Understanding Traditional Retirement Investments In Today's Economy

In our most recent article, we explored the traditional 4% rule that has been used for decades as a rule of thumb for the age-old question: how much can I take from my investments without running out of money in retirement? Unfortunately, with more recent history, this rule may leave as much as a 50% chance of failure rate, perhaps even more given the uncertainties of market returns.

Even though the 4% rule is not guaranteed and may leave considerable risk of failure, many people still focus on it based on the yields they expect from their investments. When they arrive at retirement and realize that they will run out of money much faster than anticipated if they don't withdraw less than the 4% they had expected, it may be too late to do anything about it. If you want to withdraw 4%, or even more than that, you may need to invest differently than what you have been taught in the past.

Will Bonds Work for You?

The Federal Reserve has continued to delay any material increases in the interest rate in recent years, and any further changes are expected to be slow and gradual from most recent statements from the Federal Open Market Committee.[1] While it is possible that the rates seen on bonds will improve over time, it may not be a wise choice to base your retirement plan on something that may or may not happen, especially when the evidence does not support the idea.

While bonds may serve their place as part of an asset allocation that is focused on insulating a retiree from the market volatility of equities, low interest rates make finding yields that can provide for retirement income as they did in generations past difficult to do in today's market. Instead of holding onto bonds and hoping, some retirees may be choosing other options through which they can feel more secure and see higher rates of return.

Turning to the Stock Market

With lower interest rates and yields from fixed income, many retirees are leaning on equities in search of returns in today's market. That may leave many unknowingly exposed to significant losses and a higher level of risk than may be anticipated. While stocks may have their role in a retirement portfolio, retirees may wish to use them with care. Otherwise, they could be exposed to significant losses early in retirement as they are drawing income that may severely jeopardize the longevity of their assets, as was demonstrated both in the early 2000s and in 2008, when the stock market faced significant challenges.

It is critical that market exposure be appropriately positioned in a retirement portfolio so that you are not relying on more volatile investments to produce consistent income. Rather, you may consider a portion of your savings earmarked for a longer time horizon to serve as an inflation hedge or for legacy planning, but that is not needed to generate a regular paycheck and should not be exposed to this volatility. It is important to assess your risk tolerance and exposure throughout the years as your needs continue to evolve.

Next time, in part three of this series, we will explore options outside of the market you may consider as part of a comprehensive income plan today. Contact us today to request our latest white paper, "Destination: Retirement – Why the 4% Rule May Not Get You There." To discuss your investment challenges and retirement goals, schedule a complimentary consultation today. Give us a call at (256) 715-0094!

[1] https://www.federalreserve.gov/monetarypolicy/files/monetary20160727a1.pdf