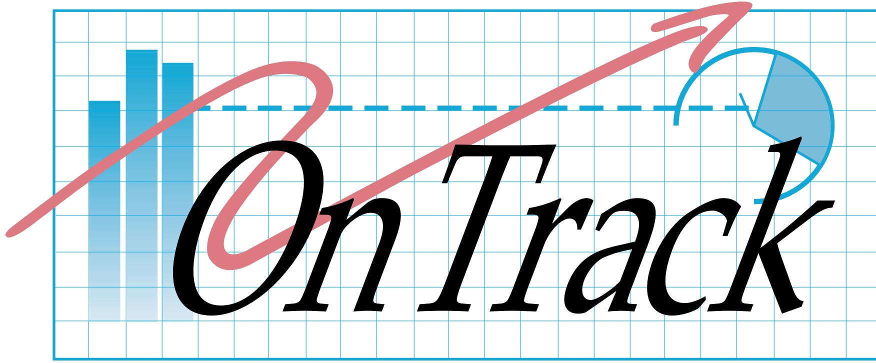
Summer 2002



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INVESTMENT REPORT FOR PLAN PARTICIPANTS

America's Shrinking Retirement Age

How old are most Americans when they retire? You may think the answer is 65 because that's the age at which retirees currently are eligible to receive "full" Social Security benefits.* But, according to a recent AARP report, about 60% of America's workers start taking their Social Security benefits at age 62. Back in 1980, the percentage of early retirees was 40%, and, in 1970, it was just 28%.

Will You Be Able To Afford a Comfortable Retirement?

	Percentage of Workers Surveyed
Yes, Very Confident	22%
Yes, Somewhat Confident	41%
No, Not Too Confident	18%
No, Not at All Confident	17%

**Source: 2001 Retirement Confidence Survey, Employee Benefit Research Institute, American Savings Education Council, and Mathew Greenwald & Associates, Inc.

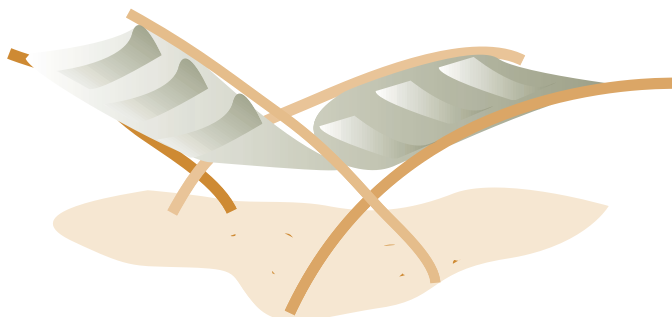
Continuing To Work

Despite the strong trend toward early retirement, many of today's workers expect to hold jobs *after* they "retire." Why? Some retirees just enjoy keeping active. But the chart points to another possible reason. Recent research** found that only 63% of today's workers believe they'll have enough income for a comfortable retirement. The same research also found that two thirds of those surveyed expect to work either full- or part-time to supply a portion of their retirement income. Sixteen percent anticipate that employment will be a major source of income, while 52% expect it to be a minor source.

Your Own Expectations

Looking ahead at your own future, you also may foresee a gap between your retirement income and your projected cost of living. Fortunately, you're in a good position to help yourself *before* you retire. Your tax-deferred retirement savings plan provides an opportunity for you to build up a significant source of future income. The more you contribute to your plan and the better your investments perform while you are still working, the less need you may have to keep working past retirement — *whenever* you decide that will be.

*The age to receive full Social Security benefits is scheduled to gradually increase from 65 to 67. The first increase will affect workers born in 1938, who can retire with full benefits at age 65 and two months.



Think 70-20-10 To Make Saving Easier

Aiming for more financial freedom in your life doesn't have to involve complicated budgeting. But you probably should have some sort of spending plan.

You could just split your income into two parts each payday — an amount that you use for your day-to-day living expenses, and a smaller part that you put into some form of savings for your long-term future, like your retirement savings plan. What this strategy leaves out, though, is a way to handle the inevitable times when you'll need — or want — to spend more than you can afford to pay out of one or two paychecks.

The Three-part Plan

Handling large purchases may be much easier if you decide to use a 70-20-10 savings plan — or some variation of it. This strategy can help you avoid the common problem of not having money on hand to pay for emergency car repairs, vacations, appliances, and other big-ticket items.

The 70-20-10 plan is a simple way to take care of your day-to-day living costs, pay for special items, *and* work toward your long-term goals. Each payday, simply divide your pay into *three* parts:

- 70% that you use for all your regular expenses,
- 20% that you set aside as a reserve for large future purchases or other major expenses, and
- 10% that you don't touch because it's invested for your long-term goals.

