

Client Analyzer Overview

Rod Greenshields,
Manager, Wealth
Management Solutions

WHAT DOES THE ANALYZER DO?

The Client Analyzer helps you assess your clients' retirement-funding status, and then maps each outcome to one of several advice profiles. The profiles include recommendations for specific actions you might take to increase the likelihood that your clients will achieve their retirement objectives.

Use it to **analyze an individual client — or your entire client roster**. This tool is flexible enough to provide either analysis. It also gives you the option to print a brief report summarizing the analysis of any single client you select.

You'll be able to see which clients have been most affected by market events and need immediate attention. Then, the tool output points you to specific recommendations for each client based on the profile the client maps to.

HOW DOES THE ANALYZER WORK?

The Client Analyzer is based on two related tests. The first assesses the feasibility of achieving an investor's desired spending goal. The second assesses the viability of establishing a minimum-spending floor based on the cost of a guaranteed¹ immediate lifetime annuity. The two tests are:

1. **Desired Spending Test** (applicable for all clients in or near retirement):
 - Assesses the probability of success for clients' original retirement spending goals, based on their portfolio value and other income sources
 - Categorizes clients into one of four zones — Red, Orange, Yellow or Green — based on their probability of success
 - Provides a comparative, sustainable-spending level that would meet the Green Zone standard (defined as a 90% probability of success). This may help frame discussions with clients whose desired spending goals exceed sustainable levels.
2. **Minimum Spending Test** (recommended for clients needing immediate attention):
 - Assesses the current viability of establishing a minimum-spending floor
 - Evaluates each client's current portfolio value relative to the cost of annuitizing,² if the client needed to establish a guaranteed-income floor

¹ Subject to the claims-paying ability of the insurer.

² While there are other approaches to creating secure income streams, including the use of CDs and fixed income strategies, they do not have the same characteristics as annuities.

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- Categorizes client profiles into Red, Orange, Yellow or Green zones based on how close they are to their minimum-spending floor.

HOW TO USE IT

The analyzer relies on basic client data that you, or your staff, enter into a workbook. All spending amounts are stated in annual terms gross of taxes (any taxes owed are to be paid out of the spending level that you input).

For the Desired Spending Test, the following inputs are required:

- Name
- Age
- Gender and Marital Status
- Retirement Status: Nearly Retired (< 3 years) or Retired
- Current Portfolio Value
- Income from Other Sources — Social Security, pensions, etc.
- Desired Spending Goal — the annual spending budget during retirement years, gross of taxes. For the test, this is modeled in the future as an inflation-adjusted value.

The analyzer calculates a spending gap by subtracting Income from Other Sources from the Desired Spending Goal. (The resulting Spending Gap is assumed to be adjusted for inflation every year.) The analyzer then applies a number of the data points to Monte Carlo simulation calculations, using Russell capital markets forecasts and actuarial mortality tables. This produces a sustainable-withdrawal-rate analysis that is rigorous enough to be useful in guiding conversations with your clients. Retirement planning is complicated with multiple factors to address. The analyzer models three of the major risks — investment, inflation and longevity.

The withdrawal-rate analysis matches the output of each client's situation to one of these four categories:

- Red Zone (less than 70% chance of being sustainable)
- Orange Zone (70% to 80% chance of being sustainable)
- Yellow Zone (80% to 90% chance of being sustainable)
- Green Zone (greater than 90% chance of being sustainable)

MAPPING TO ADVICE PROFILES

Because clients nearing retirement have different options than those already in retirement, each zone has two advice profiles (one for each retirement status), resulting in eight different profiles for you to use with your clients.

Investors in any situation (with the possible exception of those in the Green Zone) should consider their choices based on several factors. These include, but are not limited to, future income potential, spending habits, and investment decisions. Each of the eight advice profiles addresses the priority and potential impact of each decision. The information represents general guidelines. Each investor's situation may be different, and the analyzer may not take into account all variables which could affect the outcome. Advisors are responsible for making appropriate recommendations.

A SECOND TEST FOR CLIENTS NEEDING IMMEDIATE ATTENTION

For clients in the Red Zone, the Orange Zone and perhaps the Yellow Zone, consider conducting further analysis using the analyzer's Minimum Spending Test. This test requires two additional client inputs:

- Minimum Spending Floor — Clients faring poorly in the first test should assess an alternative plan based on reduced spending expectations.
- Cost to Guarantee Minimum Spending Gap — This value represents the cost of annuitizing the difference between the Minimum Spending Floor and Income from Other Sources for the rest of the client's life (or clients' lives, in the case of a joint life annuity). You may obtain this information by using insurance provider annuity pricing data.³

This second analysis evaluates the client's portfolio value based on assets required to meet the stated Minimum Spending Floor if the client needs a guaranteed income level.

