THE PROCESS OF MANAGING RETIREMENT INCOME

THE VALUE OF DIVIDENDS IN RETIREMENT

A cow for her milk. A hen for her eggs,
And a stock, by heck, for her dividends.
An orchard for fruit. Bees for their honey,
And stocks, besides, for their dividends.

\- John Burr Williams,
"Evaluation of the Rule of Present Worth," 1937

The road of retirement should be paved with more than good intentions. Soon-to-be retirees need to develop and follow a retirement income plan that balances current lifestyle and long-term sustainability of the retirement portfolio. The *Road of Retirement* series provides some best practices for accomplishing this balance.

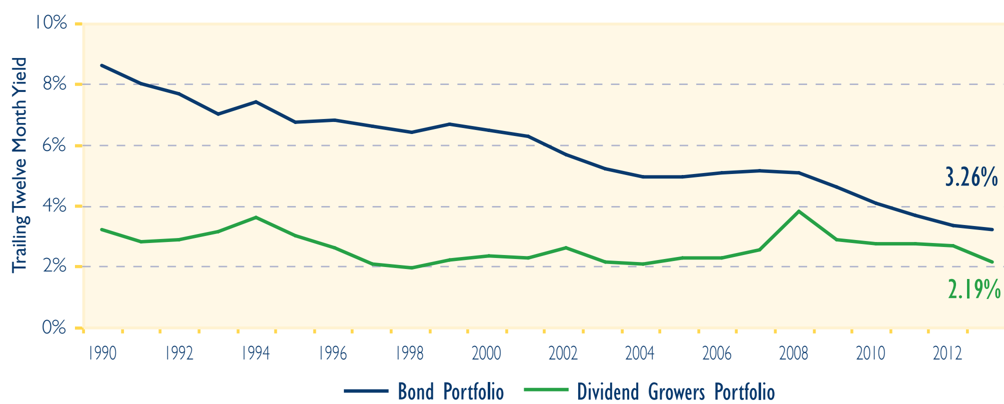
Over the past eighty-seven years, dividends have accounted for over 40% of the total return for the S&P 500 Index. The importance of dividends has been an often overlooked part of investing, but will continue to come to the forefront as baby boomers prepare for retirement and look for high and growing income-generating investments.

There are generally two schools of thought regarding how best to fund expenses in retirement. There are many who believe a total return approach is optimal, whereby an asset allocation and total return is targeted for the portfolio and a portion of the retirement assets is sold periodically to cover expenses. While this approach attempts to provide the growth that retirees need to outpace the effects of inflation, they may also be forced to sell assets at an inopportune time.

The second school of thought follows a high-income approach, whereby the portfolio is comprised of high-yielding income investments in an attempt to generate sufficient current income to cover expenses. This approach can leave a retiree too heavily exposed to fixed income investments and the ravages of inflation.

In this paper, we will explore a third approach, which is a hybrid of the total return and high-income approaches. We will explore how an investment in stocks of companies that provide both high and growing dividend income can benefit a retirement portfolio undergoing the duress of withdrawals. This type of investment strategy can have the potential to provide a growing dividend income stream as well as capital appreciation needed by retirees.

FIGURE 1. BOND YIELDS VERSUS DIVIDEND YIELDS
Calendar Year Yields



Dividends were not reinvested.
Data through December 31, 2013.
We've assumed that the hypothetical Dividend Growers Portfolio performed similarly to the S&P Dividend Aristocrats Index and the Bond Portfolio performed similarly to the Barclays U. S. Aggregate Bond Index. You may not invest directly in an index.

