Uncommon Cents

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About

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I bring over 20 years of experience helping families and business owners with their financial planning and investment needs.

Ventum Financial Corp. (Ventum) is a leading independent, Canadian-owned and operated wealth management and capital markets firm, known for our client-centered approach and entrepreneurial spirit. Ventum is a compelling option for investors seeking unbiased investment solutions, professional management and unparalleled service.

If you believe this newsletter would be of interest to your family or friends, please do not hesitate to share it with them.

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Sequencing

Investors are advised to own a well-diversified portfolio within their risk tolerance and then maintain it through all market conditions until their situation changes or they are faced with a major life event. This is all well and true, but if you're an investor who is entering your retirement years, generating a high return, while important, is only one factor that influences how long your savings will last.

Another important factor is the order in which returns are earned. To put it simply, regular withdrawals diminish the dollar value of a portfolio, and it is precisely this dollar value upon which your future returns are compounded. Experiencing negative returns early on can result in running out of savings sooner than if the portfolio experienced positive returns at the outset – definitely something you as an investor want to avoid.

Let us consider the two scenarios below. In both cases, the new retiree is beginning with $1 million and will withdraw $50,000 per year. The only difference is that the sequence of returns has been reversed. That is, Mrs. Green experienced positive returns early in her retirement years whereas Mrs. Red experienced negative returns early on.

	Mrs. Green			Mrs. Red		
Age	5% Annual Withdrawals	Annual Return	Year-end Value	5% Annual Withdrawals	Annual Return	Year-end Value
65			$1,000,000			$1,000,000
66	$50,000	5%	$1,000,000	$50,000	-25%	$700,000
67	$50,000	28%	$1,230,000	$50,000	-14%	$552,000
68	$50,000	22%	$1,450,600	$50,000	-10%	$446,800
69	$50,000	-5%	$1,328,070	$50,000	16%	$468,288
70	$50,000	20%	$1,543,684	$50,000	21%	$516,628
71	$50,000	19%	$1,786,984	$50,000	5%	$492,460
72	$50,000	23%	$2,147,990	$50,000	-16%	$363,666
73	$50,000	9%	$2,291,309	$50,000	8%	$342,760
74	$50,000	16%	$2,607,919	$50,000	14%	$340,746
75	$50,000	23%	$3,157,740	$50,000	24%	$372,525
76	$50,000	22%	$3,802,443	$50,000	14%	$374,679
77	$50,000	-26%	$2,763,808	$50,000	5%	$343,412
78	$50,000	-15%	$2,299,237	$50,000	-15%	$241,901
79	$50,000	5%	$2,364,199	$50,000	-26%	$129,006
80	$50,000	14%	$2,645,186	$50,000	22%	$107,388
81	$50,000	24%	$3,230,031	$50,000	23%	$82,087
82	$50,000	14%	$3,632,235	$50,000	16%	$45,221
83	$50,000	8%	$3,872,814	$50,000	9%	$0
84	$50,000	-16%	$3,203,164	$50,000	23%	$0
85	$50,000	5%	$3,313,322	$50,000	19%	$0
86	$50,000	21%	$3,959,120	$50,000	20%	$0
87	$50,000	16%	$4,542,579	$50,000	-5%	$0
88	$50,000	-10%	$4,038,321	$50,000	22%	$0
89	$50,000	-14%	$3,422,956	$50,000	28%	$0
90	$50,000	-25%	$2,517,217	$50,000	5%	$0

In both cases the average annual return is 6%

The data in the table was sourced from: ©2016 Robert W. Baird & Co. Incorporated. Member NYSE & SIPC. Robert W. Baird & Co. 777 East Wisconsin Avenue, Milwaukee, Wisconsin 53202. 1-800-RW-BAIRD. www.rwbaird.com

The annual average growth rate is the same across both scenarios. If there were no withdrawals, the final dollar amounts would be the same too. However, in the scenario where withdrawals were made, the sequence in which returns are earned is quite relevant - Mrs. Red is left with a shortfall at age 83 while Mrs. Green still has $2.5 million at age 90. Quite the difference!

How do you as an investor reduce your sequence of returns risk? Well, mitigating the effects of market volatility is one way. Proper diversification among multiple asset classes that don't correlate and create lower portfolio volatility especially when nearing the decumulation years, can generate income and minimize the risk of drawing down on assets during a down market. While the numbers used in the above example are extreme and unlikely to manifest in actual market conditions, they do illustrate the concept well; namely, that the sequence of returns from an investment portfolio experiencing withdrawals can have a material impact on the overall retirement picture and it is prudent to manage this risk.

Source: Charts are sourced to https://www.thelinkbetween.ca/

Quotable

"Predicting rain doesn't count; building the ark does."

-Warren Buffett

What I'm Reading

In no particular order, here are my top reads from the past quarter:

1. When We Cease to Understand the World: fictional look at real world scientists and mathematicians that have shaped our world both for better or worse.

2. The Creative Act: deep dive into the creative process from a top music producer.

3. Smoke Gets in Your Eyes: honest look at death from an actual mortician.

4. Abroad in Japan: humorous and in depth description of life as a foreigner living in Japan.

5. The Way Home: memoir accounting what it is like to completely reject modern technology and live off the grid.