

Chiropractic ECONOMICS

THE MAGAZINE DEDICATED TO PRACTICE GROWTH AND PROSPERITY SINCE 1954

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Financial Planning

Preparing for a golden future

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If you are like many of the healthcare professionals I have talked with, you may be in for a rude awakening in your financial future: Comfortable retirement is going to require a good deal more money than you imagine.

How much? At an after-tax annual return of 3 percent to 5 percent, it may take from \$5 million to \$6 million in investable liquid assets for most doctors to retire comfortably. This amount excludes residences and other non-liquid assets that tend to be included when calculating "total net worth."

Why will you need so much in liquid assets? Here are some reasons:

- **Portfolio performance.** Most people tend to overestimate what they will earn in the markets. Over the past century, bonds have returned from 5 percent to 6 percent annually before taxes, and stocks about 9 percent annually before taxes, depending on the years considered.

Although investors have seen high returns for short periods of times, they have also seen low returns for long periods of time. We have no reason to expect these averages will change. Despite this, investors commonly plan on after-tax annual investment returns of at least 15 percent!

The historic reality of about 6 percent changes the equation considerably.

For example: A hypothetical \$1 million portfolio generating a robust 17 percent annualized after-tax

return would grow to \$8 million in 12 years. The same \$1 million portfolio growing at a more probable 6 percent would become \$2 million in 12 years. And few portfolios avoid occasional losing years. The time required to make up for a losing year is far longer than most investors realize.

- **Inflation.** Inflation enters the picture as well. Even at a modest 3 percent annual inflation increase, a chiropractor who currently requires \$10,000 monthly income will need \$16,000 per month in just 12 years.

It would take at least \$4 million in invested funds at 4 percent annual tax-free return to realize \$16,000 per month, and that amount does not provide for any significant increases in health expenses, which are likely.

WHAT TO DO?

The first thing you need to do is to get a clear assessment of what you need and what might happen to your assets that could affect your needs.

- **Consider several different life-expectancy scenarios.** They should reflect your income needs, based on longevity.

- **Develop three projected investment outcomes.** Base them on different available asset amounts: One outcome would reflect the lowest amount you expect with absolute certainty. The second outcome would be a somewhat less than desired outcome. And the third would be an ideal outcome.

- **Apply different rates of annual return.** These calculations will determine how much you must set aside annually to reach your desired retirement amount. It's wise to anticipate a rate of return that reflects your

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HOW MUCH MONEY WILL YOU NEED?

Plan your retirement realistically

BY STEVEN HOLT ABERNATHY

What a loss can do to your portfolio

Most investors have not considered the impact an occasional annual loss can have on their retirement portfolios. Consider an aggressive investor with a high tolerance for risk.

Occasionally, the risks pay off. In a year when the stock market gains 8 percent, he makes 50 percent and is king of the country club locker room.

The next year, his high-wire act crashes and he loses 50 percent. Tough luck, but he is no worse off than he was at the start of year one, right?

Wrong. Assuming the investor began with a \$100,000 portfolio, he has \$150,000 at the end of year one. But in year two, his 50 percent loss leaves him with just \$75,000 — a 34 percent loss which, he has to make up just to get back to even.

At an annual return rate of 9 percent, getting even would take four years. Overall, he suffers a five-year span with less than net zero performance once inflation is factored in.

That's a big price to pay for a few weeks of bragging rights.

Obviously, this type of inconsistent return profile will cripple any retirement planning effort. By comparison, a risk-averse investor who settles for a steady if unspectacular annual return of 6 percent to 10 percent (let's use 8 percent as a mid-point estimate for the same \$100,000 portfolio) reaches \$116,640 by the end of the second year, and \$150,000 after the same five year-span it took for the "risk-taking" investor to get back to his original \$100,000. ☹

personal investment risk tolerance. Use various rates of inflation to calculate these rates of return.

GETTING HELP

Understanding what Warren Buffet calls your "Circle of Competence" is the key to building a team of competent advisors to help you navigate the years between today and your retirement.

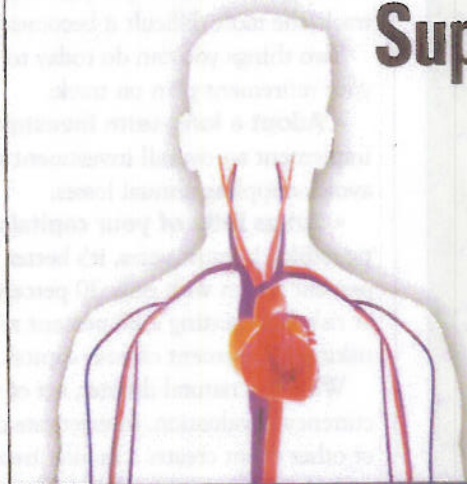
An investment advisor is the key player in your team of advisors. She or he helps you construct various retirement scenarios, determine necessary annual contributions, and manage assets within your personal risk tolerance and investment model preferences.

How do you select the best advisor for you? A key consideration is the advisor's ability to avoid losses.

Although you might think that an advisor who manages large

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YOUR finances

amounts of money may seem like a safe choice, remember that the more money a manager takes in, the harder it is for him or her to deliver performance above broad market returns.

Making money is important, but safeguarding your investable asset base is primary. *You have no opportunity for future returns without investable assets.* Obtaining returns should be the secondary priority. That's why selecting an advisor based on his or her ability to avoid losses is so important.

Working with your advisory team, review your inventory of assets and income. Look for ways to get undervalued assets and additional income into a retirement plan since all gains are tax-deferred.

Some ideas:

- Buy a professional building with a low cost basis, which can be purchased and put into their retirement plan. This strategy shelters the income generated as well as the proceeds if the building is sold.
- Finance debt through a pension plan to generate tax-free interest that is deductible.
- Assemble an inventory of assets to implement many sophisticated, but perfectly legal and beneficial tactics.

The process to determine one's true retirement needs can be daunting. However, the ramifications of not conducting such an assessment can be harsh, and the longer you wait to put your retirement plan on track, the more difficult it becomes to save enough.

Two things you can do today to begin putting your retirement plan on track:

- **Adopt a long-term investment approach.** Implement an overall investment strategy that avoids crippling annual losses;
- **Put as little of your capital at risk as possible.** In most years, it's better to have a 15 percent return with only 30 percent of your capital at risk than getting a 20 percent return while risking 100 percent of your capital.

Why? If a natural disaster, act of terrorism, currency devaluation, interest rate or inflation spike, or other event creates a market tremor, the portfolio with the least capital at risk is best insulated. ☺



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