Do Retirees Own Too Much Stock?

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What Is The Right Stock Allocation?

Traditional rule: reduce stocks as age

- **Traditional formula #1:**
  - **100 (or 110) – age = stock %**
- **Traditional formula #2:**
  - **60% stocks/40% bonds or inverse**
- **Latest financial research**

Why It Matters

- **Sequence of returns risk**
- **Five years before and after retire:**
  - **The Retirement Danger Zone**
  - **Window of Vulnerability**
- **Wide use of Target Date Funds**

Sequence of Returns Risk

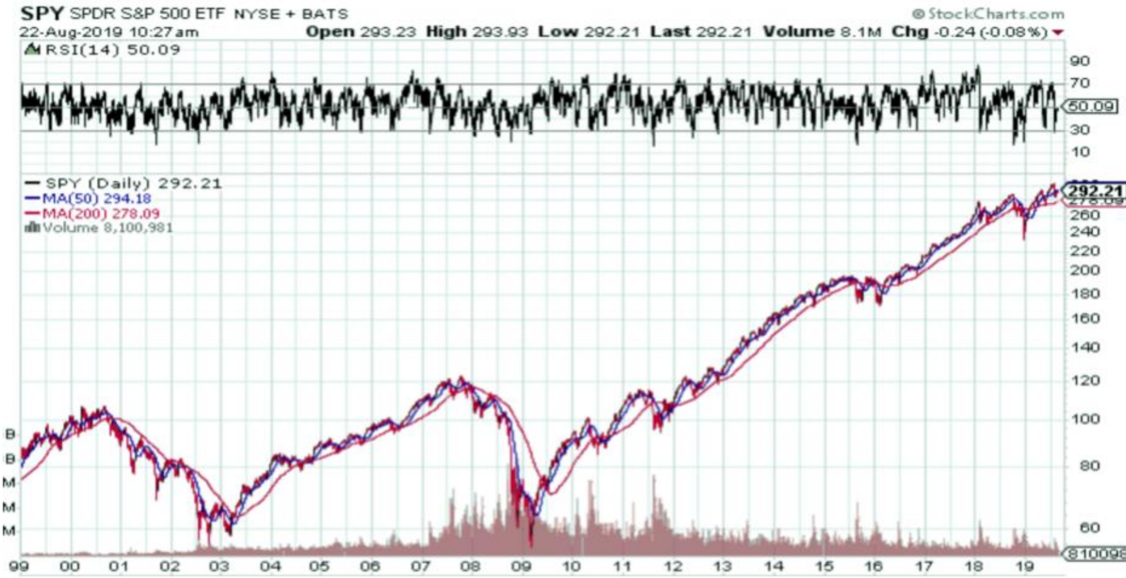
- Largest balance often is at retirement
- Begin drawing down principal
- Less ability to recover losses
- About 80% of distribution variation
- Determines success or failure and adjustments that must be made

Example #1

S&P 500

- ~ 1400 in early 2000
- 815 September 2002
- 1,550 October 2007
- Decline again in financial crisis
- Recovers by March 2013
- Worse for Nasdaq 100

Example #1



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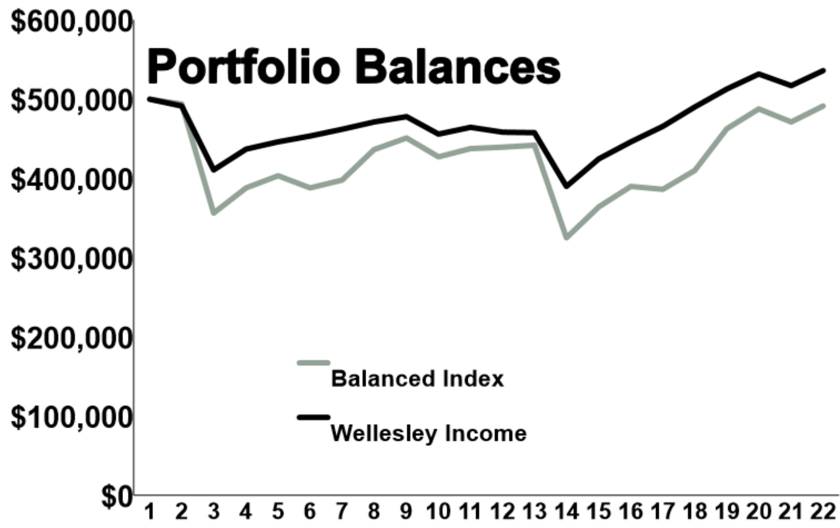
Example #2



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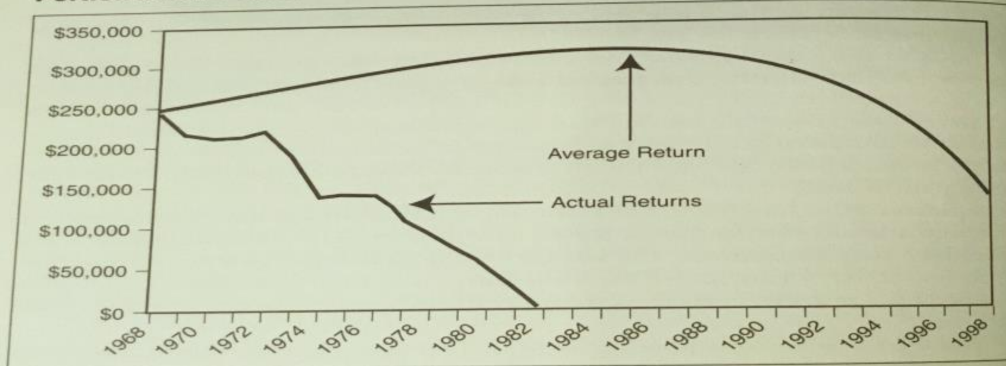
Example #3



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Some Conclusions

- Returns when balance is higher are more important than when balance is lower
- Long period of mediocre returns worse than crash and recovery
- Best time to retire is bottom of bear market

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Advice From Researchers

- Use rising equity glide path
- "U"-shaped lifetime asset allocation
- 20% to 30% at retirement
- Gradually increase to 50% to 70%
- 30% rising to 70% did best
- Or use buckets strategy

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Criticism of Rising Equity Plan

- Success rate not significantly higher
- Historic vs. random returns
- Is a bear market strategy
- Doesn't work if need to spend more

What This Matters Today

Especially vulnerable now because:

- Long period of high returns
- High valuations by most measures
- Projected returns likely below average
- Central banks have few tools left

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What You Should Do

- Historic, average scenarios not useful
- Environment when retire matters
- Stress test
- Don’t set-it-and-forget-it
- True Diversification is better
- Tactical investment strategy is better

Other Helpful Strategies

- Integrate with spending strategy
- Need flexible spending policy
- Increase guaranteed income
- Reverse mortgage LOC as a hedge