

## **Double Your Nest Egg**

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KIM NORTON SHOULD have had every reason to feel bullish about her retirement finances. She'd been dutifully contributing to 401(k)-type plans for almost 20 years, routinely hitting the maximum contribution ceiling as she built up a six-figure nest egg. But losing money in the tech bubble rattled her and eventually convinced her she'd need a bigger security blanket. And seeing her mother struggle with and succumb to cancer only confirmed that her instinct was right. "I'd see all these exorbitant medical bills coming in and wonder how regular people manage it," the 41-year-old divorcee says.

So in 2006, Norton decided to tear up the savings playbook. She pursued a rarely used strategy: buying property with her IRA funds and flipping it to earn big returns. Knowing she won't have a gold-plated pension like her mother had in retirement — and that she doesn't want to part with luxuries like weekly spa visits, nights out with friends and vacations in exotic locales like the Maldives — she's now resolved to build her nest egg to \$2.5 million.

You don't have to be a globe-trotter — or conversely, living on ramen noodles — to be legitimately worried about financing retirement. And it's not just because the near bear market has taken a big bite out of many people's portfolios. Most experts say the next wave of retirees will need more money to cover their rocking-chair years than any other generation before them — by some estimates a lot more. Soaring fuel and food prices have reminded everyone how badly inflation can hurt a fixed income. Health care costs, meanwhile, have been outstripping inflation for years, and Fidelity now estimates that a 65-year-old couple who retire in 2008 will need \$225,000 just to cover their out-of-pocket health care costs. (Cash out at 55 and you could need much more.) Companies are also increasingly dropping pensions. And as workers prepare to pay for their own retirements, longer life expectancies add another strain: The average retirement today lasts 20 years, up nearly 50 percent since 1970. All that has bred pessimism among experts like Alicia Munnell, director of the Center for Retirement Research at Boston College, who refers to the era when the baby boomers' parents left work — with pensions — as "the golden age" of retirement. "Some of these boomers," Munnell predicts, "are going to see really tough times."

But even with the economy in the doldrums, many people are finding ways to throw their future a life raft. SmartMoney talked to several retirees and soon-to-be retirees who managed to double their nest eggs within an eight-to-10-year period or are on the path

to doing so. Some of them took traditional routes: The basic law of compounding, after all, means any investor who earns a very attainable 7.5 percent annually will double their portfolio in a decade. Others are venturing into lesser-known territory, creating their own small-business pension plans or using their IRAs to invest in riskier assets. In the fight to supercharge your savings, says Scott Kane, a founder of the networking and job placement firm Gray Hair Management, "sometimes you just have to get pretty creative." Whether you think you're on track to fund a mega-expensive retirement or you're looking for inspiration, you'll find some useful ideas below.

### Beat the Market

SallyAnn and Michael Gowan, a couple in rural Staunton, Va., have seen their share of financial ups and downs. Six years ago they dipped into their savings so Michael, an optometrist, could buy his own practice. Months later they lost most of what was left when MCI's stock crashed; soon they were tapping their retirement accounts just to pay staff salaries. "I had friends that looked at what we were going through and said, 'My God, I'd shoot myself,'" Michael, 48, recalls. But thanks to some hard work and creative staffing — SallyAnn does the books, the kids sweep the floors — the practice has taken off. Still, the Gowans have also dreamed of cashing out in their mid-50s, and with two kids to put through college, their savings are far from ready for such a move.

They're tackling the problem with the kind of aggressive investing strategy that most people associate with 30-year-olds. While most people tend to make their portfolios more conservative as they draw closer to retirement age, historical returns suggest that those who want double-your-money growth from traditional investment vehicles will need to keep more of their assets in the stock market. Right now the Gowans' portfolio is 75 percent in stocks, with about half that in international markets. It's a mix that would've returned a galloping 9 percent annual return over the past 10 years; they're hoping it can do the same once the current market choppiness is over. Every time the Gowans get dividend income, it's immediately reinvested, and they max out their IRA contributions at the start of each tax year so their money has more time to compound. With a portfolio like this, market volatility is the big danger: If the markets sink just as the investor hopes to retire, the nest egg can suddenly seem very skimpy. The Gowans at least have a safety net; they own some local commercial property that can support them if their portfolio turns sour.

