

yield to between 2.5% and 3%. A second small stretch would put you in a medium-term fund like **Vanguard Intermediate-Term Bond Market Index**, with roughly a 4% yield. If you don't need the income to live on, consider the U.S. Treasury's inflation-protected I Bonds ([publicdebt.treas.gov](http://publicdebt.treas.gov)), which pay deferred interest, lately at 4.66%; that's what I recommended to my aunt. Finally, a low-cost fixed—not variable—annuity from outfits like Vanguard, GE or Warren Buffett's Berk-

shire Hathaway ([brkdirect.com](http://brkdirect.com)) may make sense. Just be sure to read all the fine print; fixed annuities have some quirky tax and estate-planning wrinkles. At [brkdirect.com](http://brkdirect.com), for example, if you're 60 years old, roughly \$165,000 will buy you a single-premium immediate annuity guaranteeing \$1,000 in monthly pretax income for the rest of your life. Not a bad deal—and, with Buffett behind it, you don't have to worry that the insurer will go under before you do. **E**

## COPING WITH LOW YIELDS

My wife and I set up our retirement portfolio to produce enough income for us to live on. When interest rates started to plunge, we had to make some adjustments. Having a cash cushion helped **BY DAN FISHER**

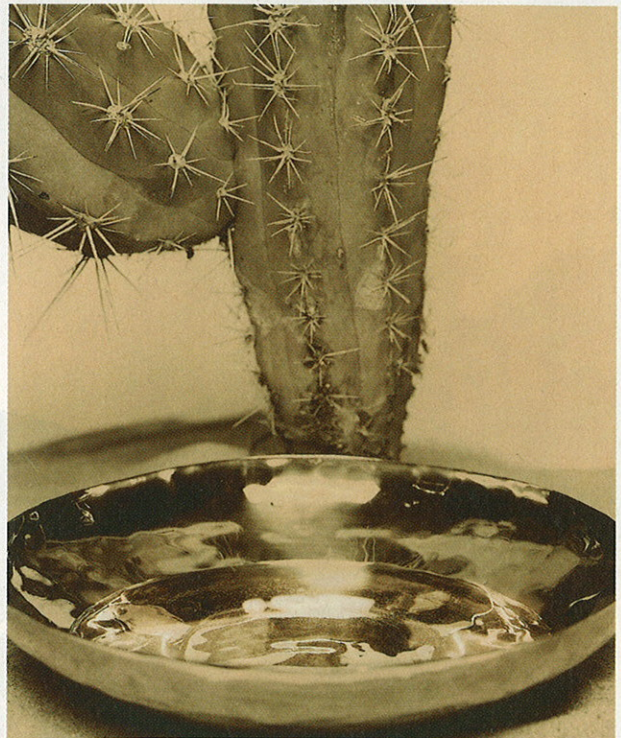
**MY WIFE CANDYCE** and I certainly didn't foresee the upheaval in financial markets that followed my early retirement in February 2001. We had built a portfolio of individual corporate and municipal bonds and income-oriented funds that promised to meet our estimated income needs. We hoped to leave two IRAs and some individual stocks to appreciate, untaxed, for as long as possible, and also kept a healthy cash reserve in a tax-free money-market account.

I was concerned, but not panicked, when the dividend from one of those income funds, **American High-Income Trust**, fell from 10.5¢ a share to 9.75¢, and then to 9¢ by April 2002. It turned out to be just the beginning. That fund payout has since dropped to 7¢ a share, and we've had two of our individual bonds called (redeemed by the issuer before maturity)—a corporate that was paying 8.1% and a muni that paid 5.5% tax-free. Another corporate, paying 7.5%, is likely to be called soon after you read this.

Working closely with our financial adviser, we've made a number of moves as a result. Last fall we sold some of our stocks and invested the proceeds in **Utilities SPDR**—an exchange-traded fund that holds S&P 500 utility stocks. Badly beaten down, they seemed to have growth potential, and they paid a 5% yield to boot. (They've gained about 18% this year.)

We invested the proceeds from one of the called bonds in **American Capital Income Builder**, an equity income fund that holds a combination of bonds and mostly dividend-paying stocks. Thanks in part to above-average dividend income from the stocks it owns, the fund has so far been able to keep the payout at around 5%.

This past spring we decided to increase our exposure to stocks and to diversify our bond fund holdings to boost our yield. So we sold all our shares of the **Intermediate Bond Fund of America**, which we considered a safe-harbor investment with very little volatility and a relatively low yield. We spread the proceeds among four funds: **Fremont Bond**, which holds high-quality bonds maturing in five to 15 years and yields about 3.3%; **Bond Fund of America**, which invests in slightly lower-quality bonds and has an estimated yield of 5.8%; **American High-Income Trust**, described above; and **American Balanced**, which has roughly equal stakes in stocks and bonds, and yields 2.5%. So far, the changes have achieved what we'd



hoped, adding to our portfolio value and giving us a small gain in income as well. They represent a more aggressive approach as we look for an improving economy in the months ahead.

Despite all those moves, we've still seen a nearly 7% drop in our anticipated interest and dividend income for the year, which is where our cash cushion has been so important. We've drawn down the balance in our tax-free money-market account to meet some expenses. Having this source of funds enables us to manage our portfolio on a more rational, long-term basis than if we constantly had to raid it to meet expenses.

We still believe the best investment philosophy for us is to keep a well-diversified portfolio and to avoid unnecessary turnover. However, this clearly continues to be an economic environment in which those of us living off such portfolios have little choice but to stay alert and nimble.