

With a combined 50+ years of experience, 2X Wealth Group is committed to educating and empowering investors. We firmly believe financial literacy helps people make better decisions.

Financial Planning: How Much Money is Enough in Retirement?

Does a low interest rate environment blow up your retirement portfolio?

To understand how much is 'enough' in retirement, we need to understand the amount that can be withdrawn annually from a portfolio (inflation adjusted) so we are reasonably certain the portfolio won't go to zero before death. This concept is called the 'Sustainable Withdrawal Rate (SWR)'.

The Sustainable Withdrawal Rate ("SWR") will depend on the individual retiree's situation, including:

- Anticipated years in retirement
- Desire for increased longevity protection
- Desire to leave money to heirs
- Portfolio mix (stocks, bonds, cash)
- Risk Tolerance (desire for higher/lower success rate)

The '4% withdrawal rule', which is the ability to withdraw 4% of your portfolio each year without running out of money, used to be a reasonable rule of thumb for retirement planning. This rule was based on **historical studies of 50% intermediate-term U.S. Treasury notes/50% common stock portfolios** over 30-year investment periods.

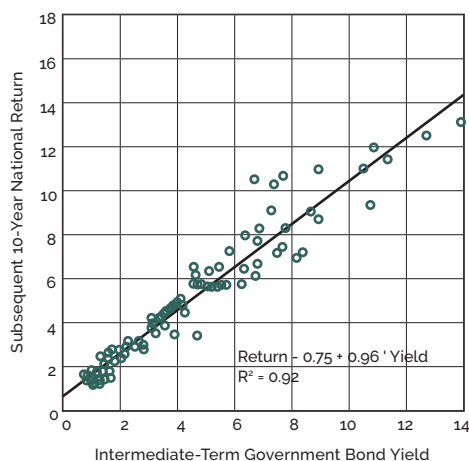
In a well-known **1994 study**, William Bengen found a 4% SWR survived **all historical** scenarios starting from 1926 to 1976. In the later **Trinity Study**, done in 1998, a 4% SWR had **95%** success rate. This lower success rate was affected by the use of corporate bonds instead of Treasury notes (in a period with some large corporate bond defaults).

In 2013, a **study** by Finke, Pfau and Blanchett calculated the SWR based on Monte Carlo simulations*, assuming 2.6% real bond returns and 8.6% real stock returns. With this new analysis, they found a 4% withdrawal rate succeeds **94%** of the time with a similar **50/50** stock/bond split over a 30-year investment period.

The past success of the 4% SWR may not be as relevant in today's interest rate environment.

Past studies include very few low interest rate periods like the one we have today. We care about low interest rates because bond yields are an excellent predictor of 10-year bond total returns AND bonds are a large part of retirement portfolios. See chart below from the Finkel, Pfau and Blanchett 2013 study.

92% Correlation Between Intermediate Bond Yields and Subsequent 10-yr Bond Total Returns



Our current Treasury bond yields of 2% are far below the historical average of 5%. If you retire today, you will likely have very low bond returns for the first 10 years of retirement. That implies lower than average returns on half of a 50/50 stock/bond portfolio. Further, returns during the first 10 years of retirement have a very large effect on future portfolio outcomes. (They explain 80% of outcomes.) Our current low yield problem means a 4% withdrawal rate has a higher risk of failure than in the past.

So, what results do we get with low bond yields at the start of retirement?

In [2018, Wayne Pfau updated the Trinity study](#), reflecting interest rates that started low at the beginning of the retirement period and increased over time to the historical average rate. He came up with the following results in the table below using corporate bonds (not Treasuries) in his Monte Carlo simulations. Under these circumstances, higher equity portfolios have higher success rates. (See Table on following page.)

