Northwestern Mutual
Retirement Strategy

Retirement Income Planning with Confidence

Official Retirement Planning Services Partner of the NCAA®

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Over the past decade, the conventional approach to retirement planning has shifted. Retirement planning used to focus exclusively on saving money to reach a “number” that’s enough to live on in retirement. However, as millions of baby boomers are reaching retirement age, they are faced with the challenge of what to do with the money they saved—to make it last a lifetime.

Retirement planning today is a lifelong, evolving journey.

It’s no longer just about accumulating a retirement nest egg, but also about having a plan that optimizes your retirement income to provide you with reliable income throughout your life, regardless of how long you live. This means the investment and savings strategies you used to accumulate wealth need to be adjusted as you prepare for and enter retirement.

As you prepare for retirement, it’s important to recognize and plan for not only the risk that your investments will not perform as expected, but the risk that your retirement may be longer (30-plus years) or more expensive than expected. This has led to a shift to expand retirement planning from a sole focus on investments to a broader, more comprehensive focus that includes solutions designed to optimize your income while managing both your personal and financial risks.

A Different Approach to Retirement Planning

Northwestern Mutual takes a different approach to retirement planning. Rather than simply looking at income needs, Northwestern Mutual comprehensively looks at your life circumstances—adapting to changes in your world as well as the world around you—to help you develop and achieve your retirement goals.

The Northwestern Mutual Retirement Strategy* is designed to help you achieve your goals through an offensive and defensive approach. This means providing you with a complete retirement plan—one that advises on how to optimize your income while managing risk, build and protect your retirement assets and draw a predictable income throughout your retirement years—that gives you confidence you can achieve your income goals over a lifetime.

Meeting Retirement Goals

A typical investment advisor may talk about the risks of the markets going up or down. We know you are most concerned with the risk of not meeting the goals you have set for the income you want during retirement and what you seek to leave to your family or charities when you die. Northwestern Mutual works with you to achieve your goals for your lifetime by addressing the six most important risks that could interfere with you achieving your retirement goals.

**Northwestern Mutual has a patent application pending on its new retirement allocation strategy planning tool.*

Managing the Risks that Can Impact Financial Security in Retirement

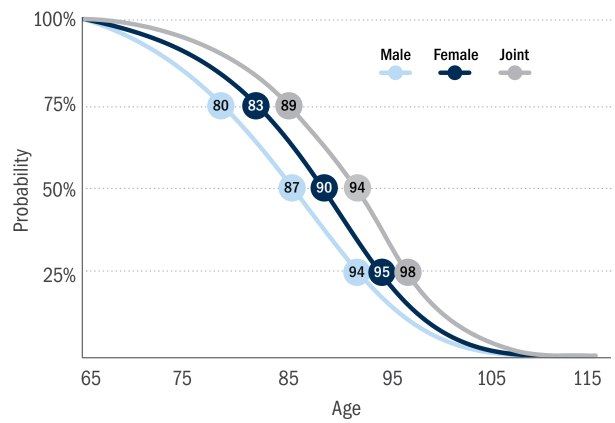
Recent events have taught us the downside of risk. A sound retirement strategy addresses the risks that can get in the way of your long-term financial security. Our strategy is designed to help you address:

1. Longevity

The average life expectancy is just that—an average. There is a significant possibility you will outlive this age and your money. As people live longer and potentially face health or employment reasons to retire early, it's critical to prepare for a longer retirement than you might expect and minimize the adverse impact to your retirement income.

As this life expectancy table shows, there is a 25 percent chance that a 65-year-old man will live to age 94, a 65-year-old woman to age 95 or at least one spouse of a 65-year-old couple to age 98.

PROBABILITY OF A 65-YEAR-OLD LIVING BEYOND VARIOUS AGES



Source: Annuity 2000 Table with mortality enhancements determined using projection scale G2

To effectively mitigate longevity risk, the Retirement Strategy was not built with a fixed life expectancy, unlike most financial plans. Instead, we studied the risks of living or dying at various ages so that your income plan succeeds with a high level of confidence no matter how long you live.[1]

2. Market

Participating in the stock market can give your retirement savings and income the potential to keep pace with inflation. However, investing in the stock market means taking the risk of market losses. Market declines in the early years of retirement can significantly reduce the amount of income you can obtain from your savings.

