The Retirement Rule Muslim Investors May Need to Rethink

Retirement planning is usually presented as a question of how much we need to save. But an equally important question receives far less attention: how should those savings be used after retirement begins?

Most discussions about retirement focus on accumulation. During our working years, we earn income, save part of it and invest for the future.

Retirement begins a different stage. Employment income decreases or stops, and the investor must gradually convert accumulated wealth into income. This process is known as decumulation.

The purpose of decumulation is simple: to provide a reliable income throughout retirement without exhausting the portfolio too early. Achieving this, however, is far from simple.

A retiree does not know exactly how long they will live, how quickly living costs will rise, what future healthcare expenses may be or how financial markets will perform. Withdrawing too much may cause the portfolio to run out. Withdrawing too little may unnecessarily reduce the retiree's quality of life.

Market timing creates another important risk.

Consider two people who retire with the same amount of money, hold the same investments and withdraw the same annual income. One retires at the beginning of a strong market period. The other retires shortly before a serious market decline.

Their results may be very different.

The second retiree must continue selling investments to meet living expenses while the portfolio is falling. This leaves less capital available to recover when markets improve. In retirement planning, this is called sequence-of-returns risk. It means that the order in which investment gains and losses occur can be just as important as the average return itself.

This is why decumulation is considered one of the most difficult problems in financial planning. The retiree must balance several competing goals: maintaining a reasonable standard of living, protecting against inflation, preserving enough capital for an uncertain lifespan and possibly leaving wealth to family or charity.

The financial industry has traditionally addressed this problem through the 4% rule.

Under this rule, a retiree withdraws 4% of the portfolio during the first year of retirement and then increases that amount with inflation in later years. A household expecting to withdraw $50,000 annually would therefore aim to accumulate approximately 25 times that amount, or $1.25 million.

The rule is widely used because it turns a complicated retirement problem into a simple calculation.

However, it was largely developed using conventional portfolios that include interest-bearing bonds. Muslim investors must work within a different investment framework. Their portfolios require Shariah-compliant assets and may also need to account for purification, zakat and the costs of Islamic investment products.

This raises an important question:

Can the traditional 4% rule provide the same level of security for a Shariah-compliant retirement portfolio?

Testing the Rule for Muslim Investors

Recent research by Mathieu Vaissié, Ph.D., CAIA, examined this question in detail.

The study, published in the Journal of Financial Planning in May 2026, tested how different Shariah-compliant portfolios might perform during retirement. It used data from Islamic stock, sukuk and real estate indices covering the period from October 2005 to December 2024.

Because this period is shorter than a full retirement, the researcher used a statistical method to generate thousands of possible 30-year market paths. These simulations included different combinations of strong markets, weak markets, inflation and prolonged periods of poor performance.

The starting point was a traditional balanced portfolio consisting of:

60% Shariah-compliant global stocks

40% long-term sukuk

Importantly, the study did not look only at gross investment returns. It also considered management fees, purification and zakat.

To estimate purification and zakat, the researcher used Muslim Xchange's screening and financial data to conduct a look-through analysis of the companies held within the stock and REIT indices. AAOIFI standards were used to estimate the relevant adjustments for each index constituent.

This added an important level of detail. A portfolio may appear sustainable when only its headline return is considered. The result can be different when the actual financial obligations of a Muslim investor are included.

The First Finding: 4% May Be Too High

Under the study's main assumptions, the traditional 4% withdrawal rate produced a success rate of slightly below 90% over a 30-year retirement.

At first, that may sound reasonably safe. However, a success rate alone does not explain the seriousness of failure.

Among the simulated cases in which the portfolio ran out, the average retiree faced a funding shortfall of approximately four years.

This is an important distinction. Running out of money a few months before the end of a retirement plan may be manageable. Running out four years early can create serious financial hardship at a time when returning to employment may no longer be possible.

The research estimated that a withdrawal rate closer to 3.5% was more supportable for the basic 60/40 Shariah-compliant portfolio over 30 years.

The estimate fell further under more demanding conditions. When the retirement period was extended from 30 years to 40 years, the sustainable rate declined to approximately 2.9%. A similarly lower rate was found when the study focused on retirees who experienced particularly weak markets at the beginning of retirement.

These findings show why a single withdrawal percentage cannot remove uncertainty. The result depends on how long retirement lasts, how markets behave and when poor returns occur.

The Risk Hidden Inside a "Safe" Portfolio

A retiree who is concerned about market losses may prefer to avoid stocks and invest mainly in sukuk.

