

ABEL Strategy — Second Quarter 2006 — July 5, 2006
Managed Investments & Retirement Planning

Die or Your Money Back

The title grabbed my attention and the content really tweaked my interest. Most clients know that you either buy or rent life insurance, just as you do a house. Buying life insurance entails making substantially larger payments than if you rent it. Now you can buy a policy that lets you make payments just slightly higher than the rented policy (term insurance) and which gives you all your payments back at the end of the term.

The need for life insurance is most evident when a couple starts their family. Prior to that, and especially if both spouses are working, the death of one spouse is more an emotional loss than an unbearable financial loss. So most young families are probably looking at a 30 year period during which coverage is needed.

At age 31 a 30-year \$1,000,000 term policy for a non-smoker costs \$1090 from Transamerica. That's over \$30,000 paid out with nothing to show for it other than the peace of mind it has bought. And whole life as an alternative is immensely more expensive. Enter the "return-of-premium" (ROP) term policy. At the end of 30 years you get all your premiums back, without interest. If you had died during the 30 year period, your beneficiary would have received \$1,000,000 income tax free.

It makes sense. Odds are that you will get your money back. The chance of a 31 year old dying by age 61 is just 5%. This policy from Genworth Financial costs \$1,671 per year (\$581 more than plain term). That extra payment amounts to \$17,430 by age 61 and will return \$50,130. The return is 6.3% a year.

If you walk away from the policy before the 30 years, you also walk away from some or all of the virtual savings account. Most companies will return 9% of your payments after 10 years, 19% after 15 years and 35% after 20 years. A policyholder may be inclined to 'walk' due to a divorce, a lack of financial discipline or a desire to change to a different kind of policy. Industry experience shows that 5% of term policies lapse each year. It is these facts that make this kind of policy attractive for the insurance companies.

What of the tax consequences? An economist would argue that \$1090 of the annual payment was buying a lottery ticket with a \$1 million payoff and the \$581 is like an investment in a bank account earning 6.3%, and that the gain (\$50,130 - \$17,430) should be taxable as interest income. Life insurance policies, however, are treated very favorably in the Tax Code. The \$50,130 returned above is likely to be tax free – the policyholder is simply getting his/her premiums back.

ROP policies are best suited for people who are young, healthy and disciplined. The older and less than good health buyer is likely to be better off in a traditional term policy. And you want to buy them from companies rated A+ or better from AM Best.

Condensed from Forbes Magazine April 24, 2006 – Carrie Coolidge

Jim Ellman

Cautious Opportunism

- Lahcen Abidar, Portfolio Manager

An investment style would be described as opportunistic when its main focus is on companies whose prices are depressed yet whose longer term fundamentals are attractive. Depressed prices can result from a number of factors: an interruption in earnings, a recent earnings disappointment, a temporary stall in business growth, a downturn in the industry, declining operating margins, management changes, or whose assets, or potential for growth, are simply not well understood by the market.

Our "master list" is one of high quality companies with long histories of earnings reliability and superior fundamentals. These are factors which offer the best gauge of a company's potential ability to rebound. The successful turn-arounds in our portfolio usually begin with earnings recovery and continue with a climbing stock price. That can take up to 24 months to occur. If after two years the stock is still out of favor and the price isn't returning toward "fair value", we would sell and move on to another opportunity. Sometimes stocks can be so undervalued they become take-over candidates, as was the case with Albertson's and MBNA.

So while we are opportunistic managers, we are also cautious ones. On top of seeking a decent return for our clients, we take managing risk quite seriously. You can evaluate our ability to reduce market risk (volatility) by comparing your account performance for a bad month to the performance of the S&P500 (the "market").

In the current environment our goal remains unchanged: to assume less risk than the market and seek higher return. So far for the first half of 2006 we are doing that: most client accounts were less volatile than the market, and were up between 4.5% and 5.2% while the S&P 500 was up 2.7%.

	2nd Qtr	12 Mos	3 years
Dow	+0.94%	+11.1%	+ 9.9%/yr
S&P500	-1.44%	+ 8.6%	+11.2%/yr
Nasdaq	-7.01%	+ 6.5%	+10.9%/yr
ABEL Strategy	-0.39%	+ 5.6%	+ 8.5%/yr *

* includes mix of Stocks, Funds and Cash

⇒ Index numbers from Managers Funds

Wise Words To Live By

"The expression and management and passing on of values is much more important than the passing on of wealth. If you pass them on together, you have created something powerful for the individual, the family, and for society. That's true whether you are worth \$100 or \$100 million."

- Stuart Lucas, a fourth-generation heir to the Carnation fortune

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Statistics ...

