Retirees and Pre-Retirees: You’ve Got This

Key steps to take back control if your retirement portfolio has taken a tumble.

25 March 2020

By Christine Benz

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There have recently been so many examples of people ingeniously working to make the best of a bad situation: the sing-alongs that broke out on Chicago streets this past Saturday night, the young people delivering groceries to older adults who shouldn’t go out, and the community groups gathering and even crafting masks and other needed safety equipment for at-risk medical personnel.

My husband and I witnessed our own version of that “we’ve got this” spirit last Friday. It was my sister’s birthday; she has an intellectual disability and lives with us for part of each year. Under normal circumstances her birthday is a big to-do for our whole family, and this year we had plans for a trip to the salon, lunch and dinner out, and an overnight in a hotel with the extended family the next day. But things being what they are, we had to put all of that on hold this year. In one of our ongoing text chains, I confided to a few neighbor friends that I was worried about how our little household could craft a satisfactory celebration while in quarantine.

The morning of my sister’s birthday, I got a message from one of them. “We’re coming over,” it said. “And we promise to stay safe.” As my husband, sister, and I gathered in the doorway of our house, our eyes absorbed a beautiful sight. About 20 people, adults and children, dogs in tow, were arrayed across the street and sidewalk, with families all keeping a safe distance from one another. “A-one, two, three, happy birthday to you …” They sang in unison and shouted birthday greetings to my sister, displayed hand-lettered signs, and lingered in the street, sharing well wishes with one another from the recommended safe distance. My sister was tickled, my husband was steadily videotaping from his phone, and I was a puddle.

They’ve got this, I thought. We’ve got this. Despite the quarantine, despite the scary headlines about the virus and job loss, despite the canceled plans, this birthday is going to be just fine. It’s going to be different from what we had planned, but that’s OK.

Lately, I've been thinking about that can-do attitude in the context of my work, especially with respect to retirement planning. If you're a pre-retiree or retiree, how can you take an indisputably bad situation--the coronavirus crisis and the related economic and market challenges--and make the best of it given the variables that you actually control?

As with any situation like this, it boils down to surveying what tools you have to work with, picking which are viable, and formulating a strategy. Even as the current crisis has sent portfolio balances plummeting, you can still make your retirement plan work, especially if you're creative and willing to be flexible. Here are the key ways to take what's in your tool kit and turn it to your advantage.

Assess spending adjustments.
As the market has been falling, many retirees and pre-retirees find themselves pondering a frightening question: Am I at risk of running out later on? The best way to protect your plan against that possibility is to tether your withdrawals to your portfolio balance. That means you'll withdraw less when the market is down, in an effort to leave more of your portfolio in place to recover when the market eventually does. On the flip side, you may also be able to spend a bit more when the market is up.

Of course, the most radical way to tie in withdrawals with your portfolio's value is to simply withdraw a fixed percentage of your assets--say, 4%, year after year. On the other hand, fixed-percentage withdrawals can leave retirees with an unpleasant lumpiness in their cash flows. A 4% withdrawal of a $1 million portfolio would be $40,000; a 30% stock-market drop later, a 4% withdrawal from the depressed $700,000 portfolio would be just $28,000.

Yet there are strategies to build in flexibility without completely turning your standard of living upside down, including the notion of simply foregoing inflation adjustments in down markets or employing small but permanent spending cuts in periods of market weakness.

Research also suggests that new retirees, in particular, should employ a modest starting withdrawal amount. Somewhat counterintuitively, that owes less to the very weak stock market, where market downdrafts actually increase future return prospects, and more to very low yields in place today. (Starting yields have historically been a very good predictor of what bonds are likely to return over the next decade. The answer: Not much.)

Exercise flexibility and creativity.
If you're not yet retired or early in your retirement, one of your most valuable tools doesn't relate to your portfolio at all, but rather to the rest of your life: How flexible are you with respect to the contours of your plan--working longer and/or reining in spending?

There are a lot of levers you can pull that fall under the heading of flexibility. If you're not yet retired, being willing to work a bit longer enables your portfolio to recover (if not fully then at least partially), allows you to make additional contributions, and makes delayed Social Security filing possible. Working longer also means that you'll be making withdrawals over a shorter time horizon. Being willing to work part-time in retirement achieves some of those same benefits, albeit not to the same extent.

