Advisors

Getting Your Retirement Right

8 tips to help you live the lifestyle you want

You could spend decades saving for retirement, and that's vitally important. But in the end, it's the planning you do in the years leading up to and immediately after you retire that may be critical in determining the lifestyle you'll be able to afford. By having a plan that covers your working years and focuses on the period surrounding your retirement, you may help increase the likelihood you'll be able to live the retirement you've anticipated.

Getting your retirement right

For many, retirement offers the possibility to pursue new opportunities and experiences. However, accompanying this sense of freedom is often heightened concern about two big questions:

- Will I be able to live the retirement I've anticipated?
- Will my money last over a retirement that could last decades?

While there are no guarantees, there are a number of things you can do during your working years to help increase the likelihood your answers to these questions will be "yes." For example, you can start saving as early as possible, have a diversified portfolio, and take advantage of employer matching contributions to your 401(k), 403(b), or similar account.

Using those strategies can be vital, but chances are you've heard of their importance before. What you, like many investors, may not know is just how critical the years leading up to and immediately after you retire can be. In fact, whether years of planning and saving result in affirmative answers to those two big questions can hinge on what happens during this crucial period.

So, successful retirement planning can boil down to having and executing a plan for both the years you spend working and saving as well as that critical period surrounding your retirement date. With that in mind, the following provides eight tips to help you get your retirement right.

1. Be aware of key risks

There are certain key elements everyone should consider when looking to mitigate risk during retirement. The overall process should seek to strike a balance between maintaining enough risk and growth potential to sufficiently fund longer-term needs while also limiting the risk associated with potential nearer-term market volatility or other adverse events.

The following are just five potential risks that retirees face:

Longevity risk. Running out of money or not having enough to maintain a standard of living over the course of a retirement that lasts longer than expected.

Market/return risk. Losing capital and/or receiving lower-than-expected returns due to market volatility.

Withdrawal rate risk. Premature depletion of a retirement portfolio as a result of withdrawing too much money over the long term.

Inflation risk. Reduced purchasing power caused by income sources that fail to keep pace with inflation. (Costs can double in 24 years given only 3% annual inflation.)

Health care/unexpected expenses. Depletion of a portfolio due to unanticipated events. This can prove very costly, especially in the latter years of retirement.

Despite these areas of uncertainty and the often seemingly perilous balancing act of managing both near- and longer-term retirement risks, there are proactive steps that can be taken to increase your potential for success.

2. Understand the trade-offs

Retirement planning often involves balancing different goals, and what is best for you will be influenced largely by your individual preferences and the trade-offs you are willing to make.

Keep in mind that you do not need to select just one trade-off to help achieve your goals; you can select any combination that works best for your personal circumstances. For instance, you decide you want to retire three years earlier than previously planned. To do this, you could opt simply to reduce retirement spending. However, you could also reduce your estate goal and increase savings between now and retirement. By selecting multiple solutions, it may be more palatable than selecting one that would potentially have to change more significantly. Also, keep in mind that if your goals or circumstances should change in the future, you may want to revisit what trade-offs you want to take.

3. Plan and prioritize expenses

Creating a budget for your retirement can provide not only a better sense of current and future needs but also help you determine how much flexibility you have in your spending by breaking down your expenses into those that are essential (i.e., food, housing, clothing) versus discretionary (i.e., vacation, dining out, charitable giving).

Given today's longer life expectancies, you need to think about how your expenses are likely to evolve over time. For example, expenses related to mortgage payments, college tuition, or other large expenditures may decrease while the potential for larger health care costs may increase.

Using the worksheet below can help ensure you include all of your expenses. For a more accurate result, **a more detailed worksheet is available.**

Retirement expense worksheet

Category	Monthly expense		Annual expense	
	Essential	**Discretionary**	**Essential**	**Discretionary**
Housing	$	$	$	$
Food and personal	$	$	$	$
Automobile/transportation	$	$	$	$
Medical/health	$	$	$	$
Family care/support	$	$	$	$
Leisure/social activities	$	$	$	$
Gifts/donations	$	$	$	$
Loans/debt servicing	$	$	$	$
Taxes	$	$	$	$
Other	$	$	$	$
Total	**$**	**$**	**$**	**$**
Total excluding taxes (net income req.)	$		$	
Total essential excluding taxes (net income req.)	$		$	
Spending flexibility (total discretionary excluding taxes)		$		$
Percent of spending flexibility (total discretionary÷total expenses)		%		%

4. Diversify income sources

When reviewing your various retirement income sources, note they're not all created equal in terms of stability. Some, like Social Security and annuities, are more likely to provide steady income over time. Others, such as your investments' value, are more apt to vary. The graphic below illustrates the continuum from more stable to more variable income sources.

