



Four Retirement Income Withdrawal Methods

How much should you withdraw from your tax-deferred 401(k) or IRA, and in what form? Here's a brief summary of four retirement income withdrawal methods to help you optimize the decumulation of your retirement income portfolio prudently.

Goals, Obstacles, And Taxes

Your strategy must annually balance withdrawing enough to live comfortably against making your assets last a lifetime. Taxes are a material consideration, since traditional IRA, 401(k) and 403(b) accounts are taxed as ordinary income.

Withdrawals before age 59½ are subject to a 10% early withdrawal penalty. In addition, you must start withdrawing from federally qualified retirement accounts when you reach age 70½. However, under provisions of the SECURE Act, which became law at the end of 2019, the required minimum withdrawal age was pushed back to 72 starting 1/1/2020. An extra 18 months of tax-deferred growth at your age is a nice unexpected bonus.

To minimize taxes on withdrawals, consider paying tax on these assets now and placing them in Roth IRAs, where you pay taxes up front instead of when you're retired. The four methods are:

Bucket Approach

You divide your retirement assets into three separate accounts. The three buckets allow you to set aside a segment of your investments to grow, while having the assurance of a steady income stream.

Your first bucket is in cash, meaning short-term instruments. Replenishing the cash bucket with

earnings generated by the other two buckets enables a quantitative discipline like dollar-cost-averaging.

It's currently not uncommon for these short-term accounts to pay 1.8% to 2.4% annually. A minimum deposit of \$5,000 or so is commonly required. Expect to fractionally beat inflation annually, and do not expect capital appreciation. Read the prospectus, of course, or call us.

In all, you allocate three to five years' worth of living expenses, around 20% of your investments in cash, to the first bucket. The second bucket contains fixed-income assets, most often bonds or bond mutual funds and yield interest income.

The third bucket is for stocks. This remains the growth component of your portfolio, as stocks tend to grow the most over the long-term. They get socked the worst during recessions, too, which is why they aren't subject to the near-term withdrawal with the bucket strategy, which would sap your financial security over time.

4% Method

The 4% annual withdrawal method aims to preserve your wealth yet throw off enough to live on. You simply withdraw 4% of your investments annually to start, and, thereafter, annually adjust it for inflation. The 4% method over 30-years is a prudent way to manage the risk of outliving your money. With this withdrawal scheme, and a \$1 million retirement account, you would withdraw \$40,000 the first year, \$40,800 in year No. 2, and \$41,616 in year three, assuming a 2% inflation rate.

How Worldwide Demographics Affect Your Portfolio

While China, Japan, Germany, and other major economies are grappling with a decline in their working-age population in the decades ahead, the U.S. working-age population is expected to grow. Since growth in the size of the labor force is one of the two determinants in economic growth, it's a key fundamental factor that will shape the future of financial markets. This is a key fundamental affecting long-term personal financial plans. It's important and it has practical consequences on retirement portfolios.

With the working age population stalling, Europe's economic growth is sluggish. To stimulate the economy, Germany's central bank has pushed lending rates into negative territory, which is unprecedented. Germany is the world's second largest issuer of government-backed bonds and its action has depressed interest rates on U.S. Treasury Bonds. This demographic trend is set to shape growth rates in major economies across the globe for the decades ahead, which means low-rate conditions in the U.S. could persist for years. No one can predict the next move in the stock market, but demographics are fairly stable and predictable. As a result, it's wise to be sure your strategic investment plan — specially, your portfolio's allocations to bonds — is in sync with this key fundamental. Please call us with any questions.

T.S.M.

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Hiddenomics™ Challenge: Find The Leading Economic Indicators

The leading economic indicators (LEI) are part of this picture, but this quiz will help you see the forest for trees. Just like this picture of change, the economic picture is always changing right in front of us, making it hard to see even the most obvious trends unfolding in front of us.

To be clear, the picture includes the trendline of two decades of monthly LEI data, a period encompassing the decade-long expansion already in progress, plus the two preceding expansions and recessions. Can you see the hidden trend?

Here's what you're looking for: the index of leading economic indicators. The LEI declined slightly in

October after going nowhere for five months. The sideways LEI fueled a new round of frightening stories in the media.