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In developing the Retirement Strategy we modeled the effects of various market conditions and developed solutions that succeed with a high level of confidence in a variety of market situations.

[1] Retirement Allocation Strategies are available that have been tested with a 90% degree of confidence and a 75% degree of confidence.

3. Inflation and Taxes

Both taxes and inflation can take a bite out of your retirement savings—inflation by reducing your purchasing power, and taxes by reducing your income and leaving you with less money to spend. Your retirement plan should include ways to protect your assets from inflation and tax risk by ensuring you have adequate income streams that include tax-efficient options.

The effects of inflation were modeled in our Monte Carlo simulation.[2] We examined economic scenarios with varying inflation rates to develop solutions designed to provide an amount of income that grows with inflation over time to maintain a constant amount of purchasing power during retirement.[3] We also tested the effect of taxes on different plans, to optimize after-tax income.[4]

IMPACT OF INFLATION ON YOUR RETIREMENT INCOME

Years	3%	4%	5%
0	$100,000	$100,000	$100,000
5	$86,000	$82,000	$78,000
15	$64,000	$56,000	$48,000
25	$48,000	$38,000	$30,000
30	$41,000	$31,000	$23,000

Over long time horizons, such as a 30-year retirement, inflation can significantly erode purchasing power. This table shows how inflation erodes the purchasing power of $100,000 over time using different inflation rates. For example, after 15 years at a 4% annual inflation rate, the purchasing power of $100,000 is reduced to $56,000.

4. Health Care Costs

Longer life expectancies, rapidly rising medical and prescription drug costs, fewer employer-sponsored retiree benefits and the limitations of Medicare make health care expenses a significant risk in retirement. It is important to obtain adequate health insurance if possible, to supplement Medicare, and to have sufficient resources to pay for these costs and other health-related expenses not covered by insurance.

Our Retirement Strategy takes into account research done by Ernst & Young regarding the use of health care services by retirees compared to the general population, and the fact that health care costs grow at a faster rate than costs for other services.[5]

ESTIMATED ANNUAL OUT-OF-POCKET HEALTH CARE EXPENSES IN RETIREMENT

65-year-old individuals on a per individual/per year basis

Health	Low	High
Very good - excellent	$3,000	$5,000
Fair - good	$5,000	$7,000
Poor	$7,000	$10,000

Estimates include the cost of premiums, deductibles and copays. They do not include long-term care costs. Based on data from the Centers for Medicare and Medicaid Services, assume an annual inflation rate of 6% for health care expenses.

Source: www.medicare.gov

[2] Monte Carlo is a problem-solving technique used to test the probability of outcomes by running repeated hypothetical simulations randomizing not only economic events such as inflation, investment returns or losses, but also the risks of living longer than expected. It's important to note that while Monte Carlo simulations can test the probability of outcomes, they are hypothetical, do not reflect actual investment results and are not guarantees of future results.

[3] Inflation was modeled as a factor of the one-year T-bill, where rates moved in a time series model (where results correlated year to year) with a mean reversion target. A health care inflation factor was added. In the 500 trials, the inflation rate could be as high as 20% in a given year.

[4] In determining after-tax income, we used tax rates that did not include the temporary reductions in tax rates passed by Congress by EGTRRA in 2001 and JGTRRA in 2003, as we assume that those reductions would expire as currently as scheduled in 2013.

