



**Efficient Frontiers in Estate Planning** (pp. 1-27)

Ronald R. Crabb

This article explores the nature of the efficient frontier in probabilistic estate planning for 16 different estate plans by considering as random variables ages at death, rates of return on assets, and borrowing rates on debts. The simulation considers two couples, one middle aged, the other elderly. Two 16x16 matrices, one for each couple, are used to record and compare the results of every simulation. That comparative data, in conjunction with the coefficient of variations based efficient frontier, contain useful information for couples who consistent with their levels of risk, desire to maximize the net present value of assets passing to their heirs. The efficient frontier is shown to be a function of three factors: assumptions, ages of the estate owners, and the discount rates of the heirs. Because of the instability shown in the efficient frontier, estate planners and estate owners must carefully examine not only the estate plans which fall on the efficient frontier but also those estate plans which fall just off that frontier.

**Market Timing for the Individual Investor: Using the Predictability of Long-Horizon Stock Returns to Enhance Portfolio Performance** (pp. 29-43)

Steven P. Rich, William Reichenstein

Recent research indicates that dividend yield and earnings-price ratio can partially predict long-horizon stock returns. We examine whether individual investors can successfully construct timing portfolios based on either of these variables or a measure of the expected market risk premium. The out-of-sample tests in this study require that investors rely only on information that was available at the time of the market-timing decision. Timing portfolios based on the market risk premium show the strongest ability to time the market. We present an economic rationale for the results that is consistent with efficient markets.

## **Real Income Growth and Optimal Credit Use** (pp. 45-58)

Jessie X. Fan, Y. Regina Chang, Sherman Hanna

Borrowing may be optimal if real income is expected to increase. If income growth is uncertain, optimal credit use is not obvious. A two period model of consumption for determining optimal credit use is presented. The impact of real income growth is analyzed with numerical analysis. The results may be useful for financial counselors and educators, as well as for insight into empirical patterns of credit use. The income growth rate expected by the household plays a crucial role in determining optimal credit use for current consumption.

## **The Individual's Tax-Exempt Bond Portfolio Decision Under Income Uncertainty** (pp. 59-73)

Amy V. Puelz

In this article, an individual's tax-exempt bond portfolio decision is investigated. A model capturing the relationship between income uncertainty and optimal portfolio choice is defined when all individual decision-maker has the opportunity to hold higher yielding private-activity bonds. The findings in this article show that in most cases risk-averse individuals will maximize the expected ability of after-tax income by holding a large proportion of private-activity bonds in their portfolio even under income uncertainty and the risk of a minimum tax liability. Those individuals who would benefit from holding private-activity bonds in a tax-exempt portfolio are identified and the magnitude of the benefit is quantified.

## **An Empirical Analysis of the Use of Money Orders, the Payment System of the Poor** (pp. 75-81)

Kenneth N. Daniels, Neil B. Murphy, Dennis M. O'Toole

Although money orders have been available in the United States since the Civil War, until the mid 1970's and the failure of United States Navigation Company and Universal Money Orders, there had been little analysis of the money order market. This study empirically investigates the determinants of money order usage by households. The results of the study, which utilizes two large national samples, indicate that money orders are clearly an inferior good which have a high probability of being purchased by a low income, young, ethnic minority.

**An Optimization Model for Scheduling Withdrawals from Tax-Deferred Retirement Accounts** (pp. 93-108)

Cliff T. Ragsdale, Andrew F. Seila, Philip L. Little

As a growing number of Americans reach retirement age, more and more people are facing important decisions about how to withdraw savings from tax-deferred retirement accounts (TDRAs). These decisions are complicated by the Federal Tax Code which imposes a number of rules and regulations on these withdrawals. Since these decisions collectively involve billions of dollars, the potential loss from even slightly suboptimal decision making is very large. In this paper, we present a mathematical programming model that can be used to assist retirees and/or their advisors in determining the optimal schedule of withdrawals from TDRA's.

**Asset Allocation, Life Expectancy and Shortfall** (pp. 109-126)

Kwok Ho, Moshe Arye Milevsky, Chris Robinson

An analytical model provides a solution to the retirement problem of how to allocate investment between risky and risk-free assets. The objective is to minimize the probability that the retiree will be unable to consume at the desired level over his/her expected lifetime. The procedure incorporates mortality tables, real or nominal rates of return, initial wealth, and desired consumption levels. Numerical Examples using standard mortality table, historic rates of return on Canadian equity and treasury bills, and a range of realistic values for wealth and consumption show that equity should play a much bigger role in retirement portfolios than other writers advise.

**The Impact of Mutual Fund Distributions on After-Tax Returns**  
(pp. 127-141)

William Lewis Randolph

This paper analyzes the impact of mutual fund distributions on after-tax returns. Mutual fund objective and management style are the two most important factors which determine the proportion of the fund's total return that is paid out in distributions. The larger the fund's annual distributions, the greater the amount of return lost to taxes. The correlation between portfolio turnover and after-tax return is examined and found to be low. A measure of effective portfolio turnover is developed to show the real effect of turnover on distributions. Within some mutual fund categories, the investor can increase after-tax returns by one or two percent by selecting funds with low distributions.

## **Coupon Resets Versus Poison Puts: The Valuation of Event Risk Provisions in Corporate Debt** (pp. 143-156)

Joseph A. Fields, David S. Kidwell, Linda S. Klein

This paper examines the valuation of the two major types of event risk indenture provisions, poison puts and coupon resets, on the debt of industrial companies. In contrast with earlier work by Crabbe (1991), we find that protection provided by poison put type of covenants is not valued by investors. The inclusion of coupon reset provisions, however, lowers the yield spread of new issued industrial bonds by 32 basis points. The yields on bonds with low credit quality ratings are reduced by including coupon reset provisions in the bond indentures.

## **A Practitioner's Perspective: Comments on "Asset Allocation, Life Expectancy and Shortfall"** (pp. 157-158)

Barbara S Poole