Of course, there's a realistic possibility that weakness in the broad economy could limit some employees' ability to work longer. That's why it's important to remember the other side of the ledger: Are there lifestyle adjustments that you could make to reduce your in-retirement overhead in case you can't work longer, or decide you don't want to? Such changes will usually be easier to undertake early on in retirement than after you've been retired for several years. Relocating from an expensive part of the country to a cheaper one can be one of the most impactful ways to meaningfully reduce in-retirement spending, but any such decision is obviously about a lot more than money. Morningstar contributor Mark Miller has talked about the benefits of more modest but still impactful relocations--for example, staying in the same general urban area but moving to a cheaper home at the end of the train line rather than remaining in the more expensive city or inner suburbs.

Ultimately, it's all about finding the right balance given your priorities. If your vision for your retirement is fixed on pursuing a very specific lifestyle that you're unwilling to change--lots of travel, for example--then working longer and/or part-time may be the best avenue to making your retirement plan add up. If you're more flexible on the lifestyle/spending front, you may be able to retire earlier. Some of the ways to assess your retirement strategy--outlined below--are good spots to enlist outside help. But determining your approach to some of these lifestyle considerations requires looking inward and being clear on your vision for retirement (and making sure it jibes with your spouse!).

Assess your portfolio--but don't obsess.
You often hear market experts caution that it's a mistake to mess around with your portfolio in the midst of a volatile market downturn like the one we've recently experienced. That's absolutely true for people who are many years from retirement. Short-term volatility is unnerving, but if they have a long time horizon to retirement, it's something they have to put up with if they want to experience meaningful gains over time. If they can, they may even want to add more to their accounts during periods of market weakness.

The hands-off approach is also right for people who have well-laid retirement plans. If you've been derisking your portfolio as stocks have gone up over the years, it's probably best to give your portfolio a wide berth and pay as little attention to it during this crisis as you possibly can. (The bucket approach has held up well, for example, and could easily be left unattended until year-end or even later on.)

But what if you're getting close to retirement but you haven't looked at your portfolio in a long time? Is it too late to make adjustments? The answer depends on a few key variables: your asset allocation given your spending horizon, how firm you are on your retirement date, and the adequacy of the nest egg you have left.

If you haven't already retired and are determined to do so soon, run the numbers on whether your planned withdrawals, combined with the presence of nonportfolio income sources like Social Security, look sustainable. (Consider getting advice from a professional, too.) If the answer is yes, with flying colors, you may want to derisk to ensure that you have enough liquid assets to draw upon in the first part of your retirement.

On the other hand, if your plan was looking tight coming into the current downturn (and that describes many Americans), you need the growth that comes with letting your equity position ride, even if that means that you could have to delay retirement a few years. I'll be writing in-depth about this conundrum in the future, but standing pat with your equity-heavy portfolio may be the right approach. Here's another spot to get some help from a professional before taking action.

Revisit your approach to nonportfolio income sources.
Given that your portfolio has likely fallen in value, it's more important than ever to make smart decisions about any nonportfolio income sources you'll be bringing into retirement: when to claim Social Security, whether to purchase an annuity and if so what kind, and whether to choose the lump sum or the annuity if you're eligible for a pension.

Each is a complicated decision unto itself, and the current crisis may change the calculus in some cases. For example, waiting longer to claim Social Security is one of the best ways to improve the viability of a retirement plan, in that it enlarges the lifetime benefit. But depressed portfolio values are in the mix now, too. If the choice is between pulling from depressed equity assets to meet your in-retirement living expenses or claiming Social Security earlier than you had planned, the latter may be the right call.

Because these decisions are so crucial and in most cases irrevocable, here's another spot where paying for advice can be money well spent. But I can't emphasise enough the importance of seeking out objective guidance. In the case of annuities, for example, an advisor who charges a flat fee for service is obviously apt to be more objective than one who earns a commission on the sale of the annuity, or even one who charges a percentage of your assets on an ongoing basis. (If the latter arrangement is in play, there could be a disincentive to recommend an annuity, in that it reduces the amount of fee-generating assets.)

Be good to yourself.
Last but not least, don't let concerns about your retirement plan overwhelm what's really important. If you're safe and healthy--and your loved ones are safe, too--you'll be in the best possible position to take care of everything else, including your finances. And staying healthy has direct implications for the viability of your financial plan in retirement. While healthcare expenses tend to trend up as we age, they're also incredibly variable; some retirees' out-of-pocket outlays are significant while others' are much smaller.

Of course, we don't exert complete control over our healthcare outcomes. But practicing the boring old strategies of eating well, staying active, limiting stress, and getting enough rest certainly can't hurt. Research also points to there being a connection between social interactions and health and longevity. So, make time for those family dinners, schedule FaceTime conversations with your friends, kids, and siblings, and take part in one of the Zoom happy hours that are getting so popular. And don't forget to celebrate birthdays.