BONDS

Scarsdale Investment Group, Ltd.

All Bond Portfolios

Using Bonds to Create A Paycheck For Retirement Planning

The goal of retirement planning is to replace your earned income with a reliable and consistent stream of predictable income, (i.e. cash flow). We call this the paycheck system of investing; its goal is to provide you with financial independence. A paycheck from bonds can be relied upon to provide you with a secure form of income. High quality bonds have low risk, low fees and are tax efficient.

The major sources of cash flow to replace or supplement your earned income are generally as follows:

- Rental income: Requires managing one or more properties.
- Dividend income: Requires predicting the direction of stock values, and may result in significant losses.
- Annuity income: You make the insurance company your heir, and give up control of your investment.
- Bond income: You receive semi-annual interest payments and a return of your investment on a specified date.

We believe that high quality bonds are the best source of cash flow in retirement   because only by investing in bonds can you predict your monthly and annual income, and they require no maintenance. Though the value of bonds will fluctuate just like any other investment, only bonds will return their face value on a specified date. Face value is the term used to describe the amount of money or principal you will receive when the bonds come due.

What is a Bond?

Bonds are debt securities. For example, the United States government raises cash by issuing Treasury bonds, Treasury Inflation Protected Securities (TIPS), and EE and I- Savings Bonds. Municipalities, Federal agencies, and corporations also issue bonds. These bonds are purchased by individuals, US and foreign institutions and corporations. Tax-exempt municipal bonds are favored by individuals because they may not be subject to federal, state, and local taxes. However, you can purchase all of the other kinds of bonds in your retirement accounts.

Why Not Purchase a Bond Fund?

All bonds are not created equal. We recommend that you only buy high quality bonds to avoid a potential loss. Why not just buy a bond fund? The bond fund may hold low quality bonds, foreign securities and derivatives that may result in large losses. Most bond fund or ETF buyers do not look under the hood. In addition, bond funds are actually quasi-equities and unlike individual bonds, the funds never come due. The funds may also charge high annual fees, as well as burdening you with the costs of trading. If interest rates rise, the value of a bond or a bond fund will decline. However, though the value of individual bonds will fluctuate, they will pay their face value when they come due. We have written a lengthy article on this subject found on our website, www.allbondportfolios.com

The Bond Ladder

A powerful strategy for using bonds in retirement planning involves the creation of a custom bond ladder. Investing in a bond ladder means buying individual bonds that have different maturity dates. For example, you might have bonds coming due each year starting in year 5 and then coming due in each subsequent year through year 15. In addition, if you need a bigger paycheck for a specific purpose, such as your child's college education in ten to fourteen years, you can purchase an unequal amount of bonds coming due in those years. The issuer is required to redeem the bonds in the maturity year, thus facilitating your planning.

If you plan on retiring in 15 years, you can establish a bond ladder that integrates your personal account, your IRA and Roth accounts that will mature starting in year 15. You can choose to reinvest the proceeds of your bonds as they come due to create more income, or start living off the principal. Reinvested interest payments give you investment growth through the compounding of interest. Knowing you have cash flow from your bond ladder to supplement other sources of income, as well as the predictability of lump sum payments, can relieve a lot of stress.

Tax Benefits of Municipal Bonds

The interest income paid by many municipal bonds is not subject to Federal income tax. In addition, if you have made you legal residence (or domicile) in a state that has no personal income tax, such Texas, Florida, or the District of Columbia you would not pay any state or local income tax on your tax-exempt municipal bond income, even if you find yourself stationed in a high tax state.,

Benefits of Bonds

An investment in high quality bonds will help you sleep at night. You can predict when the principal will be returned to you. You will get interest payments every six months for the life of your investment. You can plan for your future concretely instead of hoping that your investments will have risen in value just at the moment you need to withdraw funds. You can create a tax-free diversified bond portfolio no matter where you are deployed. You will be able to count on a paycheck that you have created.