Like the withdrawal-rate analysis, the Minimum Spending Test matches the output of each client's situation to one of four color-coded Funding Ratio categories. These categories are based on the value of assets in a portfolio relative to the cost of buying an annuity to meet the spending gap. The specific threshold values are defined so that a "favorable" status requires a surplus of assets relative to the cost to annuitize.

The rationale for this is that it's important to have a cushion of assets in case portfolio losses or changing annuity prices reduce a client's ability to establish this income floor. The color-coded labels associated with these percentage ranges (outlined below) are based on Russell's judgment of what constitutes funding ratios ranging from imprudent to prudent.

Funding Ratio categories:

- Red Zone (portfolio value is less than 100% of required amount)
- Orange Zone (portfolio value is 100% to 120% of required amount)
- Yellow Zone (portfolio value is 120% to 140% of required amount)
- Green Zone (portfolio value is greater than 140% of required amount)

While the Desired Spending Test always assumes you'll adjust spending for inflation, the results for the Minimum Spending Test depend on the type of annuity price quote you use. The results will only reflect inflation-adjusted future income if you enter the price for an inflation-adjusted annuity.

You'll find detailed instructions for using the Client Analyzer on the Instructions tab in the downloadable workbook.

³ Note that if you want to plan for the Minimum Spending Gap to be adjusted for inflation each year, the annuity price must reflect inflation-indexed payments. Inflation-indexed annuities are more expensive than fixed-payment annuities.

IMPORTANT INFORMATION

The projections or other information delivered through the Client Analyzer regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results and are not guarantees of future results.

Limitations of analysis and risks of investment:

- The analyses in the Analyzer are conducted using hypothetical estimates of future market conditions based upon Russell strategic-planning assumptions and with certain numerical models applied to that information. These assumptions may change over time. These analyses are not meant to serve as direct predictions regarding the future performance of assets or the income and capital gains that they might produce. Similarly, they are in no way intended to predict or guarantee future investment performance of any sort.
- The information contained in the advice profiles represents general guidelines. Since each investor's situation will be different, the Client Analyzer may not take into account all of the variables that could affect the outcome.
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Monte Carlo simulation methodology:

The Client Analyzer results related to the Desired Spending Test are created with Monte Carlo simulation, a sophisticated mathematical approach used within the financial industry to model possible outcomes of future investment scenarios.

The process is designed to reflect the forecasted volatility of investment markets and other economic variables. These scenarios are created using Russell Investment's proprietary forecasting models incorporating historical data from market and economic indexes. The scenarios model investment performance for a set of asset classes (i.e., stocks, bonds, cash, etc.); the level of interest rates; and the rate of inflation, to estimate how each might affect the portfolio balance over time.

While this method may reflect the uncertainty and randomness of future events, it is important to understand that it is based on assumptions about the future risk and expected returns of each asset class.

Key assumptions:

- The forecasts assume that a portfolio is well diversified and that the mix of investments in this portfolio is maintained for the entire simulated horizon, with no additional investments, no margin borrowing or short sales, annual rebalancing back to the proposed allocation and no transaction fees on this rebalancing. Russell's strategic planning assumptions are updated semiannually.
- Because assumptions about the capital markets evolve over time, results of the calculations may vary over time. Your portfolio may not be adequately diversified, which could affect the validity of the simulation process described above when applied to your actual circumstances. Furthermore, these forecasts do not consider return and risk differences associated with holding a highly concentrated position, nor how long a security is held. Other asset classes or investments not considered in this analysis may produce different results. There also may be other considerations pertinent to your client's situation that have not been addressed, including, but not limited to, market conditions, the tax position of your client's assets or cash flows, or other available assets, such as personal real estate or other investments not included in this analysis.

Forecasting represents predictions of market prices and/or volume patterns utilizing varying analytical data. It is not representative of a projection of the stock market, or of any specific investment.

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This hypothetical example is for illustration only and is not intended to reflect the return of any actual investment. Investments do not typically grow at an even rate of return and may experience negative growth.

IMPORTANT: The projections or other information generated by the Client Analyzer regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results and are not guarantees of future results.

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Diversification and strategic asset allocation do not assure profit or protect against loss in declining markets.

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