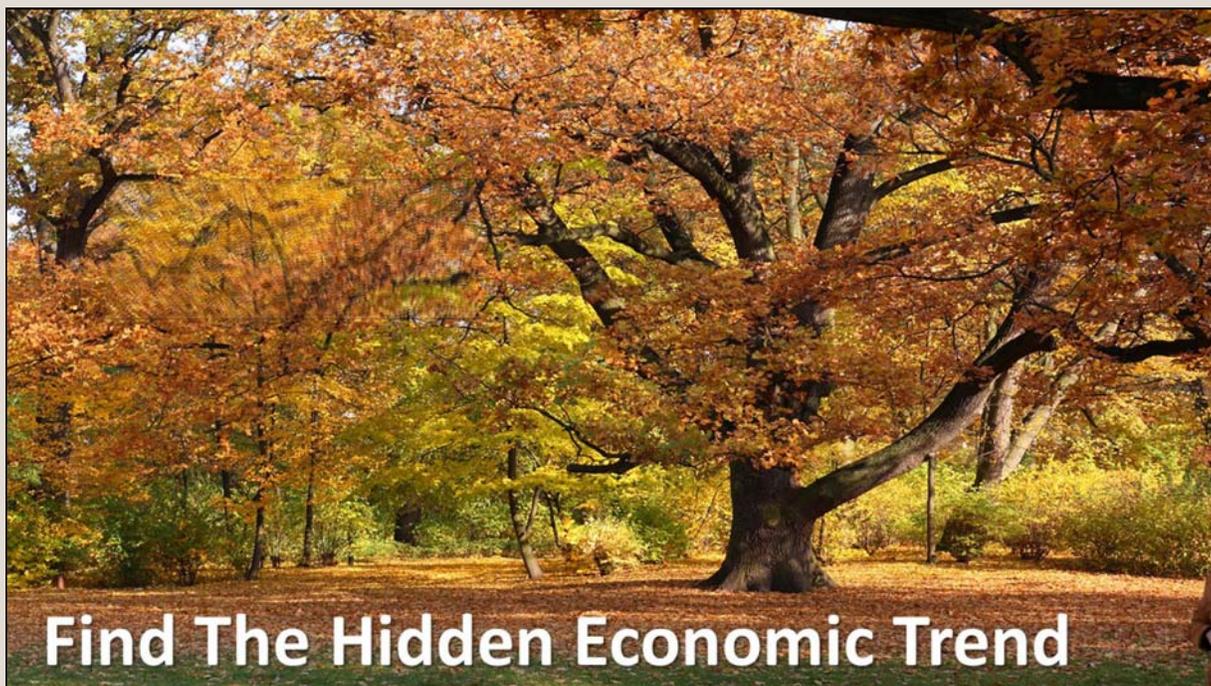
To be clear, focusing on the past six months of sideways action in the LEI index literally misses the big picture in this Hiddenomics™ challenge.

The LEI collapsed months before every recession for many decades,

earning a reputation as a reliable leading indicator of a recession. Such a collapse is not happening now.

In addition, the six months of going sideways followed three years of record high LEI readings.

Put in proper perspective, despite six months of going nowhere, the LEI currently remains near its all-time record-high. ●



Performance Anxiety: A Leading Cause Of Investor Dysfunction After Age 55

Are you nearing retirement and worried about your portfolio's performance? Do you fear outliving your money?

Investment performance anxiety is often hard to talk about for a pre-retiree and can lead to investor dysfunction. This revealing illustration vividly shows that retirement success is about the size of your savings rate when

you're in your 50s and 60s! Although your portfolio

performance is more important in your 20s and 30s, your savings rate matters more to retirement success as your retirement nears.

A 25-year-old with a \$35,000 income that rises annually by 3%, who saves 6% of their income in a tax-deferred retirement plan and averages a 6% portfolio return annually, would accumulate \$528,007 at age 65. If the 25-year-old boosts their savings rate to 10%, the retirement account would grow to



Financial Lifeboat Drill For Mustering In Emergencies

Put yourself through this brief lifeboat drill, to prepare for things suddenly going wrong. Everything may be fine right now, in the eleventh year of the economic expansion. That's a sensible time to test your ability to muster the resources to respond to a range of emergency scenarios.

next year or two, are you ready to ride out the storm — even if it takes a decade to come back? That's approximately what happened in the global financial crisis of 2008. Although this is not in the forecast, a written investment policy statement can eliminate any ambiguity about your investment risk preferences and

financial wherewithal to carry on if you die? Insurance — specifically no-frills term insurance — is meant to manage the worst of all risks families face.

