field of retirement-income planning, insurance and pensions, urges people to take action to reduce their vulnerability to each of these risks. *(continued on next page)*

THIS Issue

Planning to the rescue

Planning for your retirement involves taking a conventional financial plan and immunizing it as far as possible against these risks, says Richard Mason, the head of Investment Management and senior vice president at BMO Harris Private Banking.

Sounds like something everyone would want to do; yet many people fail to do it because they are unaware these risks pose a threat.

"The challenge for most people is they don't know what their income needs will be in retirement, and they don't know how to generate sufficient assets to provide that income," Richard says.

"As advisors, we really have to step up. As Moshe points out, advisors are risk managers. They have to help clients diversify their risk factors based on each client's individual balance sheet, and understand what each client needs to meet his or her retirement objectives. Then an advisor must assist each client in achieving those objectives."

A good retirement plan replicates the structure of a pension plan (aligning assets with future liabilities – i.e. expected spending needs in retirement) that would generate ample income to live comfortably.

If you have enough wealth to ensure a comfortable retirement, the goal becomes protecting wealth for the next generation, supporting a charitable cause, or leaving a legacy that makes you proud.

"Making ends meet in retirement is a universal concern. As income and wealth levels rise, the definition changes. Retirement income security means different things to different people."

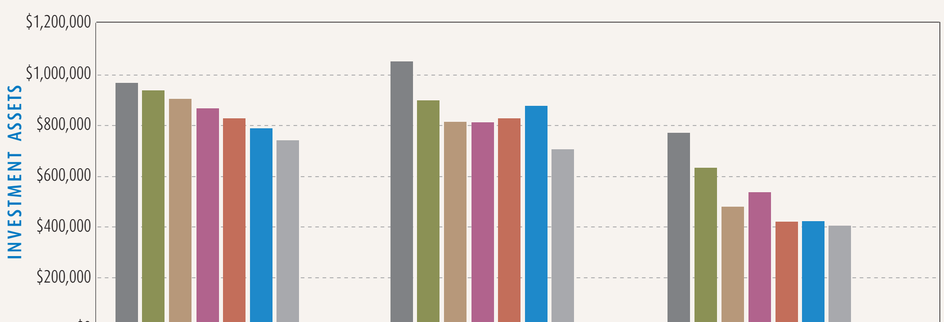
Where did you get on the retirement investment portfolio merry-go-round?

Volatile returns are hazardous to the timing of your retirement.

Sequence of returns is the order and type of returns (positive or negative) earned over a period of time. In the three scenarios illustrated below, the average annual return rate in each case is 7% over a seven-year period.

Capital Accumulation and Depletion over a 7-year period

Each scenario has an average annual 7% per year return and assumes a $100,000 withdrawal per year from an initial capital investment of $1 million.



	Retirement Capital-Constant Return	Constant Return Rate	Retirement Capital-Var. Rtn-High start	Variable Return Rate (High start)	Retirement Capital-Var. Rtn-Low start	Variable Return Rate (Low start)
yr 1	$970,000	7%	$1,050,000	15%	$770,000	-13%
yr 2	$937,900	7%	$897,500	-5%	$631,500	-5%
yr 3	$903,553	7%	$815,450	2%	$480,980	-8%
yr 4	$866,802	7%	$813,304	12%	$534,894	32%
yr 5	$827,478	7%	$827,167	14%	$418,847	-3%
yr 6	$785,401	7%	$876,057	18%	$419,370	24%
yr 7	$740,379	7%	$705,972	-8%	$403,244	20%

Notice how the difference in the sequence of returns impacts your total retirement capital when the portfolio experiences negative returns as capital begins to be withdrawn.

Prosperity in peril

Further confusing the picture are the vague guidelines, myths and generalizations about retirement finances. They can lead people to false conclusions about their own situation – or deter them from thinking about it at all.

Affluence does not necessarily provide immunity against the above-mentioned threats, Richard notes. Some high-net-worth individuals don't see the value of planning their spending. They may be less likely to budget. They may not take the time to calculate the tab for a golden old age because they believe they'll have enough, or that their current high income will somehow translate into a comfortable retirement.

Another pitfall: the newly retired tend to splurge in the first two years.

"Fledgling retirees naturally want to travel, treat themselves to expensive hobbies, and do all the things they put off in favour of their careers."

Without proper planning, sizeable withdrawals in the early stages of retirement can compromise your nest egg's sustainability.

Start with a needs analysis

A good planning conversation should answer two basic questions.

First, the advisor asks how much the client thinks he or she will need. Most clients wouldn't be able to answer without some serious thought, calculations and input from a planner, Richard says.

The client asks the advisor the second question: How much can I make?

Where the advisor adds value is identifying the factors that will add risk to a plan and, more importantly, the factors that can ensure success in a plan.

"It's never too late, and you're never too old, to have a conversation so your advisor truly understands your situation. Of course, the earlier you start, the better the outcome will be. The process of profiling must be ongoing. This is a living exercise. It doesn't stop at retirement."

If you've been putting off planning, or haven't looked at your plan lately, please contact your client advisor.

The first 50 clients who contact Bernice.lau@bmo.com will receive a complimentary copy of Moshe Milevsky's new book, Your Money Milestones: A Guide to Making the 9 Most Important Financial Decisions of Your Life.

New travel rewards BMO World Elite MasterCard

You asked for this card; now it's here.

Collect one BMO ELITE™ Rewards point for every dollar in purchases, then redeem your points for a variety of rewards, including unrestricted travel, upscale retail merchandise, luxury experiences – even RESP and RRSP contributions. With this card, you also receive 21-day out-of-country medical insurance, and trip cancellation and interruption coverage.