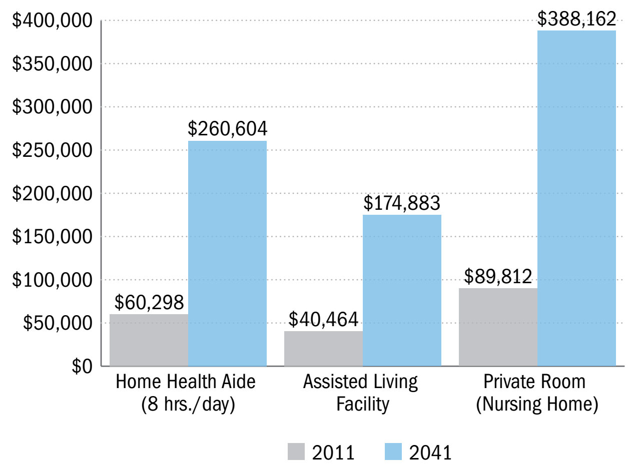
[5] Using the Consumer Expenditure reports put together by the Bureau of Labor Statistics for the years 2000-2004, E&Y constructed a retiree "basket of goods" and compared this to the basket used by the CPI for Urban consumers (CPI-U). The largest difference between the retiree basket of goods and the CPI-U basket was that much more weight was given to the medical component of the basket for retirees. The average rate of inflation for medical goods was roughly 4.35% over this period compared with an average CPI-U of roughly 2.55%.

5. Long-Term Care Needs

The cost of care for an unexpected or long-term illness not covered by private health insurance or Medicare could require you to prematurely deplete your retirement assets.

A survey of pre-retirees and retirees aged 55 to 75 found that health care and long-term care expenses together account for between 12 and 15 percent of retirement expenses, depending on the household income[6]. As shown in the chart, if long-term care costs increased five percent each year, an eight-hour-a-day home health aide who was paid $60,298 per year in 2011 would command $260,604 in 2041.

CURRENT VS. PROJECTED ANNUAL COST OF LTC (2011-2041)[7]



We examined the risks of long-term care events occurring during retirement and the costs of paying for those events. We studied solutions with and without funding for long-term care, with insurance or other assets, to determine which solutions delivered the most income at a high confidence level.

6. Leaving a Legacy

Experience has shown that, as people age, their desire to leave a financial legacy to loved ones or charities often grows. Without adequate planning you may not be able to meet your legacy goals. If you want to make an impact beyond your lifetime by leaving a financial legacy to loved ones or charity, you will need to balance that desire with the need to fund your retirement. However, with sound planning and the right mix of assets, it is possible to have a comfortable retirement and leave a legacy.

With sound planning and the right mix of assets, it is possible to have a comfortable retirement and leave a legacy.

While studying individuals' varying legacy goals, we looked at how those goals could be met while optimizing income in the most efficient manner—thus providing a solution that most closely matched the goal identified.[8]

By addressing these six key risks of retirement, you are taking a critical step toward achieving financial security in retirement.

[6] *"Retirement Income Trade-offs, Implications for Product Development," LIMRA, 2009.*

[7] *Illustrates a hypothetical situation. Costs will vary by state. Northwestern Long Term Care Cost of Care Survey, conducted nationwide, November 2011. Long Term Care Group, Inc. Future cost based on 5% annual increase. These future costs are not guaranteed.*

[8] *Retirement Allocations Strategies were developed for individuals and couples with no legacy goal at death, a goal to leave 25% of the value of retirement assets at death, 50% of the value of retirement assets at death and 100% of the value of retirement assets at death.*

A Sound Strategy For Success

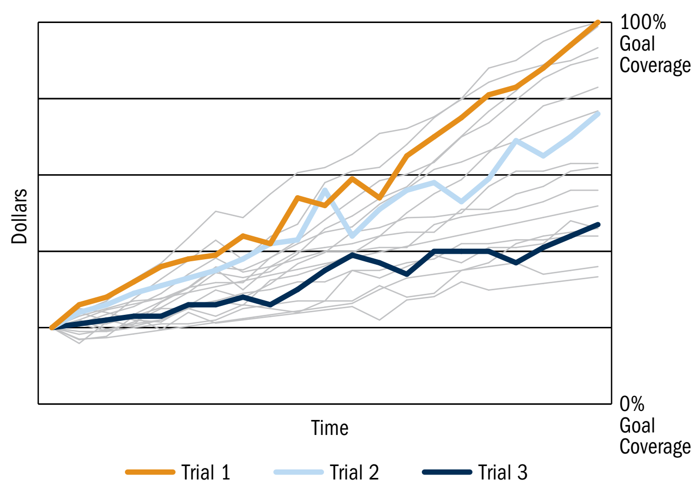
Conventional retirement planning, which is built on fixed assumptions for inflation and investment return rates, does not take into account the way the future may unfold. In today's environment, a more realistic and confident approach to retirement planning is needed—one that can provide more than a 50/50 chance of succeeding. That's why we developed and tested solutions that provide lifetime retirement income and meet your legacy goal with a 90 percent confidence level.[9]