4. Beneficiary designations.

Life changes families. Divorce, death, health, and family financial dynamics change over time, making it necessary to reexamine beneficiaries listed on your retirement and other accounts.

5. Retirement income

plan. Retirement income planning is being transformed by U.S. demographic trends and changes to the U.S. Tax Code. A retirement income plan done before the 2018 tax law changes, or that is not in tune with the demographic trends affecting income investing, should be updated.

6. Medical proxy.

If you are unable to make your own medical decisions, give the power to make medical decisions for you to someone you trust.

7. Final details.

Specify preferences about your funeral, and leave a list of all your accounts, assets, loans, important legal documents and advisors delegated to carry out your final instructions. Include how you want certain personal possessions and family heirlooms treated. If you have social media accounts, you can let someone know what to do, or there are apps that write or make recordings of final thoughts for loved ones.

A financial lifeboat drill is a pithy concept, belying its seriousness, and it requires answering hard questions about your personal financial, tax, and family situation. It would be a privilege to help. ●



1. Cash. In case you lose your job, lose your health, or are befallen by life's myriad of mishaps, can you pay the bills for at least six months?

2. Investment policy. If the stock market were to fall by 40% over the

\$880,012 at age 65.

If the 25-year-old with the same income annually saves at the same 6% rate, but earns 10% annually, the account at age 65 would be worth \$1,392,758.

Clearly, the extra 4% portfolio return annually boosts the retirement portfolio more for the 25-year-old than boosting the savings rate by 4%.

But look what happens when a 55-year-old is faced with the same dynamic.

A 55-year-old — earning \$84,954 today after 3% raises annually since age 25 — who continues to get 3% raises annually, saves at the 6% rate, and earns a 6% portfolio return annually, would have \$87,344 in their retirement

plan to survive a terrible storm.

3. Family risk. Will your children be able to afford college, will your spouse be able to maintain your family's current lifestyle, and will your other loved ones have the

account at age 65. Boosting their portfolio return annually to 10% would grow the account to \$106,961 at age 65. In contrast, boosting the 55-year-old's savings rate to 10% puts the portfolio value at \$145,573 at age 65 — a much better result.

While pre-retirees often grow anxious about portfolio performance, it's their savings rate that is more influential as retirement nears. Portfolio returns are subject to investment risks, which you do not control. Your savings rate, in contrast, is something you do control. Rather than suffering from investment performance anxiety, it's wise for pre-retirees worried about outliving their money to examine their ability to boost their savings rate. ●

Three Major Investing & Tax Planning Trends For 2020

No one can predict the future of markets, but spotting major new trends in personal financial planning is quite doable. Here are three important new trends to consider in managing your wealth in 2020.

Delaying Distributions Until Age 72. Postponing required minimum distributions (RMDs) 18 months is a new thing you want to consider. The SECURE Act, which was signed on December 20th, 2019, delays RMDs on IRAs and other federally qualified retirement accounts from age 70½ to 72. This small change can amount to big bucks because your IRA can compound without being taxed for an extra 18 months. Deferring taxes 18 months on a large IRA is a no brainer, if you can afford it. This step in your retirement income plan should be part of your overall strategy to outlive your money and create a legacy for your family.

New Retirement

Income Planning Choices. The Setting Every Community Up for Retirement Enhancement Act of 2019 will enable more lifetime income annuities to secure retirement. This will be good generally, but there is one huge caveat: annuities can be expensive. Lifetime income backed by an insurance company's creditworthiness makes for a great sales pitch but are best advised on by a professional who places your best interest above all else, including their sales commissions.

