

A tropical beach scene at sunset. In the foreground, a wooden table and two chairs are set on the sand. In the background, a small wooden hut stands on the beach, with the ocean and a setting sun visible behind it. Palm trees frame the top and sides of the image.

Will You Retire at the Right Time?

*Understanding the Impact of Market
Timing on Retirement Savings*

Why Market Timing Matters in Retirement

Retirement planning isn't just about how much you save—it's also about when you retire and how market fluctuations impact your withdrawals. Even if you accumulate a substantial retirement portfolio, poor market performance early in retirement can significantly reduce how long your savings last. This concept, known as sequence of returns risk, highlights the importance of market timing and strategic withdrawal planning.

Understanding the Impact of Market Timing

During your working years, the sequence of market returns has little impact because you are consistently contributing to your investments. However, once you begin withdrawing funds in retirement, the order in which market gains and losses occur can make a substantial difference in the long-term sustainability of your savings.

For example, if a retiree experiences a market downturn early in retirement, they may be forced to withdraw funds from a shrinking portfolio, which reduces the amount left to benefit from future market recoveries. Conversely, if a retiree starts retirement during a bull market, their assets have more time to grow before facing potential downturns, improving their financial security over time.

Key Takeaways

-  **The order in which market returns occur can affect how long your retirement funds last.** A strong market early on can help a portfolio grow, while early losses can cause funds to deplete more quickly.
-  **Early losses in retirement can deplete savings faster than expected.** Withdrawing funds from a declining portfolio lock in losses, making it harder to recover when markets improve.
-  **Strategic planning can help mitigate risk and provide more financial stability.** Diversification, dynamic withdrawal strategies, and maintaining a cash reserve can help manage sequence risk and sustain income throughout retirement.

By understanding the importance of market timing and implementing proactive financial strategies, retirees can better navigate market fluctuations and extend the longevity of their retirement savings.



How Market Performance Impacts Retirement Savings

The timing of retirement can have a profound effect on how long savings last. Even if two retirees have the same initial investment and withdraw the same percentage annually, the sequence of market returns in the early years of retirement can lead to vastly different financial outcomes. This concept is known as sequence of returns risk, where the order in which positive and negative returns occur can significantly impact portfolio longevity.

Example: The Impact of Market Timing

- Retiree A (Bad Timing):** Retires at the start of a market downturn, experiencing negative returns early on. As they withdraw funds while their portfolio is shrinking, they lock in losses, reducing the amount of money available for future growth. This accelerates depletion, potentially shortening the lifespan of their retirement savings.
- Retiree B (Good Timing):** Retires during a market upswing, allowing their investments to grow before making significant withdrawals. Because early returns are strong, their portfolio has more time to accumulate value, helping it sustain withdrawals over a longer period.

Illustration of Sequence Risk:

Imagine two retirees each starting with \$500,000 and withdrawing \$25,000 per year. The only difference is the sequence of market returns they experience in the first five years:

Year	Retiree A (Early Losses)	Retiree B (Early Gains)
1	-15% (\$425,000)	15% (\$575,000)
2	-10% (\$357,500)	10% (\$607,500)
3	5% (\$340,375)	5% (\$618,875)
4	10% (\$344,413)	-10% (\$531,988)
5	15% (\$386,075)	-15% (\$426,190)

Note on Table Calculations: Each year's ending portfolio value reflects a \$25,000 withdrawal at the beginning of the year, followed by the annual return applied to the remaining balance. For example, Retiree A starts with \$500,000, withdraws \$25,000 (new balance: \$475,000), then experiences a -15% return, resulting in $\$475,000 \times (1 - 0.15) = \$403,750$. Rounded values are shown for simplicity.

After just five years, Retiree A has only \$386,075 left, while Retiree B still has \$426,190, despite experiencing the same long-term average return. Over time, this gap widens, making it harder for Retiree A's portfolio to sustain withdrawals throughout retirement.

Strategies to Mitigate Sequence Risk:

-  **Delay Withdrawals in Market Downturns:** Use cash reserves or alternative income sources (such as part-time work or rental income) to avoid selling investments at a loss.
-  **Adjust Withdrawal Strategies:** Reduce withdrawal rates in poor market years and withdraw more when markets are performing well.
-  **Use a Bucket Strategy:** Maintain separate pools of assets—cash for short-term needs, bonds for mid-term stability, and stocks for long-term growth.
-  **Consider Annuities for Stability:** Guaranteed income products like annuities can provide a steady cash flow regardless of market conditions.

The Sequence of Returns Explained

During the accumulation phase, the order of market returns doesn't matter much because you're not withdrawing money. However, during the withdrawal phase, the timing of market gains and losses can significantly impact your portfolio's longevity. If you experience poor returns early in retirement while withdrawing funds, you may deplete your savings faster, leaving less capital to recover when the market rebounds.

Visualizing the Impact:

	Early Gains Portfolio		Early Losses Portfolio	
Year	Return (%)	(\$100K)	Return (%)	(\$100K)
1	27%	\$127,000	-29%	\$71,000
2	16%	\$147,320	-2%	\$69,580
3	21%	\$178,257	-14%	\$59,839
4	-10%	\$160,431	+17%	\$70,011
5	8%	\$173,266	+11%	\$77,713
6	11%	\$192,325	8%	\$83,930
7	17%	\$225,021	17%	\$75,537
8	-14%	\$193,518	-10%	\$91,399
9	-2%	\$189,647	21%	\$106,023
10	-29%	\$134,650	16%	\$134,650

Even though both investors experienced the same average return over 10 years, the sequence in which those returns occurred made a dramatic difference. The investor who faced losses early had fewer assets left to benefit from later market recoveries, ultimately reducing their portfolio's longevity. Once withdrawals begin, locking in losses by selling assets in a downturn makes it harder to rebuild wealth over time.