Although 70-20-10 is a good place to start, you don't have to stick to these exact percentages. The idea is to plan for your short-, medium-, and long-term needs using whatever amounts you decide work best for you.

Tax Savings

Remember, you don't pay federal income taxes on the contributions you make to your retirement savings plan or on any investment returns those contributions earn for as long as the money remains in your plan. That makes your contributions more affordable and lets your retirement money compound faster than it would if you put it into ordinary taxable savings or investments. So, it's smart to put most or all of your long-term savings into your tax-deferred retirement savings plan. And putting money away where it won't be touched will be easier when you also have a reserve for those major purchases.

Moving ahead on the Inflation Treadmill

Treadmills are very popular with the exercise crowd these days. They're easy to use. But to avoid stumbling, you have to make sure you keep moving. You need to do the same thing as you save for your retirement — because of inflation.

Erosion of Buying Power

When the same loaf of bread and gallon of gas cost you more today than you paid last week, that's inflation. In small doses, inflation isn't a big problem. But if inflation continues for many years, even at a low rate, its effect on the buying power of income or savings may be very strong. For example, 20 years from now, you will need $1,806 to buy something that costs $1,000 today — if the annual rate of inflation averages 3% during that period.

No one knows how much future inflation will actually occur. But any amount of inflation is a danger both before and after you retire. While you are still working, inflation may slow the *real* growth of your retirement plan account. After you retire, inflation may gradually cut the purchasing power of any fixed income you may receive, such as a pension or annuity. As a result, you may have to draw an increasing amount of income from your savings in order to maintain your buying power.

Defensive Strategy

How can you keep the value of your retirement savings balance ahead of inflation? There's only one way: *Earn investment returns that are higher than the rate of inflation.* Remember, you're not likely to beat inflation if you keep a large portion of your retirement money in low-risk cash equivalent investment portfolios whose historical returns have been close to the rate of inflation.

Finding Extra Money for Savings

Are you maxed out on your living expenses? Are you having trouble putting money away for your future? Changing your spending habits may make a big difference.

Keep a Record

Knowing where and when you spend your income is the key to finding extra money for savings. Start tracking your cash flow in detail. By carefully recording all of your expenses for a month or two, you may discover that you're actually using a "cookie jar" spending plan.

Lots of people do the same thing. They put their net pay into a checking account. Then they take care of the rent or mortgage and utility bills and make minimum payments on everything else. Whatever is left over goes into the cash "cookie jar" and is spent freely until it's all gone — just before the next payday.

Pay Yourself First

If you find yourself doing this, you need some better priorities for spending your income. One strategy that works well is simply to pay yourself *first*. Take a percentage of your pay and put it into savings each payday *before you pay anything else*. You'll still owe the same regular bills. But with less money available for other spending, you'll have to force yourself to trim your everyday expenses. For example, just taking a little time for a meal at home instead of stopping for take-out on your way to work may easily cut $15 or more from your weekly spending.

Saving more of your pay is all about watching how you spend your money. So, before you buy anything, stop and ask yourself: *Do I really need this? Where does it fit into my spending plan?*

Don't "Set and Forget" Your Investments

When summer gets going, it's easy to just set your air conditioner at a comfortable level and leave it there until cooler weather returns. That's not a bad idea at home — but you don't want to do the same thing with your retirement plan investments. Giving your account careful, periodic checkups is essential.

Recent research has shown that many participants in the large retirement plans surveyed simply let their contributions be invested in their plan's default options, the investments automatically selected if a participant does not make specific choices. But retirement plan participants should avoid being couch potato investors — because their investment values aren't sitting still.

Tracking Results

Over time, some plan funds or portfolios may have outstanding results, and others may be disappointing. You won't know the difference unless you track your returns by examining the plan statements you receive or by using another available source of plan investment results. Tracking your returns will help you decide whether your investment mix is right for your goals.

Comparing Performance

How can you tell if a specific portfolio is performing well? Rather than just examining a portfolio's return in isolation, it's a good idea to compare the return to the results of similar investments. Just check the return of a market index of *comparable* securities against your portfolio's return *over the same time period*. Be sure to look at the performance of both over one-year and longer time periods, not just over a few recent months.

Don't expect an exact match when you compare a portfolio's results with an index. The securities in an actively managed portfolio won't be exactly the same as those in a benchmark index. Plus, an investment portfolio has management and transaction expenses that an index doesn't have.