For those without quite as high a tolerance for risk, most advisers say greater diversification is still the magic that'll double a nest egg, as long as you have the patience for a time frame of 10 years or longer. The meaning of diversification has changed in recent years, however, adding a degree of difficulty. A decade ago investors could have felt confident approaching retirement with a mix of large-company foreign and domestic stocks, as well as corporate and government bonds. Today, advisers say, investors have to go farther afield to insulate themselves from turbulence in the U.S. economy and what many think will be low returns from American stocks in the near term. "With globalization, it doesn't matter where large companies are based anymore, so you don't get the diversification with them that you used to," explains Paul Baumbach, a financial planner with Mallard Advisors in Newark, Del.

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Baumbach has been moving clients into international small-cap mutual funds as a hedge against trouble in the U.S. markets. Two funds he's watching, Artisan International Small Cap and Hartford International Small Company, had trailing annualized returns of 13 percent and 20 percent, respectively, over the past three years, compared with the broader market's 4.5 percent. Small-cap stocks tend to deliver roller-coaster ups and downs, however; many advisers recommend balancing them with investments that are less volatile. Diane Pearson, an adviser in Pittsburgh, has been recommending international real estate investment trusts and exchange-traded funds that focus on foreign currencies, but her volatility killers of choice are so-called long-short funds, which are designed to avoid big losses in markets like today's. "There are always going to be cyclical bear markets," says Pearson, "and when those hit, these long-short funds are likely to do better."

#### Redefining the IRA

Just about everyone invests his nest egg in vanilla stocks and bonds. But why not put a fleet of limousines, a peer-to-peer loan to a promising scientist or a rental beach cottage in your retirement account? It might sound bizarre, but tens of thousands of Americans are doing something very similar by using what's called a self-directed IRA. These arrangements allow investors to use their retirement assets to buy almost any item that generates a stream of income, provided the income flows right back into their retirement account. At most, 2 percent of the \$5.7 trillion IRA market is in such investments, but some of the bigger custodians of such IRAs saw double-digit percentage growth in the number of accounts in 2007. "As more people get burned by the stock market, this becomes a way for them to take control," explains Jeff Desich, a vice president of Equity Trust, a company that manages such IRAs. And although official statistics on the success of such investments are not available, Desich claims it's not uncommon for his investors to see double-digit returns.

That sort of promise lured Kim Norton, the Denver real estate agent. Back in 2006, Norton was working for a firm involved in promoting Glass House, a soaring luxury-condo complex being built downtown with an eighth-floor pool deck and killer views of the Rocky Mountains. Seeing how fast the condos were selling, Norton used \$100,000 of her IRA money to scoop up a unit. She then rented it out and sold it early this year, landing a 114 percent return on her investment. Now she says she's well on the way to a second flip — as well as her goal of retiring in her early 50s. "It's all kind of exhilarating," she says.

There's a clear allure to seeing your savings earn go-go entrepreneurial money instead of ho-hum (or worse) stock market returns. But the do-it-yourself market can pose a lot of risks. The majority of investors, for example, use them to buy real estate — and in the recent crash, many have taken painful losses. Ed Slott, an accountant and IRA expert, points out that there's also "a regulatory minefield" surrounding the products. Norton, for instance, will have to pay almost \$22,000 in taxes on her Glass House sale because she used an outside loan to help buy the property. Self-directed investors can't

materially benefit from any of their IRA purchases — if your IRA owns a limo fleet, you can't use it to loan a car to your kid for prom. Most important: There has to be a strict divide between IRA and personal funds. Investors can't devote any of their non-IRA assets to bail out an investment gone sour — or even to pay the cleaning lady or contractor at a rental property. One misstep on any of these fronts and the Internal Revenue Service acts as though all the IRA's money has been withdrawn; the investor must immediately pay taxes on all the funds, and if she's younger than 59 1/2 years old, she faces a 10 percent withdrawal penalty. Daunted? Take heart: The law requires that investors hire a "custodian" company like Equity Trust or Entrust to handle the income and payouts. Generally, adds Slott, people should rely heavily on these firms for advice about the dos and don'ts of managing the investment.