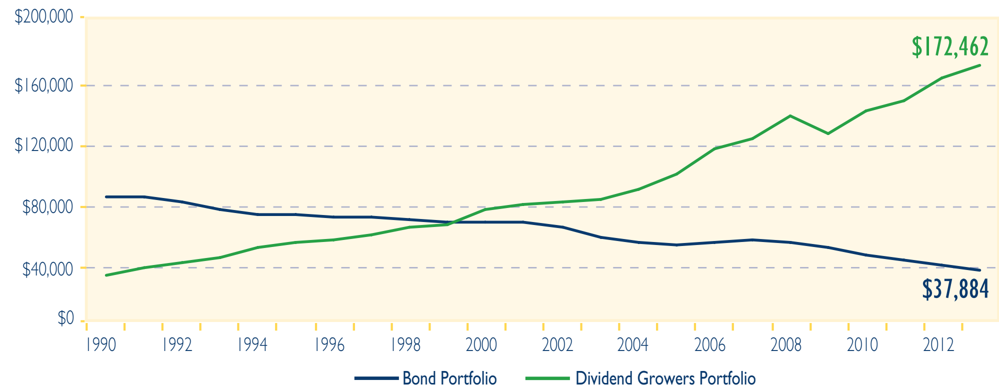
Past performance does not guarantee future results.

Sources: Barclays and Standard and Poor's.

Understanding Yield

When reviewing income-generating alternatives, retirees often focus on current yield (the current income divided by the current price). This works well for fixed income investments, which are, essentially, contracts that pay a certain level of income to the bond holder each year and then return the principal amount at maturity. However, for equity investments, where both the income and stock price may appreciate, looking solely at current yield can disguise the growth in the actual dollar amount of the income generated.

FIGURE 2. BOND INCOME VERSUS DIVIDEND INCOME
Annual Income from a Hypothetical $1 Million Investment Made in January 1990



Data through December 31, 2013
Dividends were not reinvested.
We've assumed that the hypothetical Dividend Growers Portfolio performed similarly to the S&P 500 Dividend Aristocrats Index and the Bond Portfolio performed similarly to the Barclays U. S. Aggregate Bond Index.
You may not invest directly in an index.
Past performance does not guarantee future results.
Sources: Barclays and Standard and Poor's.

To illustrate this point, ***figure one***, on the prior page, shows a comparison of bond yields versus equity yields over calendar years. At first glance, it is obvious that current yields on bonds are higher, but this higher yield comes with little to no potential for growth.

To show the difference between the growth of income provided from bonds versus a dividend-paying equity investment, in ***figure two***, we calculated the amount of income generated annually on a hypothetical $1 million investment made in 1990. While the income from the bond investment steadily declined from 1990 to 2013, the amount of dividend income derived from the dividend-focused equity allocation grew fairly steadily. Although beginning at a relatively modest level compared to the bond investment, the dollar amount of dividend income generated surpassed the bond income in approximately 10 years and ended at 355% of the bond income by 2013. For this example, it was assumed that the dividends were being used to support expenses and not being reinvested.

Total Return for Dividend Growers

Our analysis assumes that the hypothetical Dividend Growers portfolio performed similarly to the S&P 500 Dividend Aristocrats Index, a subset of the S&P 500 Index. It is comprised of U.S. companies that have consistently increased their dividends for the past twenty-five years. Since the Dividend Aristocrats Index began in January 1990, we can compare its returns versus the S&P 500 Index for the period beginning January 1, 1990 to December 31, 2013, to determine its performance in a dividend focused retirement portfolio, from a total return perspective. For the results, see ***figure three***.

What becomes apparent is that the total return for the Dividend Aristocrats Index of 12.09%, as compared to the return for the S&P 500 Index of 9.45% is very attractive.

This test period included some very different investment environments, including the banking and real estate crisis of the early 1990's, the "internet bubble" in the mid- to late-1990's, that culminated with the 2000–02 bear market, and the maelstrom in the financial markets that began in late 2007. To determine how the hypothetical Dividend Growers portfolio performed during these difficult market scenarios, the twenty-four-year period was segmented into five-year periods, 2010, 2011, 2012 and 2013 as stand alone calendar years, and finally the twenty-four year period in its entirety.