What's important to note is how these sources can all fit together to help provide the income you'll need over a retirement that may last decades. For the essential expenses you identified during your budgeting process, you can turn to your more stable income sources, beginning with Social Security. On the other hand, your discretionary expenses can be covered using more variable sources.

Even if your goal is to have your more stable income sources cover your everyday expenses, they may not be enough, and you might occasionally need to tap into your more variable sources, such as your investments.

Take care when claiming Social Security benefits

One of the primary decisions you need to address as you near retirement is when and how you (and, if married, your spouse) want to claim your Social Security benefits. The strategy you select will affect both when and what total benefits you may receive. Your Wells Fargo Advisors financial advisor can analyze claiming strategies to help you determine which one fits your personal circumstances.

5. Construct a retirement portfolio

It's critical to assess your portfolio's overall risk/return profile.

You may want to consider these principles for your retirement portfolio:

- **Diversify your investments.** Diversification seeks to help manage risk by holding various categories of investments. The result is your asset allocation—the ratio of stocks, bonds, cash alternatives, and other investments in a portfolio. It's paramount to find the appropriate level of risk for your situation. For example, a portfolio with a significant level of stocks offering greater return potential might be right for someone you know but be too risky for you.
- **Keep a long-term perspective.** You should maintain a long-term perspective with your portfolio even when you retire. Although market movements and the passage of time may require you to make changes, you should seek the asset allocation you feel comfortable with for a few years at a time.
- **Maintain alignment to your plan.** You should review your portfolio annually to determine whether you need to "rebalance" it by, for example, trimming investments that have grown beyond the target levels and investing in those that have dropped below target levels. A more subtle way of rebalancing is to direct any new funds into asset classes that are below target levels and to fund any cash needs by selling asset classes that are above their target levels.

By constructing your retirement portfolio with these principles in mind, you should find increased confidence in retirement. Although these principles may sound simple, implementing them can actually be complicated and time-consuming, so you may want to turn to a financial advisor to help you create and implement your plan and stick with it over the long term.

6. Understand "sequence of returns" risk

The years immediately preceding and following your retirement date can be especially crucial because the risks of adverse events can be particularly damaging during this time, making this an especially important period to maintain the right balance of discipline and flexibility.

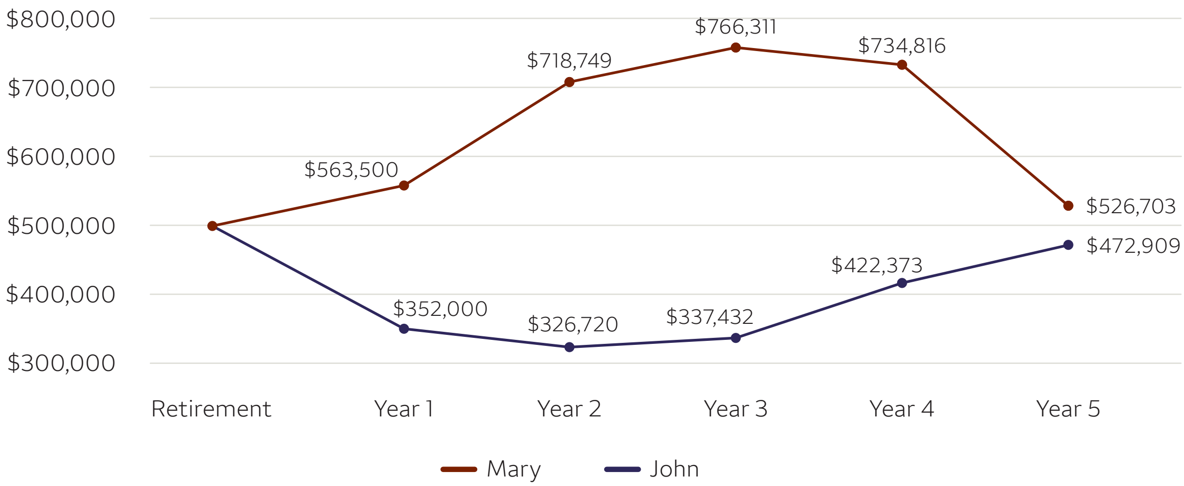
This elevated potential risk is referred to as a sequence-of-returns (SOR) risk. This refers to the fact that it's not only what returns you achieve or the demands you place on your investment portfolio but also when they occur that can have a significant long-term impact on your retirement possibilities.