- A 4% withdrawal rate succeeds 75% of the time with a 100% allocation to stocks for 30 years
- A 4% withdrawal rate succeeds 73% of the time with a 75/25 stock/bond split for 30 years
- A 4% withdrawal rate succeeds 64% of the time with a 50/50 stock/bond split for 30 years

Need help sorting this all out? Make an appointment with us to help you through it.

Strategies to consider for a low interest rate environment:

- 1. Delay retirement until you have a bigger retirement account.
- 2. Use a lower withdrawal rate.
- 3. Increase the equity percentage of your portfolio (more volatility).
- 4. Accept a lower probability of living off your portfolio until you die, or lower probability of leaving money to heirs.
- 5. Trade off withdrawing more now and less in the future.
- 6. Increase stock allocation after a big market drop.
- 7. Use a ratcheting strategy: If your portfolio value increases to 50% above the beginning level, increase your spending by 10%. Revisit every 3 years.
- 8. Call us!

You must determine the appropriate tradeoff between your standard of living in retirement versus the risk of running out of money or leaving too much behind. While the data in the cited studies are instructive, it's important to evaluate both interest rates and the nature of the equity market at the beginning of your retirement. Your portfolio experience will be specific to your retirement timing, it is not an average.

Here's to a successful retirement!

Lori & Lisa

A Monte Carlo simulation performs risk analysis by building models of possible results by substituting a range of values—a probability distribution—for any factor that has inherent uncertainty. It then calculates results over and over, each time using a different set of random values from the probability functions.

Nothing contained herein is intended to be a formal research report, or as a source of any specific investment recommendations and makes no implied or express recommendations concerning the manner in which any specific accounts should be handled. Any opinions expressed in this material are only current opinions and while the information contained is believed to be reliable there is no representation that it is accurate or complete and it should not be relied upon as such. Investing involves risk, including loss of principal, and no assurance can be given that a specific investment objective will be achieved.

TABLE 2:	Portfolio Success Rates Based on Current Market Conditions							
Inflation-adjusted withdrawals for various withdrawal rates, asset allocations, and retirement durations using Monte Carlo simulations incorporation current market conditions.								
	3%	4%	5%	6%	7%	8%	9%	10%
100% stocks								
15 years	99	96	91	82	70	58	45	33
20 years	96	89	78	65	51	39	28	19
25 years	92	82	68	53	40	29	19	12
30 years	88	75	60	46	33	23	15	9
35 years	85	70	55	41	29	19	12	8
40 years	82	67	51	37	26	17	10	7
75% stocks								
15 years	100	98	93	83	68	51	36	23
20 years	98	91	78	60	43	28	16	9
25 years	94	81	63	45	29	16	9	4
30 years	89	73	53	35	21	11	5	3
35 years	85	66	46	29	16	8	4	2
40 years	74	46	22	9	3	1	0	0
50% stocks								
15 years	100	100	94	73	43	18	6	2
20 years	99	91	73	48	27	12	5	2
25 years	95	78	52	28	12	5	2	0
30 years	88	64	37	17	7	2	1	0
35 years	81	54	28	12	4	1	0	0
40 years	74	46	22	9	3	1	0	0
25% stocks								
15 years	100	100	94	73	43	18	6	2
20 years	99	88	58	26	8	2	0	0
25 years	92	63	27	8	2	0	0	0
30 years	79	40	13	3	1	0	0	0
35 years	65	26	7	1	0	0	0	0
40 years	53	18	4	1	0	0	0	0
0% stocks								
15 years	100	99	84	50	20	5	1	0
20 years	97	69	28	7	1	0	0	0
25 years	76	30	7	1	0	0	0	0
30 years	48	12	2	0	0	0	0	0
35 years	28	5	1	0	0	0	0	0
40 years	17	2	0	0	0	0	0	0

Need help sorting this all out? Make an appointment with us to help you through it.

Contact Us:

Lori Zager
lori@2xwealth.ingalls.net
212-269-7757

Lisa James
lisa@2xwealth.ingalls.net
212-269-7758

www.2xwealth.ingalls.net