Using Monte Carlo Simulation to Increase a Plan's Chance of Success

Today, financial planners commonly use Monte Carlo simulation to measure the risks of clients failing to meet their goals. Monte Carlo simulation is a problem-solving technique used to approximate the probability of certain outcomes by running multiple simulations, called trials, using random variables. Typically, Monte Carlo simulation trials are used to test a plan in a variety of market and economic scenarios—such as how a plan fares in times of high inflation or declining markets.

Recently, financial professionals have used Monte Carlo simulation as a research tool to determine the maximum amount of retirement income in real dollars that can be supported each year by someone's nest egg with a certain probability of success. This research has focused on risks such as market volatility and inflation for a retirement income plan.[10] However, it is critical to plan for not only the risk that your investments will not perform as expected, but also the risk that your retirement may be longer or more expensive than you expected.

Northwestern Mutual secured Ernst & Young (E&Y) to assist in developing our Retirement Strategy. Using their Monte Carlo tool, called Retirement Analytics™, we were able to randomize not only economic events such as inflation and investment returns or losses, but also the risks of living or dying during a given year, as well as the probability of having a long-term care event during retirement.



An example of Monte Carlo simulation with several trials is shown above—with each trial yielding a different level of goal coverage. The three highlighted trails show instances of a good, intermediate, and poor result; each of which is possible for the given plan depending on the economic conditions experienced. Viewing all trials together allows you to see the range of potential outcomes for this particular goal.

IMPORTANT: The projections or other information generated by the Monte Carlo simulation depicted in this graph regarding the likelihood of various outcomes are hypothetical in nature, do not reflect actual investment or life results and are not guarantees of future results. Results may vary with each use and over time. Other investments not considered may have characteristics that are similar to or superior to those being analyzed.

[9] *Northwestern Mutual tested Retirement Allocation Strategies with the Retirement Analytics Monte Carlo tool running 500 trials. A plan with a 90% confidence level means that in 90% of the trials (450), the plan met both goals of providing a specified amount of income over the lifetime of a hypothetical retiree and of meeting that retiree's assumed legacy objective. A 75% confidence level option is also available.*

[10] *E.g., David M. Blanchett and Brian C. Blanchett, "Data Dependence and Sustainable Real Withdrawal Rates."* Journal of Financial Planning *21, 9 (September 2008): 70–85; William Bengen,* Conserving Client Portfolios During Retirement. *Denver: FPA Press. (2006); Ameriks, John, Robert Veres, and Mark J. Warshawsky, "Making Retirement Income Last a Lifetime."* Journal of Financial Planning *14, 12 (December 2001): 60–76.*

Adding Value to Your Financial Plan

In developing the Northwestern Mutual Retirement Strategy, we reviewed published research and tested case studies[11] to determine whether certain products would add value to your financial plan. The following list shows the products we selected through our research:

- Investments
- Fixed and variable income annuities
- Fixed and variable deferred annuities
- Long-term care insurance
- Life insurance

Thousands of hypothetical plans were constructed and stress-tested to determine the maximum amount of income a plan could provide while meeting a certain probability of success.

For each type of product, we designed a hypothetical, industry-neutral product, taking into account the products offered by Northwestern Mutual and other companies in the industry. Using these hypothetical products, Ernst & Young built a complete set of hypothetical financial plans that represented almost every conceivable combination of investments and available products that an individual could use. Thousands of hypothetical financial plans were constructed and stress-tested to determine the maximum amount of income a plan could provide a retiree with a high probability of success. Out of the thousands of plans tested, we identified the top-performing plans to identify the solutions that provided the most income with a high degree of confidence.[12]