Retire Later — And Richer

In a society where leisure is cherished and people qualify for Social Security payments at 62, the idea of working longer to build up a nest egg might sound pretty groanworthy. But a recent study by the financial-services company T. Rowe Price suggests that relatively minor adjustments in retirement timing can deliver some much-needed punch to the savings accounts of soon-to-be retirees. The study looked at a hypothetical 62-year-old who earns \$100,000 a year and has saved at least \$500,000 for retirement. Assuming that his savings are conservatively invested with only 40 percent in stocks, the study showed that by staying in the workforce and delaying taking Social Security until age 65 (instead of 62), that worker would increase the amount he could live on each year in retirement by at least 20 percent. If he kept it up until age 70 while socking aside \$25,000 a year, his retirement income would grow by 88 percent. Voila: In return for eight years of work, he's getting almost twice the retirement lifestyle.

What makes the difference? Much of it has to do with the impact of delay on your Social Security itself. For workers in this bracket, each year of waiting beyond age 62 raises their annual payment by about 8 percent. In fact, Christine Fahlund, the planner behind the study, notes that because of the Social Security boost, to some extent these preretirees can see their expected standard of living get better even if they save nothing during the 62-to-70 years. Pair that with the benefits of several more years of gains in their portfolios and workers are looking at the potential for a much more luxurious retirement.

Extending a career can boost retirement prospects in other ways as well. The think tank Civic Ventures says that as many as 8.4 million Americans between the ages of 44 and 70 have already embraced what it calls "encore careers" — paid work in fields like health care and education that allow a retiree to have a social impact. And people like Lloyd and Barbara Franklin have found that it's possible to do well financially while doing good. A few years ago Lloyd, who had taught at a seminary in Tennessee, and Barbara, a longtime homemaker, moved to the suburbs of Atlanta and made the transition to teaching eighth graders at a public school that has its share of struggling students. These days Lloyd, who's 55 and teaches English, relishes telling his students, "Each of you has a unique gift, and we're going to polish it up" so the world can appreciate it.

But the Franklins are also polishing up a nest egg that Lloyd says was formerly so small "it was embarrassing." The couple chose the Atlanta area in part because of its generous benefits for school employees: They'll each now qualify for a retirement plan that will pay them a partial pension for life based on how many years they work before retirement. In Georgia, unlike in several other states including California and Texas, collecting a teacher's pension doesn't compromise a retiree's Social Security eligibility. Indeed, the Franklins plan to continue working until late in life, which will pump up the size of their Social Security payments. They've become avid Caribbean cruisers, and Lloyd jokes, "We'll be able to retire to a cabin on the Queen Mary 2."

#### The Small-Business Secret

The sprawling homestead Bob and Susan Hansen moved into this summer is nestled in Montana's Ruby Valley, with a giant deck and sweeping views of Wisconsin Creek, a fly-fishing playground where elk roam. It's their retirement dream house, but if you'd asked them six years ago, they wouldn't have been so sure they'd ever get there. Although Bob had begun earning a very healthy salary as an aerospace executive, the couple's nest egg had just barely cracked six figures, and retiring in their 50s seemed like a long shot. Their solution: A big change in strategy and a series of accounting somersaults. Bob left the corporate world in 2005 and founded Big Sky Consulting, a mostly one-man show (with Susan as scheduler) that advised small aerospace firms on mergers. And with the help of an adviser, he equipped the firm with a defined-benefit plan — the sort of old-school pension one might associate with the good old days of the railroads and airlines. Soon he and Susan were setting aside nearly all their business income, which totaled as much as \$200,000 annually, in tax-deferred retirement accounts; in a year or so, Bob, now 54, hopes to be fully retired. "It just all fit together for us," Bob says, "like a jigsaw puzzle."

Starting your own business to boost your savings may sound counterintuitive — after all, it looks pretty risky compared to a 401(k). Still, the number of entrepreneurs has exploded in recent years thanks to the Internet, which has allowed any mom and pop with a brainchild to start a business at a relatively low cost. And almost one in six small-business owners started his enterprise after age 45, according to the National Federation of Independent Business. Best of all, if a new business does very well and generates enough surplus revenue, it can enable the owner to put together a supercharged pension plan like the Hansens'. Compared with the defined-contribution plans we've all gotten used to, these plans have very high yearly contribution limits, especially for employees older than 45. (They do limit the amount of income one can create for the future at \$185,000 a year — meaning accounts can't grow above \$2.2 million.) The plans can also eventually be rolled into a traditional IRA — so unlike with a traditional pension, the beneficiary has flexibility about where to invest the assets after retiring.

