Steward Advisors

In Brief

A Brief Review of Financial Best Practices

Portfolio Withdrawal Strategies

Preparing for and enjoying retirement should be an exciting time for Americans. Oftentimes, though, there is a level of anxiety involved as retirement age looms…wondering "Will we have enough?" or "What can we spend per month so it doesn't run out?"

If you will be retiring off an investment portfolio you'll need to maintain a level of spending that matches the portfolio. There is a lot of research regarding withdrawal strategies. To sum it up, there are basically 4 different withdrawal strategies that most people use:

1) A constant dollar withdrawal (adjusted for inflation)

2) Withdrawing a constant percentage of an investment portfolio

3) Using a formula similar to the IRS required minimum distribution formula for IRA withdrawals (an increasing percentage of the portfolio is withdrawn each year)

4) A rules based strategy such as only increasing withdrawals in years when the portfolio grows.

The challenge with all of these strategies is that the planning is usually done once at retirement (or irregularly during retirement) and there is no way to anticipate all of the changing variables that will affect a retirement portfolio.

Some of the moving targets include life expectancy, investment returns, inflation, and changing health (and related costs). On average, a couple retiring at age 65 can expect at least one person to live to 92.

Anyone's estimates of investment returns, inflation and medical expenses will be wrong for a nearly 30 year planning horizon.

Plan Your Lifestyle & Expenses (As Best You Can)

Moreover, setting a constant or nearly constant annual withdrawal amount ignores the impact of lumpy expenses, other income sources which may or may not be permanent and the desire for many people to leave a bequest to loved ones and/or a charity.

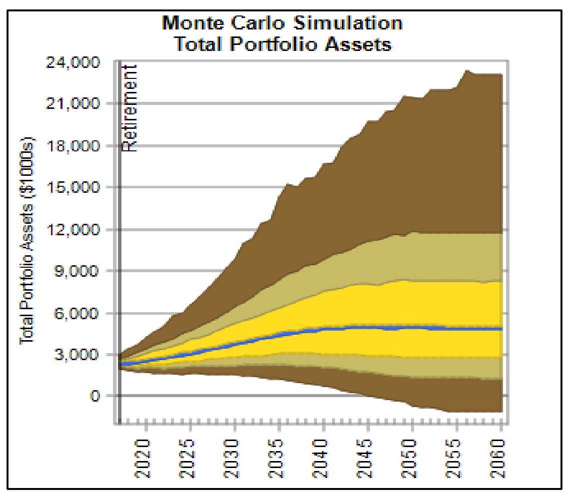
The retirement income planning puzzle quickly becomes very complex. To deal with this complexity, we've found a few best practices to help guide our clients.

First, we project cash flows for clients which take into account lumpy expenses like the 75th birthday cruise you've always wanted to take. These cash flow projections also consider outside income such as Social Security, inheritances or real estate sales

Second, we run multiple scenarios changing variables such as investment returns, inflation, and life expectancy.

Third, we target investment withdrawal levels that will only have to be adjusted about 10-20% of the time. Our preference is to work with clients to get the odds of needing to adjust spending close to 10% at the beginning of retirement, but we will identify how much risk is in the plan on the front end.

Fourth, we update the cash flow plan regularly and identify changes that need to be made early enough so that clients have good options.



Monte Carlo simulation is a computerized mathematical technique that allows us to show our clients all possible outcomes of any decisions to help us assess the impact of risk.

Because our planning process anticipates that markets can drop like they have in the past week, we don't have to tell clients to change their plans with every market fluctuation. In fact, more often our conversations with clients involve reassuring them that their plans are on track or that they can increase their spending as time passes. In summary, plan and withdrawal as best you can and you can live your dream retirement.

To learn more about our Portfolio Withdrawal Strategies call Tim Obendorf at 630-537-0111 or email: Tim@StewardAdvisors.com.