Managing Sequence Risk:

One way to mitigate this risk is through the bucketing strategy, where assets are divided into different investment pools based on time horizon:

- **Short-term bucket (0-5 years):** Cash and low-risk bonds to cover near-term expenses and avoid selling stocks during downturns.
- **Mid-term bucket (5-10 years):** Conservative investments like bonds and dividend-paying stocks that provide moderate growth while reducing volatility.
- **Long-term bucket (10+ years):** Stocks and higher-growth investments to take advantage of long-term market appreciation.

This strategy ensures that retirees have liquid assets available for withdrawals without needing to sell volatile investments at a loss during market downturns.

How to Protect Your Retirement Savings

While no one can control market performance, these strategies can help reduce the impact of sequence risk and preserve your retirement savings for the long haul:

1. Maintain a Diversified Portfolio

- Spread investments across a mix of asset classes, including equities, fixed income, real estate, and alternative investments to mitigate risk.
- Adjust asset allocation over time based on retirement proximity—gradually shifting toward more conservative investments as you near retirement.
- Consider rebalancing your portfolio annually to maintain your target allocation and avoid overexposure to high-risk assets.
- Utilize low-cost index funds or ETFs for diversification while keeping investment costs minimal.

2. Use a Cash Reserve Strategy

- Keep 1-3 years' worth of essential expenses in highly liquid, low-risk investments such as high-yield savings accounts, money market funds, or short-term bonds.
- Establish a separate emergency fund to cover unexpected expenses like healthcare costs, home repairs, or market downturns.
- Withdraw from cash reserves during market downturns instead of selling investments at a loss, allowing your portfolio to recover.
- Consider a tiered cash strategy where funds are divided between short-term liquid assets and slightly longer-term, stable investments.



How to Protect Your Retirement Savings *(Continued)*

3. Consider Guaranteed Income Options

- Explore annuities with guaranteed income riders to provide stable, predictable retirement income regardless of market conditions.
- Factor in Social Security and pension benefits as foundational income sources that can help cover essential expenses.
- Look into bond ladders or dividend-paying stocks as additional income streams that provide reliable payouts.
- Assess whether longevity insurance, such as deferred income annuities, may help protect against outliving savings.

4. Withdraw Funds Wisely

- Follow the 4% rule as a general guideline but remain flexible—adjusting withdrawals based on market performance and personal needs.
- Use a dynamic withdrawal strategy, reducing withdrawals during market downturns and increasing them during strong performance years.
- Implement a bucket strategy, allocating assets into short-, mid-, and long-term investment pools to optimize withdrawals.
- Prioritize tax-efficient withdrawals by drawing from taxable accounts first, tax-deferred accounts next, and Roth accounts last to maximize tax advantages.



Consulting with a financial professional can help tailor a withdrawal strategy suited to your unique financial situation; balancing income needs with market risks while ensuring long-term sustainability of your retirement savings.

Is an Annuity Right for You?



Guaranteed lifetime income, ensuring you don't outlive your savings



Protection against market downturns, reducing exposure to sequence-of-returns risk



Joint income options for spouses, offering financial security for a surviving partner

However, annuities are not one-size-fits-all and come with costs, limitations, and considerations that should be carefully evaluated. While they can offer stability, they also have potential drawbacks, such as fees, surrender charges, and restrictions on withdrawals. It's crucial to understand how each type of annuity functions:

- **Fixed Annuities:** Provide a guaranteed rate of return, making them a stable choice for risk-averse retirees. However, their returns may not keep pace with inflation over time.
- **Indexed Annuities:** Offer returns linked to a market index, with downside protection. While they prevent losses in a downturn, they often have caps or participation rates that limit upside potential.
- **Variable Annuities:** Allow investment in market-based options with potential for higher growth but also come with risk, including the possibility of losing principal. These often carry additional fees for management and optional benefits.



Risks and Considerations

- **Liquidity Constraints:** Many annuities impose surrender charges if you withdraw funds too early, which can be costly if you need access to your money.
- **Fees and Expenses:** Some annuities come with high administrative costs, rider fees for income guarantees, and mortality & expense charges that reduce overall returns.
- **Tax Implications:** While annuities offer tax-deferred growth, withdrawals are subject to ordinary income tax, and early withdrawals before age 59½ may incur an additional 10% penalty.
- **Complexity:** Certain annuities, especially indexed and variable annuities, have intricate terms and conditions that may be difficult to understand without professional guidance.

Tip: Before investing in an annuity, compare different options, assess fees and restrictions, and consider your financial goals. Consulting a financial professional can help determine if an annuity aligns with your retirement strategy.

Final Thoughts: Timing and Strategy Matter

Retirement success isn't just about how much you save—it's about how well you manage your withdrawals to ensure long-term financial security. The sequence of returns risk can have a significant impact on how long your retirement savings last. By planning strategically, diversifying your portfolio, and considering guaranteed income options like annuities, you can help safeguard your financial future.

Key Takeaways:

- ✓ Market fluctuations in the early years of retirement can greatly affect your savings longevity.
- ✓ Diversifying investments and having a flexible withdrawal strategy can help manage risks.
- ✓ Cash reserves, pensions, and annuities can provide stability when markets are volatile.

Next Steps:

- ✓ Assess your current retirement savings and withdrawal plan.
- ✓ Consider strategies to reduce market risk in early retirement.
- ✓ Speak with a financial professional about securing lasting income and reviewing annuity options.



By taking proactive steps today, you can better position yourself for a financially secure and stress-free retirement. Don't wait—start reviewing your retirement strategy now and ensure you're prepared for any market conditions ahead.

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