

Withdrawal Strategies for Your Retirement Savings

Retirement represents a shift from depending upon income from work to accessing other income sources such as Social Security, pensions, annuities, savings, and investments. Making this transition from the asset accumulation phase of your financial life to the distribution phase requires striking the right balance between how little you can withdraw and still live comfortably vs. how much you can withdraw and not outlive your savings.

The rate at which you draw down your assets, generally known as your withdrawal rate, is the single most important determinant of success in terms of making sure your savings last throughout your lifetime.

The following is an overview of four basic strategies for choosing how to make withdrawals. Which withdrawal methods you choose to implement will depend on your personal situation. This information provides a good overview, but you may want to enlist the help of a Financial Advisor to help you choose which method – or combination of methods – works best for you. Keep in mind, regardless of which withdrawal methods you use, the more critical piece in determining how long your savings will last is how much you withdraw and when.

“Income only” method. The first method is the traditional “income only” method. With this strategy you withdrawal only the interest and dividends generated by your portfolio and do not touch the principal. This might be a good option if: (a) you have a substantial portfolio; (b) you have spending flexibility and can restrict your spending to the income your portfolio generates each year; or (c) you have other sources of income (e.g., pensions, annuity payments, Social Security) that can supplement any shortfalls in years of lower than anticipated returns. However, this strategy may not deliver enough income to meet the spending needs of most retirees.

“Total return” method. A second method to consider is the “total return” method. Using this strategy, your portfolio is invested according to your asset allocation guidelines and rebalanced periodically to maintain the allocation. You determine what percentage you want withdrawn at periodic intervals to provide income. This strategy can be useful if you have a relatively large portfolio, you’re comfortable with market volatility, and you can adjust your spending (as market fluctuations affect how much income is distributed and the value of your portfolio).

“Income floor” method. The third option is the so-called “income floor” method. Using this method, you establish a minimum amount or “floor” of income that supports your essential spending. This strategy is geared toward generating enough income from lifetime income sources, such as Social Security, pensions, and annuities, to cover essential needs (e.g., day to day living expenses). Discretionary spending such as travel, leisure activities, etc., is typically drawn from other income sources as well as your investment portfolio. In order to make this strategy work, you need to have sufficient lifetime income sources to draw upon and other sources of income to make up any potential essential spending shortfalls and to cover discretionary spending needs.

“Bucket” method. Using this final strategy entails dividing your overall portfolio into separate investment pools or “buckets” designed for a specific purpose. Each pool has its own investment goals, strategies, and time lines. For example, you might have a pool of cash and short-term investments for near-term spending, fixed-income investments to cover mid-term spending, and a balanced stock/bond portfolio to cover long-term spending. This strategy can be less daunting than trying to create a sustainable income stream from one large portfolio and help you feel more in control of your assets.

Determining which withdrawal methods will work best for you depends on the size and composition of your portfolio, income needs, risk tolerance, and the amount of flexibility you have in your overall spending. Deciding how much to withdraw when and from which accounts can be complex. A Financial Advisor can help evaluate your personal circumstances and create a customized plan that will generate income and help ensure that your portfolio is positioned to continue to generate income over the course of your retirement years.

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