2% U.S. Growth & Low Rates. The latest indication of what to expect

on interest rates and economic growth came on December 17th, 2019, in an interview with Robert S. Kaplan, President and Chief Executive Officer, Federal Reserve Bank of Dallas. "We expect, again, 2%-plus growth, 2% growth for next year, unemployment rate around 3½%," Mr. Kaplan told the Council on Foreign Relations. "We'll have some firming in inflation gradually toward 2%. And I think with that profile, I think the right—at 1 1/2-1 3/4 fed funds rate, I think the right thing for us to do is stay right where we are unless something changes materially on the upside or the downside." In addition, on December 11th, the Federal Reserve released its latest expectations for growth, inflation, and unemployment for 2020, which are highlighted in the chart.

Strategic tax and financial planning can boost an individual's retirement fund year after year but requires personal attention from a qualified professional. ●

Variable	Median ^a					Range ^b				
	2019	2020	2021	2022	Longer run	2019	2020	2021	2022	Longer run
Change in real GDP	2.2	2.0	1.9	1.8	1.9	2.1-2.3	1.8-2.3	1.7-2.2	1.5-2.2	1.7-2.2
September projection	2.2	2.0	1.9	1.8	1.9	2.1-2.4	1.7-2.3	1.7-2.1	1.6-2.1	1.7-2.1
Unemployment rate	3.6	3.5	3.6	3.7	4.1	3.5-3.6	3.3-3.8	3.3-4.0	3.3-4.1	3.5-4.5
September projection	3.7	3.7	3.8	3.9	4.2	3.5-3.8	3.3-4.0	3.3-4.1	3.3-4.2	3.6-4.5
PCE inflation	1.5	1.9	2.0	2.0	2.0	1.4-1.7	1.7-2.1	1.8-2.3	1.8-2.2	2.0
September projection	1.5	1.9	2.0	2.0	2.0	1.4-1.7	1.7-2.1	1.8-2.3	1.8-2.2	2.0
Core PCE inflation ⁴	1.6	1.9	2.0	2.0		1.6-1.8	1.7-2.1	1.8-2.3	1.8-2.2	
September projection	1.8	1.9	2.0	2.0		1.6-1.8	1.7-2.1	1.8-2.3	1.8-2.2	
Memo: Projected appropriate policy path										
Federal funds rate	1.6	1.6	1.9	2.1	2.5	1.6	1.6-1.9	1.6-2.4	1.6-2.9	2.0-3.3
September projection	1.9	1.9	2.1	2.4	2.5	1.6-2.1	1.6-2.4	1.6-2.6	1.6-2.9	2.0-3.3

Source: Federal Reserve release December 11, 2019.

Income Withdrawal Methods

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The virtue of the 4% solution is simplicity. The downside is that, in the event of a bear market loss, you must be prepared to withdraw less and perhaps live more modestly. In The Great Recession of 2008, stocks dropped and lost nearly half their value, for example. If stocks made up 60% of your portfolio, even this prudent method put a big dent in your retirement income portfolio and took years to recover from.

Fixed Dollar Withdrawal

With this approach, you withdraw a fixed amount each year, perhaps a flat \$40,000. After two or three years, you would reassess the annual amounts you are withdrawing to ensure you are comfortable with the way it is going. A

fixed dollar method is a simple approach, and you can instruct your IRA custodian to withhold an amount to pay for taxes on the income withdrawn each year.

The trouble is, this strategy will not insulate you from inflation and fixed dollar withdrawals are not mindful of year-to-year depletion of your nest egg due to market downturns in stocks, bonds and other risk assets.

The inflation rate has been below 2% for years and is expected to remain low, but that could change and a decline in stock or bond prices in combination with your fixed withdrawals could precipitously shrink the size of your portfolio.

Systematic Method

Another strategy that's easy to administer is to withdraw only the

interest and dividends your portfolio accrues. This allows your principal to grow over time and better ensures a retirement income portfolio. The disadvantages are that you won't take out the same amount each year, and conservative income investors must accept the risk of owning stocks as well as bonds or be prepared for the risk that their fixed-income portfolio will result on less real retirement income.

These methods are tools for making a retirement income portfolio custom built to your personal specifications. No single method is best. While the 4% strategy is the method favored for long-term investors, the fixed dollar withdrawal may make sense depending on your health, Medicaid planning, and other personal details. Please call our office with any questions. ●