This may feel safer because sukuk are generally less volatile than equities. However, lower volatility does not always produce greater retirement security.

The study found that a portfolio invested entirely in long-term sukuk could support a withdrawal rate of only around 1.9%. Its lower growth made it difficult for the portfolio to support withdrawals and remain ahead of inflation for several decades.

This leads to one of the most important lessons from the research:

The investment that moves the least in the short term is not necessarily the safest investment over the long term.

For a retiree, risk has more than one form. A sudden decline in portfolio value is a visible risk. But there is also the less visible risk that the portfolio will grow too slowly and eventually run out.

The opposite approach—holding only stocks—did not provide a complete solution either. An all-stock portfolio offered greater growth, but it also exposed the retiree to deeper losses and greater sequence-of-returns risk.

The investor therefore faces a difficult balance. Too little exposure to growth assets can increase the risk of depletion. Too much exposure can make the portfolio highly sensitive to market conditions, especially during the first years of retirement.

The answer is not to eliminate all risk. That is impossible.

The more practical answer is to diversify the sources of risk and return.

A Shariah-Compliant “All Weather” Portfolio

The researcher tested an alternative portfolio designed to perform across a wider range of market conditions.

This Shariah-compliant “All Weather” portfolio was divided equally among four asset classes:

1. Shariah-compliant global stocks
2. Sukuk
3. Shariah-compliant REITs
4. Gold

Each asset served a different purpose.

Stocks provided long-term growth. Sukuk offered relative stability and income. REITs provided exposure to real assets, rental income and potential capital appreciation. Gold added another source of diversification and could offer protection during inflation or periods of financial stress.

The portfolio was intentionally simple. Each asset received a 25% allocation rather than using a complicated system to predict which investment would perform best.

The results were encouraging.

The All Weather portfolio produced an average historical return similar to the 60/40 portfolio. However, its volatility was approximately 30% lower. Its estimated maximum sustainable withdrawal rate increased from about 3.5% to approximately 3.9%.

Diversification did not remove every risk, but it made the retirement outcome more stable across the different market scenarios.

This suggests that Shariah-compliant retirement portfolios do not need to depend only on stocks and sukuk. REITs and gold may also play useful roles when they are included carefully and remain consistent with the investor's Shariah requirements.

However, the 3.9% result should not be treated as a guaranteed withdrawal rate.

Historical data cannot include every possible future event. Markets may experience conditions that have never occurred before. Investment products may also perform differently from the indices used in research.

For this reason, the researcher proposed a more conservative planning anchor: 2.5%.

He referred to this as the 1/40 rule.

The 1/40 Rule

Under the 1/40 rule, a retiree begins by withdrawing 2.5% of the portfolio annually and adjusts that income for inflation over time.

For every $100,000 invested, the initial annual withdrawal would be $2,500. To support $50,000 of annual spending, a retiree would need approximately $2 million.

The purpose of the 1/40 rule is not to maximize retirement income. Its purpose is to create a wider margin of safety.

A lower withdrawal rate makes the plan better able to withstand a long retirement, poor market conditions and unexpected expenses. It can also increase the possibility of leaving wealth to family members or charitable causes.

Yet this apparently safer solution creates another serious challenge.

Under the 4% rule, an investor needs approximately 25 times their annual retirement spending. Under the 1/40 rule, the investor needs approximately 40 times annual spending.

For a household requiring $50,000 per year from its investments, the difference is significant:

The 4% rule requires approximately $1.25 million.

The 1/40 rule requires approximately $2 million.

Many Muslim households may find the second target difficult to achieve.

This is the central trade-off. A lower withdrawal rate offers greater security, but it also requires more savings, a longer working period, lower retirement spending or some combination of all three.

The practical lesson is therefore not that every Muslim investor must follow 2.5% without exception. The lesson is that the 4% rule should not automatically be treated as safe simply because it is widely known.

The appropriate rate must depend on the investor's full financial situation.

Benefits and Limitations of a Conservative Approach

The 1/40 rule offers several advantages.

It provides a clear and simple planning target. It builds in a margin for market uncertainty. It may be more suitable for people expecting a long retirement, and it gives investors greater ability to absorb unexpected expenses.

It may also be helpful for those who want to preserve part of their wealth for heirs, sadaqah, waqf or other charitable purposes.

However, the rule also has limitations.

A 2.5% withdrawal rate may cause some retirees to save more than they realistically need or spend far less than they can afford. It may be especially conservative for someone who has a strong pension, government retirement benefits, rental income or other reliable sources of cash flow.