The BMO Harris Private Banking World Elite MasterCard is the first World Elite MasterCard to launch in Canada.

"Our clients have been telling us they would like a premium travel card with features and rewards that would be attractive based on how they spend," says Peter Tracz, the national director of Platinum Banking at BMO Harris Private Banking. "We designed this card in response."

You can redeem your points, which never expire, for travel on any airline, any seat, any flight, including all fees and taxes. Cruises, hotels, vacation packages and one-of-a-kind travel experiences are also part of the rewards program.

For BMO Harris Private Banking World Elite MasterCard cardholders who spend $50,000 or more in a year using the card, the annual $150 fee is waived in the subsequent year.

"There are many expenditures you're going to make anyway; with this card, you're getting something in return," Peter says. "It makes complete sense to take advantage. Our clients are very sophisticated when it comes to card use. They understand the practical value of a rewards card. This one has a wide array of flexible options, plus extras that aren't available anywhere else in the marketplace."

A catalogue of high-end merchandise like flat-screen TVs, espresso makers and designer watches gives you extra choices for trading in your points.

The BMO Harris Private Banking World Elite MasterCard is the first World Elite MasterCard to launch in Canada. Our own proprietary rewards program expands the flexibility and range of the way you can redeem your points.

It allows you the option of converting your points into BMO financial investment choices, including Registered Retirement Savings Plans (RRSPs), Registered Education Savings Plans (RESPs), and non-registered accounts. If you prefer, you can use your points to help someone in need by making a charitable donation to the Canadian Cancer Society, Canadian Red Cross, Make-A-Wish Foundation of Canada or United Way of Canada.

At bmoelite.com you'll find a complete list of all the benefits, rewards and services. For more information or to apply, just ask your client advisor, visit bmo.com/bmoharriswe or call 1-866-991-4769 and ask for a BMO Harris Private Banking World Elite MasterCard.

As a welcome bonus, new cardholders receive 15,000 points. Short-haul flights start at just 13,000 points.

"The flight's on us," Peter says. "Why not reward yourself?"

Travel rewards and more

- 21-day out-of-county travel medical insurance
- trip cancellation/delay insurance
- collision or loss damage insurance
- Priority Pass access to more than 600 VIP airport lounges world-wide
- 24/7 international concierge service that can assist with travel, dining, golf, leisure and entertainment recommendations and reservations
- exclusive access to tickets for popular concerts, theatre, international cultural events and live performances
- dedicated customer service and access to MasterCard World Elite travel discounts, exclusive events and luxury travel experiences – like wine tours, rainforest escapes, luxury spa visits or extreme adventures

Market Outlook

Rising interest rates and the threat to bond returns

by Paul Taylor, Chief Investment Officer

Lately people have been asking me what the outlook is for the bond market.

It's a good question.

First, let's acknowledge that fixed-income investments always play an important role in a portfolio: they provide diversification and act as a buffer to the volatility of the stock market. Yet, returns on bonds are expected to underperform last year's fixed-income returns, not to mention equity market returns over the next while.

When interest rates go up, bond prices move lower

That expectation for underperformance is directly related to the probability that benchmark interest rates will rise over the next 12 months. When interest rates go up, bond prices move lower; the longer the bond's term to maturity, the greater its price sensitivity to rate changes. The figures in the chart are the total returns for bonds of varying maturities, given various increases in interest rates. The analysis assumes a one-year time horizon and shows how interest rate increases can lead to more significant negative total returns the longer a bond's maturity (see chart).

The Bank of Canada has said it won't raise rates until the end of June unless inflation jumps significantly. The U.S. Federal Reserve recently stated that low interest rates are warranted for "an extended period."

	Bond Maturity		
Interest Rate move	5 years	10 years	30 years
+50 basis points	0.41	-0.36	-3.73
+100 basis points	-1.99	-4.19	-11.48
+200 points	-6.78	-11.85	-26.99

The trigger for raising interest rates will be evidence that the economic recovery is sustainable.

North American economies are showing signs of continuing recovery; however, in our view, employment is the key to a sustainable recovery. Andrew Osterback, Portfolio Manager for our Fixed Income strategies, offers some insight.

"In 2008, the Fed stepped in and rescued the system with stimulus spending. Until the U.S. economy itself consistently creates jobs, central banks won't raise rates. Overall, none of the three supporting factors we see as having significant impact on inflation (capacity levels in factories and businesses, wage growth and growth of the money supply from credit expansion) is at a point where it would push inflation up. So there's not a lot of pressure on interest rates. If we see a change, we would shorten the duration (that is, decrease the sensitivity of bond prices to changes in yield) to below that of the benchmark."

Right now, the economy is nowhere close to overheating. Rates will have to go up eventually, likely later in 2010 or in early 2011. We think this return to a more normal rate environment will happen without a large inflation increase.

Until the U.S. economy itself consistently creates jobs, central banks won't raise rates.

Although rising interest rates could be bad news for bond returns, we're managing the exposure to interest rates in bond portfolios in a few ways: investing a larger weight in shorter-term bonds versus the benchmark; using preferred equities selectively; and, from an asset-mix standpoint, we've been allocating a higher proportion to equities within the ranges appropriate for our clients' different circumstances.

We balance our clients' portfolio holdings based on each client's personal risk tolerance and investment objectives. To learn more about the role that bonds play in your financial strategy, contact your BMO Harris Private Banking investment counsellor.

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