BEST CHOICE OF PLANS THAT OPTIMIZE YOUR RETIREMENT INCOME

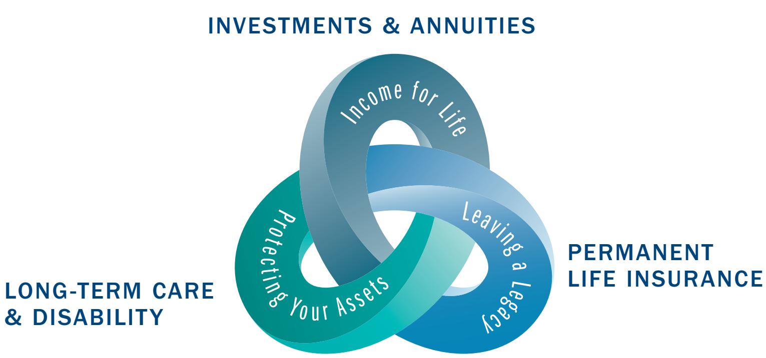
[11] *E.g.,* Lifetime Financial Advice: Human Capital, Asset Allocation, and Insurance, *Roger G. Ibbotson, Moshe A Milevesky, Peng Chen, Kevin X. Zhu, Chapter 4, at 50-52, Research Foundation of CFA Institute (2007) (research on utility of fixed and variable income plans).*

[12] *In the trials where the plans did not meet a 90% or 75% confidence level, it does not necessarily mean one would completely run out of funds. It could mean slightly less income must be lived on than hoped for, or that children or a charity will not be left as much money as desired.*

Achieving a Financially Secure Retirement

Northwestern Mutual's suite of solutions is uniquely positioned to address the range of needs and goals specific to your retirement picture. Our comprehensive planning approach includes tailored solutions designed to optimize your income while managing the key risks that could challenge your financial security. The result is a retirement strategy that is designed to build and protect your retirement assets, provide you with predictable income throughout your retirement years, and help you leave your desired financial legacy.

Leveraging tailored solutions makes sense—as no single product solution can meet every retirement need. Each component of the plan addresses a unique purpose, that when brought together achieves a powerful, statistically modeled strategy for success that can help provide the confidence needed to achieve your income goals.



Northwestern Mutual's comprehensive planning approach includes a suite of tailored solutions for optimizing your income while managing the key risks that could challenge your financial security.

Key Findings from Our Research

The development of the Northwestern Mutual Retirement Strategy and the solutions that support it unveiled some noteworthy elements:

Long-Term Care Funding Improves a Plan's Chances for Success

Long-term care funding, from other assets or insurance, is a way for you to prepare for the cost of care that an illness, physical or cognitive impairment, or the lasting impact of an accident can require.

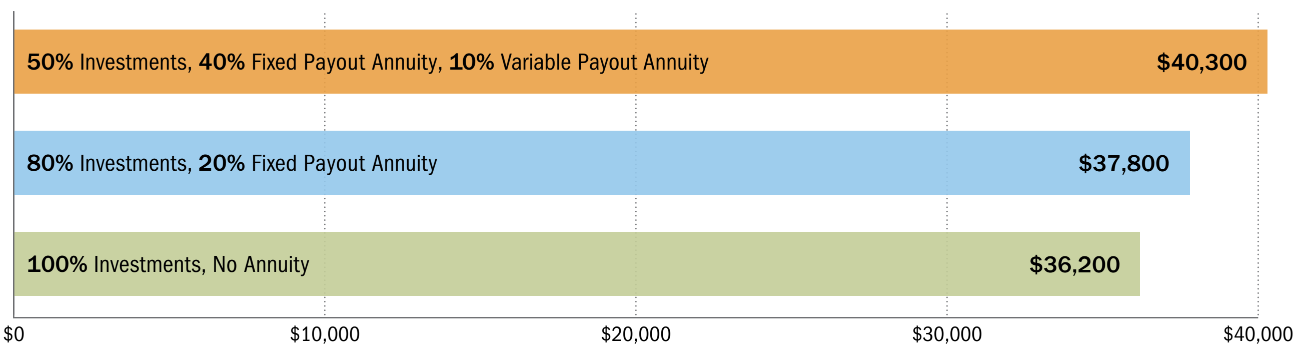
Considering your options early in life, while in good health, can help you protect against the unexpected need for care now and in the future. By including funding for long-term care in your retirement strategy, you reduce the need to deplete income and retirement savings, maintain control of your care decisions, reduce reliance on others and help ensure your ability to pay for services when you need them.

