

How often should I rebalance my investments and recalculate my retirement budget?

These are questions that are asked frequently. Unfortunately, most of the material in retirement planning assumes that you choose one allocation, take out some percentage the first year, say 4%, and then adjust the amount upward for inflation each year until you die.

That may be OK for an estimate of how much you should save for retirement, but it's obviously not the way you would want to blindly manage your finances in the future. First it assumes that you will not get more conservative as you age. Next it assumes that the investments will go steadily up or, with Monty Carlo programs, will behave in a statistical pattern as investments performed in the past. Older folks who retired in the late 1990's will bear witness to that fallacy.

There are not many 80 year olds who would feel comfortable with a stock allocation that was the same as would be recommended for those who were in their 60's. Most 80 year olds are more concerned with getting a steady income than expecting to get rich, while the 60 year olds still may be wearing rose colored glasses expecting to get 10% returns from their own judicious selection of stocks.

Retirees who have lived through a severe stock market drop know that they cannot continue to draw down the same amount from their stocks as they did before the plunge in market values. And they certainly are not about to increase their withdrawals by the amount of inflation. This last decade of very small returns from the stock market and even lower interest rates from bonds has stressed retirees on both ends of the stock/bond allocation extremes—as well as those in the middle.

Many users of the planning material on www.analyzenow.com write me about how well they have done in spite of the poor economy and my long-standing advice not to count their home as a retirement investment. They don't say they got rich, but they have not suffered like so many retirees. The site has always recommended both conservative security allocations and a conservative withdrawal approach.

My allocation formula is simple, modeled after the old fashioned age-related approach that was maligned by so many professionals years ago as being too conservative. Now those same pundits are eating a lot of crow. My formula for the stock allocation percent is just 100 less the retiree's age. The rebalancing should be whenever the stock values drop below that percentage or grow beyond 10% higher than that percentage. I've found that I've had to rebalance only about every other year.

I certainly do not increase my retirement budget by inflation every year. Instead I calculate a new budget at about the time I do my income tax every year. That's convenient because I have all of the numbers in front of me at that time—and it's also the time of year when it's raining outside in Seattle, so I'm more likely to be house bound. I don't spend a lot of time either on investing or fretting when I should recalculate a new budget. My budget calculation always includes an update of my replacement budget (see www.analyzenow.com) and something for emergencies, so those give me a little cushion.

The baby boomers are going to face a tougher economic time than the boom years after I retired more than twenty years ago. They are going to bear the brunt of (1) current excessive government spending, (2) much less savings than previous generations and (3) the results of an aging population that demands more expensive medical services and where there are less workers to support Social Security, Medicare and government pensions. It's a triple whammy that is inevitable. There are no magic bullets that can get rid of the exponential growth of government debt and baby boomer overconsumption of the last two decades or that can make us younger. These are all cumulative effects that aren't considered by the overly optimistic economists attempting to make us feel good and spend more so that their employers can make more money or the government can collect more income and corporate taxes.

Henry K. Hebeler

11/1/11

www.analyzenow.com