SMART INSIGHTS FROM FINANCIAL PROFESSIONALS

3 Dated Rules of Thumb Retirees Should Think Twice About

The tried-and-true investing and saving rules of thumb retirees depend on may no longer be as reliable as they hoped. Don't let dated "rules" steer your retirement wrong.

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Wouldn't it be great if following just a few "one-size-fits-all" financial formulas really could make planning a successful retirement less problematic?

Unfortunately, there's no such thing.

Oh, sure, there are theories and guidelines and strategies. And some can be helpful as a starting point for financial planning. But there also are some widely used rules of thumb that can end up pointing retirees in the wrong direction, leading them toward a bumpy future.

And this is not just because we're all different, with different challenges, goals and paychecks. (Although that's a big part of it.) But there also is this: The world around us keeps changing, and those long-accepted approaches to investing and income planning often require updating.

Here are three investing and retirement "rules" or strategies you've probably heard of, along with the reasons they might not work for you.

THE 60/40 RULE

Regardless of their goals, risk tolerance or other relevant factors, investors frequently are told that a generic "60/40" portfolio mix (with about 60% invested in stock and 40% in bonds) is the best way to go while they're still working and saving for retirement. And I get it: It's safer than overcommitting to equities. But that conservative 60/40 mix also could potentially shortchange portfolio growth in years when owning more stock might make sense.

Then, when those investors retire, financial professionals often suggest moving even more of their money to bonds — because "when you're older, you should be more cautious."

Though these bond-heavy allocations might have worked out just fine in the past — when interest rates were much higher, and inflation was much lower — today, it can be a recipe for trouble.

Remember: **Bonds are loans**.[1] If you invest in bonds when interest rates are low (and they really don't get any lower than they were last year), you're basically handing over your hard-earned money for little in return. Indeed, with the current rate of inflation, you could end up being paid back with dollars that are worth less than what you invested in the first place.

The amount of risk in your portfolio should be based on factors besides your age, including your retirement income requirements, your desire for growth or a combination of both. Your portfolio mix should be carefully chosen — and adjusted over time — to suit your individual needs.

THE 4% RULE

Another troublesome old-school formula is **the "4% rule**,"[2] which suggests you can safely withdraw 4% from your portfolio when you retire and, from that point on, continue to withdraw 4% annually while adjusting for inflation.

This rule of thumb has been around for decades, and backtesting has shown the concept did make sense ... in the past. However, because interest rates today are dramatically

lower, it's been proposed that retirees might have more success making their money last if they lower their expectations to a 3% starting withdrawal rate. And even then, the number you decide on may need adjusting when the market is struggling.

PASSIVE INVESTING THEORY

If you can't beat 'em, join 'em.

That's the basic premise behind passive investing, which suggests that cherry-picking individual stocks is an exercise in futility. Fans of passive investing believe that since most investors won't ever manage to reliably "beat" the market, it makes more sense to invest in an index fund built to match or track it.

And they aren't wrong.

Most active stock managers can't beat the market consistently over the long term, especially when you add in the extra cost for the work they do. Therefore, owning a wide swath of the market (i.e., an index matched by a mutual fund) can be smart and cost-efficient.

The problem is this approach doesn't necessarily apply to bonds — or real estate or other alternative investments like commodities — in the same way it does to stocks. And yet I seldom see any distinction made among the different asset classes.

The theory also doesn't apply across all indices.

For example, if you buy an index fund that tracks the S&P 500, you're matching an index that always changes based on what all investors think the top 500 companies are worth. It's "market-weighted," and that makes sense to me.

But what about the Dow Jones Industrial Average? This index is mentioned a lot on the news, but it contains only 30 stocks — and the actual companies or stocks in this index have changed 55 times since the index was established in 1896. So, wouldn't the index creator, in this case Dow Jones, be considered a sort of active manager?

The truth is, it doesn't have to be an either-or argument.

Many investors can benefit from **blending both passive and active investing strategies.**[3] Mutual funds are easy to buy, easy to understand and offer broad market exposure. But there's nothing wrong with using a portion of your portfolio to actively prepare for or respond to changing market conditions or to further diversify your holdings.

The key is flexibility.

THE BOTTOM LINE FOR RETIREMENT SAVERS

Financial theories and rules of thumb are best used as general guidelines, not set-in-stone rules. Many were meant to make planning easier — but if you treat them as a mandate or force yourself into a formula that doesn't meet your needs, risk tolerance or goals, you'll likely find you're making things harder than they have to be. And you could find the promised path to success has instead thrown you way off course.

[1] *https://www.kiplinger.com/investing/bonds/604585/how-to-navigate-the-amusement-park-of-rising-interest-rates*

[2] *https://www.kiplinger.com/article/retirement/t037-c032-s014-is-4-withdrawal-rate-still-a-good-retirement-rule.html*

[3] *https://www.kiplinger.com/article/investing/t023-c032-s014-active-vs-passive-investing-the-case-for-both.html*

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