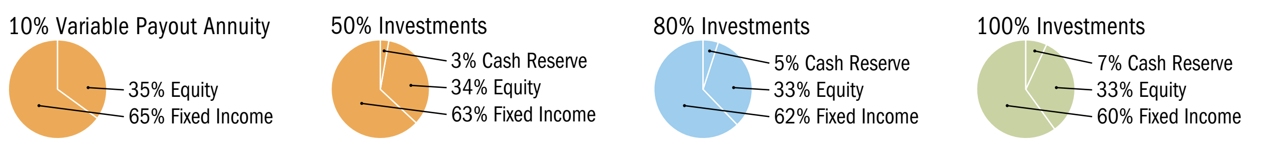
Adding Annuities Can Allow You to Spend More in Retirement with Confidence

Our research found that solutions with annuities added significantly to the amount of income that assets could generate with a high probability of success—with benefits still seen in a low-interest rate environment.

There is no market risk associated with fixed annuities, and the lifetime payout provides a base of income for as long as an individual lives. Using annuities also reduces your reliance on investment performance for income since down markets will have a lower impact on a portfolio with annuities, as less is being withdrawn. Lower withdrawals from investments allow for continued growth and tax deferral.

USING ANNUITIES AND INVESTMENTS—INCOME GENERATED FROM $1,000,000[13]





The income guarantees in annuities are backed solely by the claims-paying ability of the issuer. The chart shows three potential outcomes and does not represent all possible outcomes. The annuities shown here are immediate annuities that pay income for life but have no liquidity or surrender value.

The graph shown uses a scenario where a hypothetical male and female couple, both age 65, retires with $1,000,000 in retirement assets. It displays the amount of real, inflation-adjusted, before-tax income the couple could withdraw from their assets with a 90% confidence level for their lifetime for three different strategies using investments and annuities, based on the investment analysis tool output. If you were to use the retirement allocation strategy planning tool with a financial representative, you would receive additional options for implementing a plan with investments and annuities depending on the percentage of your assets that you wanted to annuitize. Each option has its own mix of fixed and variable immediate annuities representing the recommended optimal mix of the two products, depending on the amount you choose too annuitize. Clients with significantly higher or lower assets than $1,000,000 will receive different recommendations. The options shown here represent actual options available from the retirement allocation strategy planning tool. Please see the disclosures on the back page for additional information about this research.

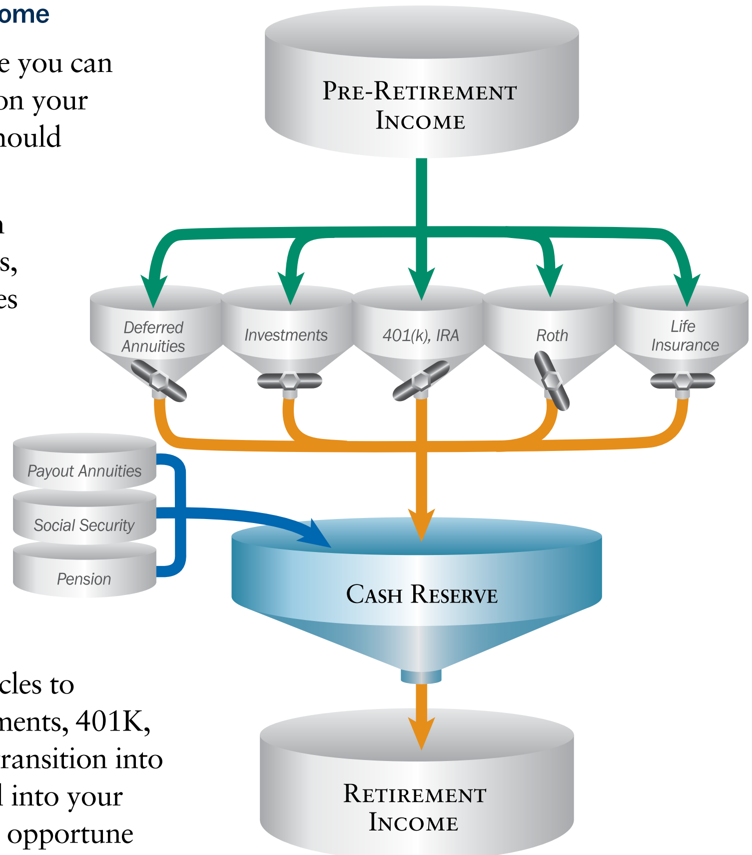
The fixed payout annuity is based on a joint life expectancy for annuitants both age 65, single premium immediate annuity lifetime income plan. Annuity income is based on the amount used to purchase the income plan, the age and gender of the annuitant, the income plan selected, and the rates in effect at the time of purchase. Annuity rates change frequently. For this hypothetical example, the pricing interest rate was assumed to be 3.75% based on 100% of the Annuity 2000 mortality table (no mortality improvements). An assumed load of 7% was used to reflect mortality improvements and expenses in order to bring the assumed rate in line with market rates.