Zakat treatment may also differ according to the investor's assets, circumstances and scholarly guidance. It should not be assumed that one adjustment applies in exactly the same way to every investor.

The research itself has limitations. It used index data covering approximately 19 years and applied statistical techniques to create longer retirement scenarios. Actual funds have

different fees, tracking results and liquidity. Taxes, currencies and local retirement systems can also affect the outcome.

The 1/40 rule should therefore be understood as a conservative planning reference, not a universal Shariah ruling or a guarantee of financial success.

What Islamic Funds and Portfolio Managers Can Do

The findings create several opportunities for the Islamic asset-management industry.

First, Islamic funds can be designed specifically for decumulation. Most investment products focus on building wealth. Retirees need portfolios that can also provide income, manage inflation and control the risk of large losses.

A retirement solution may need exposure to several asset classes rather than relying on one equity fund or sukuk fund.

Second, portfolio managers can report more than average returns. Retirees also need to understand how a portfolio performs during market declines, how long it might support withdrawals and how sensitive it is to poor returns early in retirement.

Metrics such as withdrawal sustainability and potential funding shortfalls may be more useful to a retiree than return alone.

Third, managers can provide greater transparency about the investor's net outcome. This includes management fees, purification estimates and relevant zakat information. Retirement plans should be built around what the investor can actually use, not only what the portfolio earns before these adjustments.

Finally, the industry can develop simple, diversified and regularly rebalanced solutions. Complexity is not always an advantage. A retirement strategy must be understandable enough for the investor to remain committed during difficult markets.

What Financial Advisers Can Do

Financial advisers have an important role in turning these findings into personal retirement plans.

The first step is to separate essential spending from flexible spending. Housing, food, utilities and medical needs may be difficult to reduce. Travel, gifts and other discretionary expenses may allow more flexibility.

This makes it possible to create withdrawal rules in advance. During a poor market, the client might temporarily limit increases in spending or reduce discretionary withdrawals. During strong markets, part of the gains could be placed in a reserve for future weak periods.

The study found that adjusting withdrawals according to market conditions could reduce the rate of portfolio failure. The cost, however, was that retirees sometimes had to accept a temporary reduction in income.

Flexibility therefore improves sustainability, but it requires realistic expectations.

Advisers should also include all sources of retirement income. Government benefits, workplace pensions, rental income and part-time employment can reduce the amount that must be withdrawn from the investment portfolio.

Inheritance and charitable goals should also be discussed clearly. A person who wants to preserve 50% of the original portfolio for heirs will need a different plan from someone who is comfortable gradually using most of the portfolio.

The withdrawal rate should be the result of the financial plan. It should not be chosen before the plan is created.

What Individual Investors Can Do

For individual Muslim investors, the research provides several useful principles.

Begin planning early. A conservative withdrawal rate requires more accumulated wealth. Starting early gives investments more time to grow and reduces the amount that must be saved later.

Estimate actual retirement spending. Investors should calculate expected expenses rather than choosing an arbitrary savings target. They should then subtract reliable income from pensions, government benefits and other sources.

Diversify across different assets. Stocks, sukuk, Shariah-compliant real estate and gold respond differently to economic conditions. No single asset will perform well in every environment.

Maintain enough growth exposure. Avoiding all market movement may feel comfortable, but a portfolio still needs to overcome inflation and support many years of withdrawals.

Remain flexible. Small adjustments to discretionary spending during weak markets may significantly improve the life of the portfolio.

Avoid emotional decisions. A diversified long-term strategy can only work if the investor remains committed during periods of fear and market excitement.

Review the plan regularly. Retirement planning is not a one-time calculation. Spending, health, family needs, markets and Shariah considerations may change over time.

Beyond a Single Percentage

The main value of this research is not the replacement of one fixed rule with another.

The 4% rule offers simplicity, but it may create too much confidence. The 1/40 rule offers a stronger margin of safety, but it may be too demanding for some households.

Neither percentage can fully describe a person's retirement.

A sustainable plan must bring together three elements:

1. A withdrawal rate that reflects the retiree's actual needs.
2. A diversified portfolio that can support those withdrawals.
3. The discipline to adjust when circumstances change.

Islamic wealth management should not end with deciding which investments Muslims may own. It must also address how that wealth will be used, preserved, purified and eventually distributed.

This is particularly important in retirement, when financial wealth may need to replace employment income for several decades.