As the analysis in ***figure four*** (on the next page) illustrates the hypothetical Dividend Growers portfolio, as represented by the Dividend Aristocrats Index, outperformed in three of the four five-year periods. It only underperformed during 1995–1999, when investors were infatuated with high-growth stocks that fueled the internet bubble and lead to the 2000–02 bear market. While the Dividend Growers didn't keep pace during this period of "irrational exuberance," they produced an attractive total return of 19.48%.

Dividend Income in Retirement

To illustrate how a dividend grower-strategy can be used to fund a retiree's expenses, ***figure five*** assumes a hypothetical $1 million retirement account invested in January 1990 in a portfolio that performed similarly to the S&P 500 Dividend Aris-

FIGURE 3. DIVIDEND ARISTOCRATS INDEX VERSUS S&P 500 INDEX

	Dividend Aristocrats Index	S&P 500 Index
Income Return	3.11%	2.31%
Price Return	8.98%	7.13%
Total Return	12.09%	9.45%

Dividends were reinvested.
Data from January 1, 1990 through December 31, 2013, annualized.
Past performance does not guarantee future results.

tocrats Index. To calculate the retiree's spending, we assume that 5% or $50,000 will be needed to cover pre-tax expenses in the first year of retirement and then increase that amount annually by a 3% cost-of-living adjustment to cover inflation. For the early years in retirement, when dividends don't fully support the spending, the retiree will redeem a portion of the investment to cover the shortfall. For the later years, the dividend income, beyond what is needed for spending, was reinvested in the portfolio.

In this hypothetical, the Dividend Growers Portfolio generated sufficient dividend income to cover 100% of the retiree's spending after seven years. Once this 100% coverage was achieved, it never fell below that level and generated excess dividends that could be reinvested into the portfolio. As summarized in the table below the graph in ***figure five***, the initial $1 million investment produced $2.19 million in dividends of which $1.72 million was spent and $466,702 reinvested. The portfolio value, as of December 31, 2013, was $7.78 million.

For most retirees, developing a growing dividend income stream should be an attractive alternative to the total return or high-income approaches described earlier. Having the retirement portfolio generate sufficient income to cover expenses while the portfolio is poised with an opportunity for continued growth should be a goal for every retiree.

Best Practices

Before implementing a dividend-grower strategy, there are two improvements that should enhance the portfolio's diversification and selection of attractive dividend opportunities. First, looking for companies around the globe that offer both a high and growing dividend, versus limiting the investment universe to just domestic stocks, may improve results. As seen in ***figure six***, dividend yields outside the United States, on average, have a tendency to be more attractive, given that culturally dividend growth is seen as a sign of financial strength.

Another benefit from using a global approach is the opportunity to improve the portfolio diversification by industry sector. In the United States, attractive dividends are typically concentrated in real estate and utilities. Outside the United States, dividend opportunities exist in a multitude of sectors, as shown in ***figure seven***, on the next page.

The second improvement when implementing this dividend growers strategy would be to use an active investment management team that chooses investment opportunities based upon fundamental research. The decline of dividends for U.S. companies in the S&P 500 Index during 2008–09 has

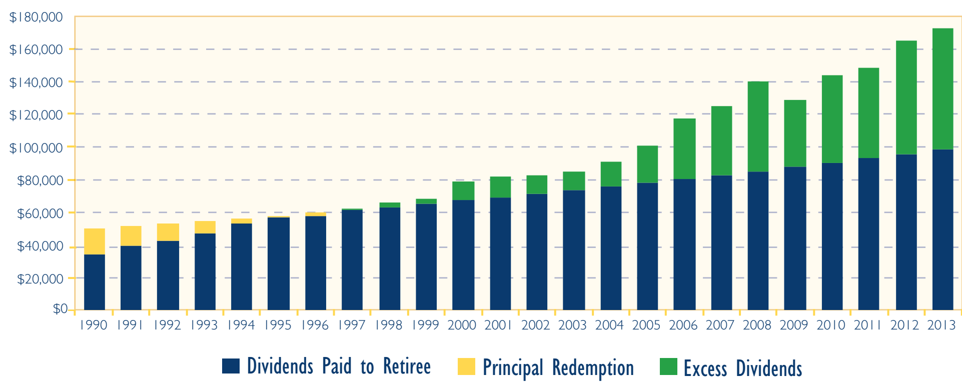
FIGURE 4. DIVIDEND ARISTOCRATS INDEX VERSUS S&P 500 INDEX

