

## **Will you outlive your money?**

Many investors in their 50s, 60s and 70s wonder whether they will outlive their money in retirement. After all, Americans are living longer than ever, and fewer retirees are covered by pension plans that provide income for life. Those basic facts highlight the importance of building a diversified portfolio of assets during the working years. Certainly, building a large nest egg can give you more options in terms of your retirement lifestyle.

One of the biggest financial questions facing retirees is how to find the right formula for tapping those accumulated assets. After all, if you withdraw too much money from your portfolio, you might run out of money in your 80s or 90s.

Twenty years ago, Bill Bengen, a financial analyst from California, developed a relatively straightforward strategy for investors nearing retirement age. After examining the market conditions and inflation rates since 1926, he calculated that a 4 percent annual withdrawal rate would allow those savings to last 30 years – say from age 65 to 95. He later revised his calculations to 4.5 percent, but the "4 percent rule" remained a yardstick for retirement planning.

That formula may have made sense during the 1990s when high quality U.S. corporate bonds could generate 7 or 8 percent interest, which was well above the inflation rate at the time. But financial conditions have changed dramatically in the past five years and that traditional withdrawal strategy makes less sense.

That's because the Federal Reserve dropped interest rates to almost zero after the 2008 financial crisis, and they have remained at historically low levels over the past five years. While those low rates have had a positive impact in terms of stimulating the U.S. economy, they have put a severe crimp in retirees' income. High quality U.S. corporate bonds now pay – less than half what they paid in the 1990s.

As a result of today's low interest rates, retirees who follow the 4 percent withdrawal rate may have to dip into their principal, increasing the risk of outliving those savings. After all, many of today's Baby Boomers spend almost as many years in retirement than they did during their working careers. According to the Social Security Administration, a man reaching age 65 can expect to live, on average, until age 84, and a woman until age 86. About one out of every four 65-year-olds will live past age 90, and one out of 10 will live past age 95.

So, what's the best strategy for maintaining a comfortable retirement income in a low interest rate environment?

First of all, don't move all your portfolio funds into fixed income investments like bonds upon your retirement. While most retirees want to be sure they don't lose any of their hard-earned savings, fixed income investments may not generate enough income to support a desirable lifestyle – at least at this point in time. They also don't help retirees guard against the hidden risk of inflation, which can rob your portfolio of its buying power. Maintaining some exposure to stocks can help to counter that inflation risk, while potentially increasing the overall return from your portfolio. Second, make sure the portion of your portfolio dedicated to bonds is also diversified into different sectors. For instance, you might consider including emerging market bonds and high-yield bonds, as well as fixed-income assets that can hedge against inflation, such as Treasury Inflation Protected Securities (TIPS) and floating rate bonds.

Finally, make sure that your portfolio includes assets that historically don't move in tandem with one another. That way a decline in any one investment, for example, won't have as great an impact on the total value of your portfolio.

So, consider investing in different types of stocks – large-cap, small-cap and emerging market equities – as well as alternative investments, such as real estate, hedge funds and managed futures.

That's an excellent strategy for sustaining the value of your portfolio during retirement and reducing the risk of outliving your savings.

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