SOR risk can be a difficult concept to grasp. To help explain, consider the hypothetical tale of Mary and John, who each retired with $500,000 in investments and withdrew $50,000 annually from their portfolios. Over a five-year period, they also averaged the same 6% rate of return on their portfolio.

The difference here, though, is the SOR. Notice in the table below that Mary experienced a positive return in her first few years of retirement and a market decline later on. John experienced the exact same annual returns but in the opposite order, meaning he experienced a negative returns right after he retired followed by a market rebound.

	Mary	John
Year	**Rate of return**	
At retirement	N/A	N/A
1	16.7%	-25.6%
2	31.1%	-1.5%
3	9.4%	9.4%
4	-1.5%	31.1%
5	-25.6%	16.7%
Average annual return	6.0%	6.0%

This chart shows the SOR risk's effects on the two portfolios:



Although it may appear that Mary and John arrived at essentially the same place—despite his rougher ride—the fact is he wound up with $53,794, or approximately 10%, less than her due solely to the market decline early in his retirement. This difference could prove critical in allowing him to live the retirement he wants, especially given today's longer life expectancies.

It's also important to keep in mind that your portfolio is likely to be at or near its greatest value at retirement rather than after you've taken withdrawals for a few years. This can leave it at increased risk of adverse market activity. The table below shows the different impacts on a hypothetical portfolio with $1 million at retirement, $300,000 withdrawn after retirement, and a 25% decline due to market activity.

	Decline occurs at retirement	Decline occurs after $300,000 withdrawn
Portfolio value	$1,000,000	$700,000
25% decline	($250,000)	($175,000)
Difference in loss	$250,000–$175,000=$75,000	

Example is strictly hypothetical and not demonstrative of any actual investment's performance.

Taken together, SOR risk and the potentially higher value of your portfolio mean adverse markets near retirement can have significantly greater effect on savings than if they occur later on. Because the period surrounding your retirement is so critical, it's important to stay in close contact with your financial advisor in the years leading up to retirement to discuss strategies to help manage these risks.

7. Consider counter strategies

When talking with your financial advisor in the time leading up to and immediately after your retirement, strategies you may want to discuss include:

Reallocating your investments. Stocks are considered attractive for retirement planning because of their long-term growth potential. However, that comes with the possibility of significant market volatility. As a result, you may want to shift your asset allocation away from stocks and toward investments that have historically demonstrated more stability, such as bonds, in the years leading up to your retirement. The trade-off you'll have to weigh is these investments' lower growth potential.

Having a cash reserve. Maintaining a reserve in lower-risk accounts that's equal to the amount you expect to withdraw from your investments over 1 to 3 years can help you get through periods of market volatility. By tapping into this reserve instead of your portfolio to cover expenses, you can have more invested to participate in potential rebounds.

Adapting your spending. Itemizing your expenses when you create your budget helps you see which expenses you cannot easily reduce (essential) versus those you can (discretionary). By lowering your discretionary spending and tapping into your cash reserve when there's market volatility, you may be better positioned both psychologically and financially to keep more funds in the market during these periods. If the markets recover, you may be able to return your spending to the previous level but potentially with more assets remaining in your portfolio for use down the road.

8. Have a flexible plan

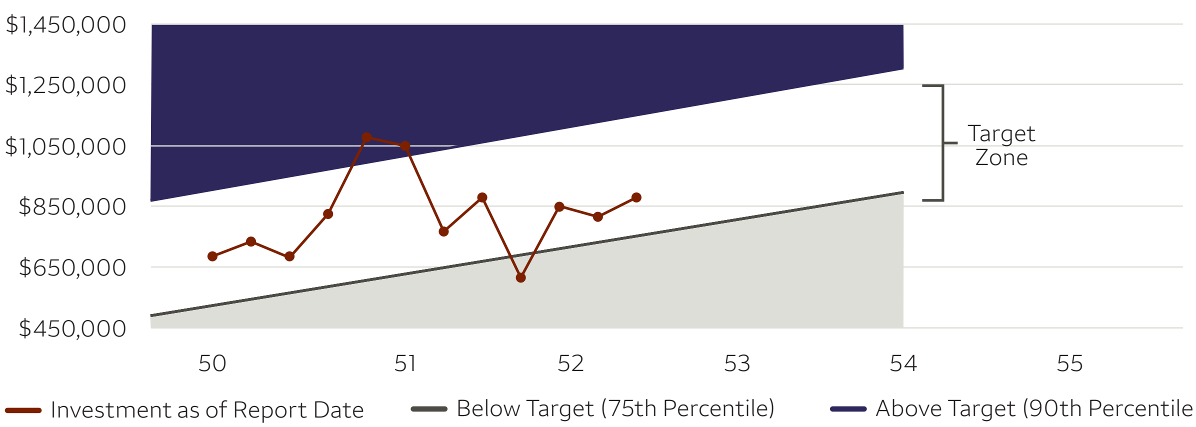
It's important to regularly assess the likelihood that your assets and expected income will fully cover your expected future expenses. Wells Fargo Advisors Envision® planning process is focused on doing just this. It not only helps establish an initial plan but continues to track your progress based on your current portfolio, stated priorities, achieved investment results, and changing circumstances. Because unexpected events are bound to occur, the process can help you explore various courses of action.