Fewer than 1 percent of businesses with 20 or fewer employees use these plans, but that may very well change. A 2006 pension reform law made them easier to set up, and companies like San Francisco's Dedicated Defined Benefit Services now specialize in

drawing up simple contracts and then administering the plans on the investors' behalf. Still, the plans aren't for everyone, cautions Ted Gregory, the Huntington Beach, Calif., certified financial planner who helped the Hansens. "If you have high volatility in your income," he explains, "the costs can add up quickly"; among other things, you'll have to pay actuaries to revise your plans if your year-to-year contributions are erratic. And if your firm has other full-time employees, the law requires that you sweeten everyone's pot when you sweeten your own — in other words, you have to fund their pensions, too.

Not interested in becoming a part-time pension accountant? Self-employed people still have a lot of flexibility to pump up their nest egg. While corporate types bump up against \$15,500 annual 401(k) contribution limits (\$20,500 if they're age 50 and over), the self-employed can contribute a full 25 percent of their income, up to \$46,000 each year, to Keogh or Simplified Employee Pension plans — typical vehicles used by small businesses. And solo 401(k)s, which are available to businesses with just one full-time, adult employee or one full-time employee plus spouse, can be even more powerful: People age 50 and over can contribute up to \$51,000 a year, and the 25-percent-of-income cap goes away.

Luxury Lifestyle for Less

Living in what used to be a massive chicken coop might not be most people's idea of luxury. But Susan Spencer, an artist in Sebastopol, Calif., sees things a little differently. Eleven years ago she was still living in what she calls "a much too big" four-bedroom house in Minneapolis, dealing with the headaches of frozen pipes and crushing property taxes. Wanting to live closer to her daughter Ellie, Spencer decided to sell the house and rent instead. First she took a comfortable apartment in San Francisco; now, at 76, she's settled down into the "coop" — an airy cottage with sliding glass doors and an inviting front porch that she rents for \$1,500 a month. Meanwhile, a good chunk of the proceeds from the sale of her Minnesota home is still invested and growing, and paying for a very comfortable and active retirement. "It's given me freedom on so many levels," Spencer says of her decision. That freedom has included the ability to take vacations with her eight grandchildren: Grandmother-grandkid adventures have included a two-week trip through England focused on the Harry Potter series and a Lord of the Rings-themed excursion in New Zealand.

It's rather crude math, but a retiree who cuts her costs of living in half has, in effect, doubled the value of her savings. It's a potentially attractive idea, but one that doesn't always sit easily with boomers who've spent decades accumulating wealth. Some advisers, though, are now focusing on easing such emotional transitions while making the new lifestyle comfortable. **Spencer Sherman**, a San Francisco-based adviser, says he often asks wealthy clients to do an exercise where they write down how they would live a full, happy life on half their current income. "People often end up imagining a life that's fuller than what they have now," he says. They imagine moving into the city, having more potluck dinners with friends, and walking more places instead of driving. Not surprisingly, the sell-and-rent move often dovetails with such goals. And as Sherman notes, those who make that move often come out ahead financially, too, given

the vast maintenance costs of a mini-mansion and the potential upside of investing the difference between the costs of owning and renting.

There are other ways to make a nest egg do double the work, of course. One is to move to a town where costs of living are lower; the Web site Sperling's Best Places lets consumers compare how costs overall (and housing costs in particular) vary from city to city. If a couple moves from Chevy Chase, Md., to the cozy nearby beach community of Lewes, Del., for example, their cost of living will drop by 47 percent, according to the site. That means if they're living on \$100,000 a year in the tony Washington, D.C., suburbs, they could survive on roughly \$53,000 on the Delaware shore, without compromising their standard of living.

As gas prices soar to Himalayan peaks, it's also worth taking a hard look at the car in the driveway. Buying a used 2005 Lexus GS 430 sedan instead of a comparable but brand-new 460 model will save a driver more than \$23,000 in ownership costs alone during the first five years after the purchase, according to car site Edmunds.com. Those costs include insurance, taxes and evil old depreciation, which makes a car lose much of its resale value in the early years of ownership. And all those savings come on top of the roughly \$22,000 the buyer would save at the dealership — freeing up still more money to invest in other aspects of the good life.