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Our economy continues to shock and surprise, causing growing concern for investors, particularly those with their eye on retirement. A recent article by William Reichenstein in *The American Association of Individual Investors Journal* titled "Will Your Savings Las? What the Withdrawal Rate Studies Show" provides insight into what can be done to weather this economic storm. This article reviews two studies that seem to suggest a definitive safe withdrawal rate is possible to help minimize risk while maximizing the benefit to the investor.

First, the article points out that determining the withdrawal rate is a balancing act. If withdrawals begin with an initial rate that is too large, the investor will have an unacceptable large shortfall risk, which is defined as the probability of running out of money within the investor's lifetime. However, if the withdrawals are too little, the investor's lifestyle will be below his or her means. Based on the two studies evaluated in this article, the "Rule of Thumb" is as follows:

> *Assuming an asset allocation of at least 50% stocks, a retiree who withdraws 4% of the portfolio in the initial year and an inflation-adjusted equivalent amount each year thereafter has about a 90% to 95% probability that the portfolio will last 30 years.*

As with any Rule of Thumb, this, while a useful thought, is grossly understated. Several factors can influence the shortfall risk. The first factor considered in this particular article is the sequence of returns; a portfolio will last much longer if returns are strong in the early years and poor in the later years than vice versa. Also, a portfolio's asset allocation between stocks and bonds can vastly impact the longevity of the income stream. Finally, another major factor, as is always the case with "Uncle Sam", is taxes. It is important to consider whether funds have been held in tax-deferred accounts such as 401(k) or if the funds are in a taxable account, where interest, dividends and realized capital gains are taxed each year.

Perhaps most notable, these studies implicitly assume that future gross stock and bond real returns will mimic- or at least be similar - to historical gross returns. Conversely, recent economic reports seem to imply that we are facing unchartered territory. In short, while using the 4% Rule of Thumb as a guideline, be prepared to adjust future withdrawals as necessary to accommodate to the economic fluctuations.

Sincerely,

Steve Walker

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