The process starts with your current investment mix, how much you plan to add to your investments down the road, retirement goals and estimated expenses, and other factors. It then employs statistical modeling based on historical investment performance and Wells Fargo Investment Institute's strategists' forecasts for how various investments may perform in the future. It stress tests your retirement plan against 1,000 potential market outcomes to create a customized investment plan and a score for its probability of success. The higher the score, the greater the likelihood you'll be able to reach your goals.

The chart below shows one of the process's most valued outputs. It's called simply the "dot," and it tracks your investments' value as you work toward achieving your long-term goals. With an *Envision* plan, you can keep track of your dot as often as you like—even daily. And as long as it stays within a 75% to 90% probability of success, the "Target Zone," you should be reasonably on track toward achieving your goals without making unnecessary financial sacrifices today.

Once a plan is established, adjusting it to account for changes in market activity (a down market, for example) or life events (such as incurring a significant unexpected expense or wanting to retire earlier than you originally planned) becomes relatively simple.

The *Envision* process can help you stay on target toward your goals



IMPORTANT: The projections or other information generated by Monte Carlo simulation depicted in the chart regarding the likelihood of various outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Results may vary with each use and over time.

Envision methodology: Based on accepted statistical methods, the *Envision* tool uses a simulation model to test your Ideal, Acceptable, and Recommended Investment Plans. The simulation model uses assumptions about inflation, financial market returns, and the relationships among these variables. These assumptions were derived from analysis of historical data. Using Monte Carlo simulation, the *Envision* tool simulates 1,000 different potential outcomes over a lifetime of investing varying historical risk, return, and correlation amongst the assets. Some of these scenarios will assume strong financial market returns, similar to the best periods of history for investors. Others will be similar to the worst periods in investing history. Most scenarios will fall somewhere in between. Elements of the *Envision* presentations and simulation results are under license from Wealthcare Capital Management LLC. Wealthcare Capital Management LLC is a separate entity and is not directly affiliated with Wells Fargo Advisors.

Envision plan holders believe it helps them stay on track.

Based on a survey of these investors, here's what they think:

98%

their plan is personally tailored to meet their unique financial goals.

97%

their plan makes them feel comfortable about having the money they need through retirement.

96%

their plan helps them feel better prepared for retirement.

93%

their plan helps them stay on track financially by adapting to changes in their life.

91%

their plan helps them weather market volatility.

Source: Results are based on a survey conducted online by Versta Research from June 5–June 22, 2019, among 457 *Envision* clients with financial advisor relationships. Results are not representative of other client experiences or indicative of future success or performance. The *Envision* process is a brokerage service provided by Wells Fargo Advisors.

Find help to get your retirement right

Whether you're already retired or retirement is decades, years, or only weeks away, you need to help put the odds in your favor by developing a plan that considers what is happening now and what may happen later on.

Wells Fargo Advisors helps investors build retirement strategies that consider both opportunities and potential risks. We understand the complexity of planning for retirement now and in the future and have tools and resources like the *Envision* process to help investors get their retirement right.

For more information and help in developing a retirement plan, talk to a financial advisor at Wells Fargo Advisors.

Risk considerations

Asset allocation and diversification are investment methods used to help manage risk. They do not ensure a profit or protect against a loss. All investing involve risks, including the possible loss of principal. There can be no assurance that any investment strategy will be successful. Investments fluctuate with changes in market and economic conditions and in different environments due to numerous factors, some of which may be unpredictable.

Stocks offer long-term growth potential but may fluctuate more and provide less current income than other investments. An investment in the stock market should be made with an understanding of the risks associated with common stocks, including market fluctuations. There is no guarantee that dividend-paying stocks will return more than the overall stock market. Dividends are not guaranteed and are subject to change or elimination.

Investments in fixed-income securities are subject to market, interest rate, credit/default, liquidity, inflation, and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond's price. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.

Disclosures

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