76 ... Percentage of college students carrying credit cards in 2004, down from 83% in 2001. (Nellie Mae)

15,000 ... Number of tax law changes since the 1986 tax act. (Associated Press)

13 ... percentage of private-sector employers that offered early-retiree health benefits in 2002, versus 22% in 1997. (Employee Benefit Research Institute)

33... Percentage of US single-family housing market that is extremely overvalued. (National City Corp)

72... percentage of Americans earning over \$125,000 who clip supermarket coupons, versus 65% for the population at large. (VISA)

20 ... percentage of lottery players, mostly low income, minority men, who provide 82% of lottery revenues.. (Associated Press)

4.1 ... Percentage hike in monthly Social Security income for 2006, the largest since 5.4% in 1991. (Social Security Admin)

40 ... Percentage of US labor force that will reach traditional retirement age by 2010. (Conference Board) XXX

The Independent 529 Plan

It's a prepaid tuition plan. This unique plan lets you buy 'tuition certificates' for a child that he or she can redeem later. The Plan is treated the same as a 529 Savings Plan. No more than 5.6% of the plan value will be used to assess need if financial aid is applied for under federal guidelines.

There are more than 250 private colleges and universities participating nationwide, offering a variety of choices to fit the talents and interests of every student. And the list grows annually.

With the Independent 529 Plan there is no market risk. Member colleges and universities carry the risk in exchange for prepayment. When you pay a percentage of today's tuition rate you get that same percentage as a discount in the future, no matter the actual future tuition cost.

Many institutions discount today's tuition rate as an incentive to participate. And the Independent 529 Plan is federal tax-free, at least until Dec 31st 2010 when a number of current tax code provisions expire. Congress may extend the law in the future.

Interested? If you would like to see the list of colleges and universities participating in the program, go to their web site, or call their toll-free number below.

Visit www.independent529plan.org
or call 888-718-7878

Independent 529 Plan

Of Times Gone By

Consider the following

- ◆ US average life expectancy was age 47
- ◆ 14% of our homes had bathtubs
- ◆ 8% had a telephone
- ◆ A 3 minute call between Denver and NY cost \$11
- ◆ There were only 8,000 cars on our 144 miles of paved roads
- ◆ Mississippi had a larger population than California
- ◆ The average wage in the US was 22 cents per hour
- ◆ The average worker made \$200 to \$400 per year
- ◆ A dentist made \$2,500 a year
- ◆ 95% of births took place at home
- ◆ 90% of the doctors had no college education
- ◆ Most women washed their hair once a month, and used borax or egg yolks for shampoo
- ◆ Five leading causes of death: pneumonia & influenza, Tuberculosis, diarrhea, heart disease, stroke.
- ◆ 2 of 10 adults could not read or write.
- ◆ Only 6% had graduated from high school.
- ◆ There were 230 reported murders in the entire US.
- ◆ Marijuana, heroin and morphine were all available over the counter at the local corner drugstores. Back then pharmacists said, "Heroin clears the complexion, gives buoyancy to the mind, regulates the stomach and bowels, and is, in fact, a perfect guardian of health."

The year? 1905



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"To succeed, jump as quickly at opportunities as you do at conclusions." - **Ben Franklin**

Maximum Initial Withdrawal Rates – An Update

How much income can I safely take from my investment portfolio continues to be one of the most frequently asked questions by people approaching, at, or in retirement.

First the Portfolio Management Rule – this determines the source of each year's withdrawal.

- Assets performing better than expected are reduced; proceeds to cash
- Funded in the following order:
 - Over-weighted equity assets
 - Over-weighted fixed income assets
 - Cash
 - Remaining fixed income assets
 - Remaining equity assets
- No withdrawal taken from an equity with a negative return if cash or fixed income assets are sufficient to fund the withdrawal

Then the Inflation Rule – this determines the size of the yearly increase.

- Withdrawals are increased by the annual inflation rate as measured by the CPI except when the Withdrawal Rule freezes withdrawals
- Maximum annual increase is 6%
- No make-up for capped adjustments
- Not applied if Capital Preservation Rule is in effect

A Capital Preservation Rule – when current year's rate is >20% above the initial rate

- Current year's withdrawal reduced by 10%
- Not applied the last 15 years of expectancy

A Prosperity Rule – when the current year's rate is <20% below the initial rate

- Current year's withdrawal increased by 10%

And lastly the Withdrawal Rule – conditions when withdrawals are frozen

- No increase in a subsequent year when the portfolio rate of return is negative, and the new year's rate would be larger than the initial year.
- No make-up for missed increases

Possible allocations between asset classes:

Asset Class	Index	50% Equities	65% Equities	80% Equities
Cash	90 day T-Bill	10%	10%	10%
Fixed Income	LB Agg Bond	40%	25%	10%
Lg Cap Val	Russell 1000 V	10%	13%	15%
Lg Cap Gro	Russell 1000 G	10%	13%	15%
Sm Cap Val	Russell 2000 V	7%	9%	10%
Sm Cap Gro	Russell 2000 G	7%	9%	10%
International	EAFE	11%	15%	20%
Real Estate	Wilshire REIT	5%	6%	10%

Applying the above rules to a 65% Portfolio allows for an initial withdrawal rate of between 5.4% and 6.2% with a 95% to 99% chance of lasting for 40 years.