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The Importance Of Equity Returns In Your Retirement Portfolio

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As retirement approaches, there is a general glide path shift of moving investment assets out of the stock market and into bonds or fixed income. In fact, target date retirement funds created an entire industry that use a gradual passive shift from equities to bonds as the retirement target date gets closer.

With healthcare costs rising and questions regarding Social Security funding over the next few decades, many fear that this shift to bonds will be inadequate to generate the returns necessary to fund what could be a 30+ year retirement. This uncertainty has also lead more savvy investors holding higher and higher allocations in equities to fund their retirement goals than in years past. While stocks have traditionally rewarded investors with the best rate of return over the long term, they undoubtedly experience more volatility on a day-to-day and year-to-year basis. Here are a few tips to follow to make the transition to retirement while owning stocks.

1.) **Have an emergency fund.**

It is typical to recommend having 3-6 months of living expenses. For the first few years of retirement, it would be wise to err on the longer-conservative end of this range. Taking into consideration the lower cost of living in retirement, an emergency fund is easier to achieve than the average investor would expect. The emergency fund allows flexibility in where you take your income from in retirement, also known as asset location. For example, if there is a period of volatility in the early part of retirement, you would not be forced to sell your stock positions at an inopportune time to cover an unexpected cost. Instead, you would be able to dip into the emergency fund while allowing for the long-term thesis of the equity position to play out.

2.) **Not all stocks are created equal.**

While small or mid-size companies can certainly offer attractive returns, they are also most susceptible to market cycles. In contrast, large companies may not provide the outsized returns of these riskier equities, but they often have stronger balance sheets, are not as volatile, and may offer a cash dividend to their investors. Changing the overall make up of your equity cap exposure can provide confidence through any market condition encountered.

3.) Invest with the future in mind.

Many think of their time frame as the year they retire, this is the concept target date funds use. However, most retirement assets are set aside to fund what can be a 20-30+ year retirement. With that in mind, it makes sense to have a long term view of your asset allocation. Having $1,000,000 today is quite different than having $1,000,000 20 years from now. With the 10 year US Treasury bond paying

0.62% today, it is easy to see how this return would not be sufficient to sustain you through retirement alone. With a focus on the long-term, having some of your retirement assets in equities could provide returns that bring you closer to your financial goals.

4.) Including income streams outside of retirement savings.

Many people overlook other sources of income for retirement outside of their savings. For example, Social Security will provide funds to cover some of your retirement expenses along with a pension if you have one. This can be included as part of your fixed income in your overall portfolio. When looking at how much you need to withdraw from our retirement assets to cover living expenses, it is important to incorporate all sources of income.

We can all remember stories of CDs, money markets and treasuries paying 15%, but those days are long gone. In a different era, it may have worked to have the vast majority of your money in fixed income for retirement. In general, that is not an option in today's environment. Many things have changed over the years and any good financial plan requires flexibility and adaptability. As always, consult with a financial professional should you have any questions regarding your retirement plan.