The variable payout annuity purchase by the couple pays out a variable income stream for the joint lives of the annuitants. The funds annuitized are invested into funds in different asset classes, and the performance of those investments determines the income paid out over time. The annuity had an assumed interest rate of 3.5% (the benchmark rate the investments must earn for the annuity to have a level payout). Joint plans assume joint and survivor payout. Pricing was based on 100% of the Annuity 2000 mortality table (no mortality improvements), and mortality and expense charges were assumed to be 0.42% per year. We assumed that the funds invested in the annuity had annual expenses of 1% for equities and .65% for fixed income.

[13] *"Income" refers to real, inflation-adjusted, before-tax income that plan can support with 90% probability of success.*

Using a Cash Reserve Improves Sustainable Income

A cash reserve increases the amount of income you can spend with confidence.[14] If you plan to draw on your investment portfolio during retirement, you should maintain a cash reserve account.



A cash reserve is an account with cash or cash equivalents, funded by your retirement savings, which can be used to fund your living expenses each month. Its purpose is to provide you with the income you need to meet your living expenses while helping you avoid selling investments in a down market. The account should contain roughly two years' worth of living expenses that are funded by investments or variable income sources.

As you save money for retirement, you may use some or all of the following vehicles to accumulate wealth: deferred annuities, investments, 401K, IRA, Roth IRA and life insurance. Once you transition into retirement, your retirement savings can funnel into your cash reserve—from liquidating investments at opportune times, income-producing annuities, dividends and interest generated by investments, or from other income sources such as cash value life insurance, social security or a pension.

By establishing a cash reserve, you won't be as likely to have to sell your investments or withdraw from your other income sources at inopportune times, giving you a greater sense of security. Plus, you can be better positioned to more efficiently make withdrawals for your retirement income needs and have better control over income taxes.

Summary

Achieving financial security in retirement requires a strategy that preserves and continues to manage your wealth, mitigates the risks that can affect your retirement years and provides you with predictable and steady income for life. It's something that can be achieved with confidence when a plan has the right combination of tailored solutions to optimize your income while managing both your personal and financial risks.

[14] *For example, Harold Evensky, a nationally recognized thought leader in financial planning, uses a cash reserve with his clients and has published research demonstrating the utility of such an approach. Harold Evensky, "Withdrawal Strategies, A Cash Flow Solution," Chapter 11 of Harold Evensky and Deena Katz, eds.,* Retirement Income Redesigned: Master Plans for Distribution: An Adviser's Guide for Funding Boomers' Best Years *(2006).*

Information About the “Using Annuities and Investments—Income Generated from $1,000,000” Graph on Page 10

IMPORTANT: The projections or other information generated by the Monte Carlo simulation depicted in this graph regarding the likelihood of various outcomes are hypothetical in nature, do not reflect actual investment or life results and are not guarantees of future results. Results may vary with each use and over time. Other investments not considered may have characteristics that are similar to or superior to those being analyzed.

