



PRODUCT ALLOCATION AND EXPENSES

Paula is a 59 year-old widow who plans on retiring next year. She receives a survivor’s benefit from her husband’s pension of \$10,000 per year. She is also entitled to her Canada Pension Plan (CPP) at age 60, and Old Age Security (OAS) at age 65. Before the market meltdown that began in the latter part of 2008, Paula had an investment portfolio that was valued at \$969,000. Today, it’s worth \$725,000 – a drop of over 25%! In response to the volatility of the markets, Paula switched all of her investments to cash-equivalent investments, a reaction stemming from her conservative investment style.

When Paula retires, she hopes to have an income of \$55,000 annually before taxes. With her retirement nest egg having already lost 25%, she has serious concerns about being able to have the retirement lifestyle she wants. Paula wants to find out if her current retirement income plan is on track and if there’s anything she can do to help meet her retirement income goals. A co-worker recommends her advisor, Doug.

Retirement Expense Worksheet

| Category | Amount |
|----------------------------------------|--------------------|
| Essential Expenses | |
| Housing | \$13,426.00 |
| Transportation | \$6,454.00 |
| Daily Living | \$6,550.00 |
| Healthcare Expenses | \$2,454.00 |
| Financial Obligations | \$996.00 |
| Total Essential Expenses | \$29,880.00 |
| Discretionary Expenses | |
| Recreation & Leisure | \$5,920.00 |
| Miscellaneous | \$5,000.00 |
| Total Discretionary Expenses | \$10,920.00 |
| Total Expenses from all Sources | \$40,800.00 |

| Category | Amount |
|-------------------------|------------|
| Gas/Fuel | \$1,400.00 |
| Insurance (Car) | \$738.00 |
| Loan/Lease Payments | \$3,766.00 |
| Public Transit | |
| Maintenance and Repairs | \$550.00 |
| Parking | |
| Other (please specify) | |

To help Paula stress test her retirement income plan, Doug explains that he needs to understand all of the details about her financial situation. He asks Paula to first complete a budget showing what her anticipated expenses will be in retirement separating her essential expenses (such as housing, food and clothing) from her lifestyle expenses (travel, entertainment, restaurants, hobbies etc.).

Based on this information, Doug determines that Paula needs \$40,800 annual income after taxes: approximately \$29,880 to cover off her essential expenses and a little over \$10,920 for her discretionary expenses. Doug is then able to establish that the \$55,000 pre-tax income will provide the money she needs to achieve her goals.

Using this gross income amount, Doug then uses Manulife's Product Allocation Tool to test Paula's investment portfolio. Paula's move to a 100% cash-equivalent portfolio isn't helping her retirement income plan. The Retirement Sustainability Quotient (RSQ) for her current portfolio is 68%. An RSQ in this range indicates that the desired retirement income may only be sustainable for the early part of retirement and is not likely to be sustainable for life. Doug suggests that Paula may want to consider adjusting both the Asset Allocation and Product Allocation of her investment portfolio.

Doug uses the Product Allocation Tool to identify a model Product Allocation portfolio that will help improve her current situation. The results suggest Paula will be much better off if she invests 80% of her portfolio in an Annuity, 15% in a GMWB (Guaranteed Minimum Withdrawal Benefit) product and 5% in Mutual Funds with a SWP (Systematic Withdrawal Plan) option. The probability of Paula sustaining her retirement income throughout her lifetime is now 99% based on her new RSQ.

While this is a drastic improvement over her current situation, both Paula and Doug agree that this solution is not ideal for Paula since she does not want to completely give up control of her investment portfolio. Knowing Paula's essential and discretionary income goals, Doug makes adjustments to the model Product Allocation to customize Paula's retirement income plan. Doug decides a good approach is to cover Paula's essential expenses with guaranteed products and her discretionary expenses with traditional investments that offer a SWP.

Based on Paula's preferences and risk tolerance, Doug recommends Paula put 75% of her portfolio in guaranteed products to cover her essential expenses by investing 15% in an Annuity and the balance, 60%, in a GMWB (30% fixed income/70% equity). To cover discretionary expenses, the remaining 25% of Paula's portfolio would be invested in a SWP with a balanced portfolio of 5% Cash, 35% Fixed Income and 60% Equity.

Paula's new RSQ is 94%, a dramatic improvement over the RSQ of 68% she started with. This is a satisfactory score that will help ensure she sustains her income for life. Despite the 25% drop in the value of Paula's investment portfolio, she will likely be able to retire with her desired income level.



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