
Floor It!

By Editor Test Thu, Mar 25, 2010

In the Arizona desert, Mike Zwecher had a vision that led to his new book on building outcome-oriented retirement portfolios.

Seekers of enlightenment travel to Sedona, Arizona to drink from the region's legendary font of spiritual energy. So Michael J. Zwecher still marvels that he just happened to be there, after attending the 2008 Super Bowl, when he received his life-changing insight about retirement portfolios.

"In Sedona, it dawned on me that you could make a lot of the retirement income framework compatible with an accumulation framework," he told RIJ recently. "You simply had to reformat it a little bit.

"You just shift the fixed income component of your portfolio from an amorphous blob of relatively safe securities into something that delivers an outcome. Not just safe—but delivers a tangible outcome."

That was two years ago, when Zwecher took the first step on an intellectual journey that led him from risk management at the pre-BofA Merrill Lynch to finishing a book that shows financial advisers how to build outcome-based portfolios for retirees.

In the book, [Retirement Portfolios: Theory, Construction, and Management](#) (John Wiley & Sons, 2010), whose text is by turns technical, straight-forward and lyrical, Zwecher proposes that retirement investing is very different from pre-retirement investing.

The first is comparable to flying a plane at 30,000 feet; the other, as he put it, is like trying to land that plane on an aircraft carrier deck. "With a perpetual horizon," he writes, "there will always be another whack at the cat and the world isn't about to end; riding out a storm may be a feasible tactic... In retirement, the strategy is to protect lifestyle and there is only one whack at the cat."

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In pursuit of that protection, the book advocates the division of a retiree's assets into "flooring"—comprised of sources of guaranteed income such as Treasury strips, income annuities, private pensions or Social Security—and everything left over, which provides emergency cash, a planned bequest and money for growth or "upside potential."

While Zwecher's book (and accompanying workbook) is useful for any adviser, it is actually a required text in the core curriculum of the Retirement Management Analyst designation, a new credential created by the Retirement Income Industry Association, or RIIA, which held its annual conference in Chicago this week. (See cover story, ["Spock-o-nomics at the RIIA Meeting."](#))

RIIA, for those who are not familiar with it, is an organization started in 2005 by Francois Gadenne, a French-born, Boston-based entrepreneur in the retirement field. He had been urged by friends in the financial services industry to start a new kind of trade group.

What the industry needed, they said, was a forum where all sectors of the retirement industry—advisers, economists, asset managers, insurers—could swap ideas. It would take a blend of views from all of those “silos,” they believed, to create income solutions for retiring Boomers.

Gadenne and Zwecher met a few years ago and found that they shared similar ideas about retirement income. When Zwecher left Merrill Lynch they collaborated on the creation of the RMA designation and co-wrote an RMA training manual, *How to Benefit from the View Across the Silos* (RIIA Publishing, 2009). It and Zwecher’s new book are the basic texts for the designation.

Advisors who have never considered any retirement income strategy for their clients other than the systematic withdrawal of four percent per year from a balanced portfolio should find Zwecher’s book eye-opening. On the hand, advisors who are accustomed to building bond ladders or incorporating annuities into their retired clients’ will find themselves in fairly familiar territory.

Zwecher’s system shares some of the elements of so-called bucketing methods. It involves different pots of money for generating a reliable retirement paycheck, for emergencies, and for potential growth. But he doesn’t believe that stocks can ever be fully relied on to produce income—even when given a time horizon of 15 or 20 years.

The ideal reader for Zwecher’s book is an advisor who is a “student of the game” and who enjoys thinking about this stuff. The ideal clients for the solutions described in the book would be people whose annual income needs in retirement will be more than 3.5% but less than 7% of their investments.

As the book explains, people who need less than 3.5% a year can generally afford to live on interest and dividends. Those who need more than 7% of their savings each year often need help from income annuities, whose “mortality credits” can help make up for a shortage of savings.

The book is filled with nuggets that are likely to stick in the mind: “We want to change the focus from volatility to outcomes,” and “Having the flooring in place creates a freedom in the upside portfolio that was not previously there” and “Lifestyle relative to wealth and not just the wealth level that matters for a flooring recommendation.”

In one memorable passage, Zwecher writes, “Portfolios are occasionally described as gardens to be watered, weeded, and pruned. Even if your portfolio were a garden, your portfolio isn’t meant as a flower garden, but a vegetable garden. You probably didn’t work hard and save money just to create something decorative... your portfolio is not an end in itself, but a means to achieve your ends.”

The financial crisis, Zwecher believes, is making more clients question the value of financial advice. “Trying to pick winners is the weakest way for advisors to earn their fee,” he told RIJ. Going forward, he thinks, advisors can best justify their fee by ensuring that the client’s portfolio achieves its primary mission: providing lifetime income.