Period	Dividend Aristocrats Index	S&P 500 Index
1990–1994	11.13%	8.69%
1995–1999	19.48%	28.54%
2000–2004	9.74%	-2.29%
2005–2009	3.32%	0.41%
2010	19.35%	15.05%
2011	8.33%	2.11%
2012	16.89%	15.96%
2013	32.27%	32.39%
1990-2013	12.09%	9.45%

Reflects reinvestment of dividends.
Data through December 31, 2013, annualized.

Past performance does not guarantee future results.

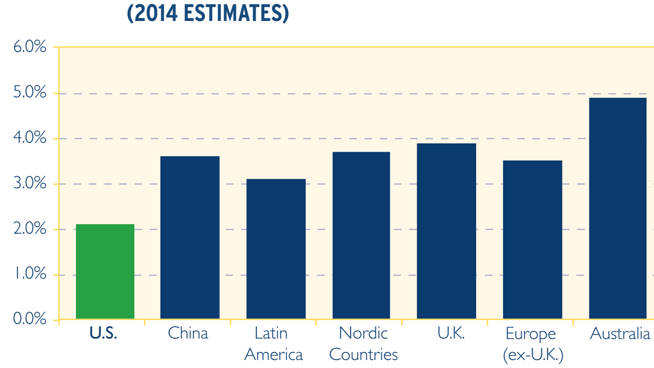
FIGURE 5. DIVIDENDS FOR RETIREMENT
Income from the Hypothetical Dividend Growers Portfolio



Dividends Earned	Amount Spent	Net Reinvested	Ending Portfolio Value
$2,188,025	$1,721,324	$466,702	$7,784,317

We've assumed that the hypothetical Dividend Growers Portfolio performed similarly to the S&P 500 Dividend Aristocrats Index.
You may not invest directly in an index.
Past performance does not guarantee future results. Source: Standard and Poor's

FIGURE 6. DIVIDEND YIELD BY COUNTRY
(2014 ESTIMATES)



Past performance does not guarantee future results.
Sources: MSCI indices sourced via Bloomberg as of 12/31/2013.

FIGURE 7. GLOBAL DIVIDEND YIELD BY SECTOR (2014 DIVIDEND YIELD ESTIMATES)

Sectors	U.S.	Europe ex UK	U.K.	Australia	Nordic Countries	EM Latin America	China
Telecommunications	4.5%	5.2%	4.3%	5.7%	5.8%	2.4%	3.9%
Utilities	4.0%	5.4%	5.6%	5.5%	5.7%	5.4%	2.5%
Consumer Staples	2.8%	2.9%	3.8%	4.7%	2.9%	2.6%	1.9%
Health Care	1.7%	2.9%	4.4%	2.6%	2.4%	1.3%	1.7%
Industrials	2.0%	3.1%	2.6%	4.2%	3.3%	2.0%	2.5%
Energy	2.2%	5.2%	4.4%	4.4%	5.5%	4.4%	4.1%
Materials	2.1%	2.9%	3.5%	3.8%	3.9%	2.7%	2.4%
Financials	2.1%	4.0%	4.1%	5.6%	4.4%	3.7%	5.0%
Consumer Discretionary	1.4%	2.9%	2.9%	3.6%	3.9%	1.8%	2.1%
Information Technology	1.7%	1.8%	1.1%	3.0%	2.5%	3.8%	0.7%
Market Average	**2.1%**	**3.5%**	**3.9%**	**4.9%**	**3.7%**	**3.1%**	**3.6%**

Best opportunities.