The amounts displayed are the maximum amount of real, inflation-adjusted, before-tax income that a hypothetical 65-year-old male and female couple could spend in their lifetime if they retired at age 65 with a 90% confidence level, using Monte Carlo simulation. Monte Carlo simulation is a problem-solving technique used to test the probability of outcomes by running repeated hypothetical scenarios randomizing the occurrence of different events. For our hypothetical couple, we randomized in 500 trials the following variables: market volatility, inflation, and the probability of death or longevity. A 90% confidence level means success in 450 out of 500 trials. If both members of the couple die while having been able to sustain the amount of income tested, then the trial is a success. If the couple does not have sufficient assets to sustain the amount of income tested during the trial for both of their simulated lifetimes, the trial is a failure.

The following was assumed: 1) for market volatility and inflation, equities would have an expected return of 7.4% and the standard deviation for equities (aka stocks) would be 17%, 2) fixed income would have an expected return of 4.8% and a standard deviation of 3.9%, 3) the beginning interest rate for cash was .6% randomized at that rate each year, with the rate in one year related to the previous year’s rate with a tendency to move toward a historical average rate of 4.75%.

Expected return is based on the appreciation/depreciation of a hypothetical portfolio expressed as a percentage per year. Values are based on combination of capital market return assumptions for certain asset classes and assume the same asset mix is held throughout the entire period. These hypothetical estimates are not meant to forecast the performance of a particular fund or security and do not guarantee future results.

Standard deviation is a statistical measure of the degree to which an individual value in a probability distribution tends to vary from the mean of the distribution. Higher standard deviation numbers indicate higher volatility and greater risk. Standard deviation assumes a normal bell curve-shaped distribution of outcomes. Experience has shown that not all returns or losses fall within the pattern predicted by a normal distribution. Standard deviation does not capture the risk of large short-term declines in value such as market losses that occurred in 2008-2009.

We assumed that the returns of stocks and bonds did not perfectly correlate, and that this lack of correlation reduced the overall volatility of the portfolio over time. We assumed that all investments were in mutual funds, and that mutual funds had annual expenses of 1% for stocks and .7% for bonds and .34% for cash.

We assumed an average base inflation rate of 2.4%. We randomized the base inflation rate each year assuming that inflation would move up and down in similar patterns to how it has fluctuated in the past. After a base inflation rate was calculated, a medical inflation factor of .32% was added for retirees at or below age 75 and of .44% for retirees age 76 and above. This means that if a trial began with a hypothetical retiree being age 65, inflation would be adjusted by .32% upward until, if the retiree was still living at age 76, an upward adjustment of .44% would be made for the rest of the retiree’s lifetime.

Mortality events were simulated using the probabilities from the Annuity 2000 mortality table with mortality improvements based upon Projection scale G2 as documented in a slide presentation titled “Update on Development of New Mortality Tables,” by Mary Bahna-Nolan, Chair, Society of Actuaries and American Academy of Actuaries Project Oversight Group, and Chair of Academy Life Experience Subcommittee, presented to NAIC Life Actuarial Task Force Meeting, March 24, 2011.

Asset Class Risks: *Equities*—Although stocks have historically outperformed bonds, they also have historically been more volatile. You should carefully consider your ability to invest during volatile periods in the market. *Fixed Income*—High yield bonds present greater credit risk than bonds of higher quality. Bond prices correlate inversely with interest rates, and this effect is usually more pronounced for longer-term bonds, making their prices more volatile.

Limitations: Your assets may not be adequately diversified, which could affect the validity of the simulation process described above when applied to your actual circumstances. The simulation does not distinguish between different holdings within an asset class but assumes that any holdings within an asset class are representative of the asset class as a whole. The inflation rate forecast considers consumer prices in the US economy generally as well as an adjustment for medical expenses. To the extent that your future spending differs from the basket of goods and services used in this general inflation forecast, your actual experience with inflation may vary. The simulation assumes that you purchased investment or insurance products that have the expenses pricing and features described. If you purchase products that have materially different pricing or features from those described, then you cannot use the confidence level projections made in this graph.

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