Greenleaf Financial Group

PRACTICAL SOLUTIONS | PERSONAL ADVICE | PROGRESSIVE IDEAS

Hello Jennifer:

Welcome to
The Greenleaf Guide

December 2011 Newsletter

Question

I am a divorced mother of two and have recently returned to a full-time job. My father, whom I cared for until his death this summer, left me about $50,000. I would like to apply this to my kids' college savings, but am starting to worry about my own future. I am in my early 50's and have about $150,000 in retirement savings.

Retirement Withdrawals: What is a Safe Amount?

This year, 30 million of the 78 million baby boomers that are turning 65 have do-it-yourself retirement accounts such as 403bs and 401ks. Therefore, for literally millions of people, knowing how much of their nest eggs can safely be tapped each year has become a matter of utmost importance.

The 4% Rule

In the 1990's, financial planner William Bengen published a study that said a portfolio of 60% large-cap US stocks and 40% intermediate-term US bonds could sustain an annual withdrawal rate of 4.15%, adjusted each year for inflation.

Bengen's research looked at historical stock and bond returns over 30-year periods going back to 1926. Consequently, his research suggested that a retiree with a million dollar portfolio could take out $41,500 in the first year and a similar percentage each year thereafter (adjusting for inflation) and not run out of money until age 95.

Since then, withdrawing 4% has been a

What should I do with my inheritance?

Answer

Women often have a harder time than men achieving lifetime financial security.

Caregivers for both children and aging parents, like yourself, are twice as likely to be women. Such care can mean months and years without a salary.

In addition, although the wage gap has narrowed, the US Bureau of Labor Statistics reports that women across all occupations earn 81% of what men earn.

Both aspects result in lower lifetime earnings, which in turn results in lower social security payments, lower pension benefits, and smaller balances in 401ks, workplace plans, and IRAs.

Moreover, these smaller financial resources have to be stretched over a longer time. A woman who reaches the age of 65 can expect to live to 84 on average, fully three years longer than a man, according to the US Administration on Aging. Longer lives generally result in higher health-care costs, increasing the financial burden on women.

Finally, studies show that parents -- particularly women -- skimp on their retirement savings in order to provide some kind of financial assistance to their kids.

Consequently, I encourage you to put the substantial majority of your

widely followed rule of thumb. However, recent studies show that the last decade has altered the usefulness of this rule.

Extreme Bear Markets Change Everything

Severe stock-market declines, such as those from 2000 to 2002 and in 2008, however, impact the "safe" 4% withdrawal rate substantially. In essence, if a portfolio declines substantially immediately upon retirement, then a person likely has to take out a much larger amount to meet their income needs.

For example, a withdrawal of the same $41,500 on a portfolio of $650,000 is now 6.4%. This larger percentage is a major hurdle to recouping market losses and an investor's money therefore runs out in a much shorter time period.

Be Flexible

Recent studies combine the past decade's substantial market gyrations and withdrawal rates. These studies tell us that the best approach is to adjust withdrawals with the market. When the stock market plummets, go below a 4% rate. In practice, this is difficult to do, but it is highly advantageous.

Some Bad News

Some studies are more dire. Research at Ball State says initial withdrawals should be no more than 2.52% due to low interest rates, low dividends, and volatile stock and bond markets.

Early Years are Key

Ultimately, a bad sequence of returns in the early withdrawal years are a retiree's worst enemy.

Consequently, an advantageous strategy is to go into retirement with a spending reserve that represents a few years of income needs

inheritance toward your own retirement security. Although this may be difficult, think how terrible it would be if you had to turn to your kids for financial help late in life.

You will help them most by helping yourself and by being financially solvent at all times.

(apart from social security and pensions). If your retirement coincides with a severe stock-market decline -- due to layoffs, the two often occur together -- then use your cash reserve and wait for the market to recover.

Three years of income needs is about ideal. If your early retirement years are instead during a bull market, then go ahead and withdraw from your balanced portfolio.

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