Past performance does not guarantee future results.

Sources: MSCI indices sources via Bloomberg as of 12/31/13.

made the headlines recently, and even the Dividend Growers were not immune. It is important to use an active manager who can analyze both a company's willingness and ability to pay a high and growing dividend as a way to try and navigate around some of the dividend declines seen in the broader market.

As the baby boomer generation progresses on the road of retirement, a dividend-grower strategy may be a prudent addition to their equity portfolios, as part of a core investment strategy. Not only can growing dividends help contribute to the retiree's distributions, but the portfolio value may also have the ability to outpace inflation through price appreciation.

Following this strategy does not guarantee sustainability of a retirement portfolio or better performance, nor does it protect against investment losses.

Bonds are debt investments in which an investor loans money to an entity (corporate or governmental) which borrows the funds for a defined period of time at a fixed interest rate. Bonds are subject to certain risks, including interest-rate risk, credit risk, and inflation risk. The principal value of bonds will fluctuate relative to changes in interest rates, decreasing when interest rates rise.

A stock (equity) is a share in the ownership of a company. As an owner, investors have a claim on the assets and earnings of a company, and in some cases, voting rights with the shares. Historically, stock investors have been subject to a greater risk of loss of principal compared to bond investors. However, both stock and bond prices will fluctuate, and there is no guarantee against losses. There is no guarantee a dividend-paying stock will continue to pay dividends.

Dividends and gains on investments in either stocks or bonds may be subject to federal, state, or local income taxes as well as the alternative minimum tax. Investments in stocks and bonds are not FDIC insured, nor are they deposits of or guaranteed by a bank or any other entity. Dividends are not guaranteed.

Investing outside the United States, especially in emerging markets, entails special risks, such as currency fluctuations, illiquidity, and volatility.

Sponsored by Thornburg Investment Management, 2300 North Ridgetop Road, Santa Fe, New Mexico 87506

Before investing, carefully consider the investment goals, risks, charges, and expenses. For a prospectus or summary prospectus containing this and other information, contact your financial advisor. Read them carefully before investing.

Thornburg Funds are distributed by Thornburg Securities Corporation.

The views expressed in this article are subject to change.

Diversification does not assure or guarantee better performance and cannot eliminate the risk of investment losses.

The S&P 500 Dividend Aristocrats Index is equally weighted and measures the performance of large cap, blue chip companies within the S&P 500 Index that have followed a policy of increasing dividends every year for at least 25 consecutive years.

The S&P 500 Index is an unmanaged broad measure of the U.S. stock market.

The Barclays U.S. Aggregate Bond Index is composed of approximately 8,000 publicly traded bonds including U.S. government, mortgage backed, corporate and Yankee bonds. The index is weighted by the market value of the bonds included in the index.

MSCI Country Indices (U.S., Australia, U.K., and China) – Free float-adjusted market capitalization indices that are designed to measure equity market performance in that specific country.

MSCI Europe ex-U.K. Index – A free float-adjusted market capitalization index that is designed to measure developed market equity performance in Europe. The MSCI Europe ex-U.K. Index consists of the following 14 developed market country indices: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden, and Switzerland.

MSCI EM (Emerging Markets) Latin America Index – A free float-adjusted market capitalization index that is designed to measure equity market performance in Latin America. The MSCI EM Latin America Index consisted of the following 5 emerging market country indices: Argentina, Brazil, Chile, Mexico, and Peru.

MSCI Nordic Countries Index – A free float-adjusted market capitalization weighted index that is designed to measure equity market performance in the Nordic region. The index consists of the following 4 countries: Denmark, Finland, Norway, and Sweden.

The performance of any index is not indicative of the performance of any particular investment. Unless otherwise noted, index returns reflect the reinvestment of income dividends and capital gains, if any, but do not reflect fees, brokerage commissions or other expenses of investing. Investors may not make direct investments into any index.