Staying on Plan

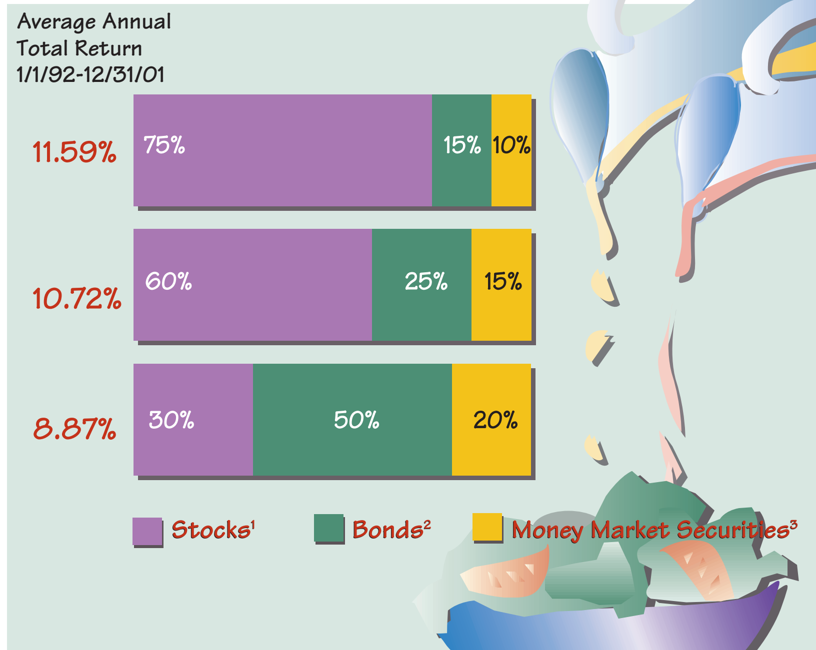
As the values of your portfolios increase or decrease, your investment mix may drift away from your original plan. For example, if large company stocks perform poorly, the percentage of your account invested in these stocks might drop considerably. Or, if stock prices rise, your stock holdings might make up a much larger part of your account than you originally planned. This may expose your account to less — or more — risk overall.

So, recheck your mix of investments once a year to see if your account has drifted. Then decide if you want to restore your original proportions.

The Right Mix of Risk and Reward

Use too much oil or vinegar and your salad dressing won't be a taste sensation — the right balance of ingredients is important. Striking a balance is something you do everyday, in many ways. Balance is also a key factor when you make decisions about investing your tax-deferred retirement savings.

Some people are comfortable putting all their money into funds or portfolios with low risk and low potential returns. Others invest all their money in high-risk funds or portfolios with high potential returns. Striking a balance between these two strategies may result in the right mix of risk and rewards *for you*. But how do you choose that mix? Here are some guidelines that may help.



Context Counts

Each of your investment options has a certain level of risk and potential return. Those factors are important — but don't stop there. Context counts when you invest your retirement account. An investment that by itself may be too risky or offer too low a potential return may be just right within a mix of different investment types. Including higher-risk investments increases your *potential* overall return, while adding low-risk investments reduces the chance of overall loss when higher-risk investments perform poorly.

Think Long Term

Short-term price volatility is a normal part of investing. You can expect the values of your stock and bond portfolios to move upward at times — and downward at times. When you track your returns, keep in mind that both stocks and bonds have a history of growth over long time periods. That history, of course, is no guarantee of future returns. Whenever you sell an investment, its value may be lower than the amount you invested. Still, time is on your side if you choose a well-balanced investment mix with the potential for long-term growth and *stick with it*.

Don't Ignore Inflation

Low-risk investments reduce your account's volatility. But investments with low risk usually also have low returns that may not beat inflation over the long term. Inflation plus low growth is a recipe for a plan account balance at retirement that may not be large enough to meet your needs. To counter this real risk, you need to choose a *combination* of portfolios that has a level of overall risk you can live with while offering the potential for rewards that exceed the rate of inflation.

Investments measured by: [1]S&P 500 Index, an unmanaged index of the stocks of 500 major corporations; [2]Lehman Brothers Government/Credit Bond Index, an unmanaged index of investment grade corporate and government bonds with maturities of one year or more; [3]Merrill Lynch 3-Month T-Bill Index, an unmanaged index that measures returns of three-month Treasury Bills; [4]MSCI EAFE (Morgan Stanley Capital International Europe, Australasia, Far East) Index, a market value-weighted average of selected securities in 21 countries.

Past performance does not guarantee future results. Your investment returns will be different. Investment cannot be made in an index.

Sources: Russell Data Services and NPI

This newsletter is designed to provide useful information about retirement plans and investing your plan account savings. While the investment performance information contained herein was obtained from reliable sources, it cannot be guaranteed as to completeness or accuracy. Before acting on any of the information provided, consult your professional advisor.

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