# Income to last a lifetime

There are lots of articles right now related to making investments that will last as long as a retiree might live. Some of these emphasize withdrawal strategies and others utilize particular investments like deferred annuities that will make fixed payments for a lifetime starting in some future year.

I feel that a number of these are promotional aimed at selling a product or service. I've seen people sucked into investments where they made little but the adviser made lots. Here are my thoughts:

It is not wise to devote an entire retirement portfolio to a particular type of investment or annuity. What was attractive in the past may not be in the future, so it's important to maintain both flexibility and liquidity for a good deal of a retiree's savings.

I like "immediate" annuities for part of an older person's fixed-income allocation, but not all of a retiree's investment income. Unlike other annuities, immediate annuities start making payments as soon as the purchase is made. I also like the idea of buying immediate annuities in small increments over a number of years because those purchased when older will have higher monthly payments, as will those bought in higher prevailing interest rates than our extraordinarily low rates now.

Unless a person has significant other investments to help fight inflation, an inflation-adjusted immediate annuity is likely to be a better buy in the long run that one with fixed payments even though its initial payments may be a third or more lower. Alternatively, consider only spending a fraction of a fixed-income payment and saving the rest for inflation protection. One formula that may help here is to spend only the amount of the after-tax fixed payment multiplied by your age at the time divided by 100.

I prefer to invest my own money rather than turning it over to an insurer, particularly one which will make more on my investment than I will. There are many "deferred" annuity products now with lots of small print that give the insurer lots of flexibility but little to the buyer. Even what little flexibility the buyer has may come at a very high cost. If this is an investment that really interests you, have a knowledgeable third party read the small print of the actual contract and explain the shortcomings.

The best alternative to an annuity, by far, is Social Security. In spite of Social Security's underfunding vulnerability, it's likely to remain one of the key government benefits for a very long time. Those who are near retirement and take Social Security early feeling that it may not exist when they need it are probably making a big mistake even though future payments could degrade somewhat. The increased benefits from delaying the start of Social Security far outweigh the temporary costs of support between, say, age 62 and the delayed start age. There is no commercial annuity that will provide anywhere near as good a benefit, particularly for those with spouses. Nor will it be as secure.

Therefore, I believe that the first "investment" decision should be when to start Social Security payments. That's true whether people are rich are poor.

That decision made, I believe the next consideration should be to preserve a good deal of very safe investments. No matter how bad you think our government may be managed, unlike any other source, our federal government can always print money to make its interest and principal payments. In my view, owning government securities provides principal protection even for depressions, and there's not much else that can do that.

The problem with most government bonds over a long period of time is loss of principal value from inflation. But there are two kinds of government bonds that have inflation protection: Savings I Bonds and Treasury Inflation Protected Securities, better known as TIPS. Both increase in value with inflation as well as a small fixed-percentage increment.

For reasons beyond my ken, the government in recent years has greatly reduced the amount of Savings I Bonds you can buy in a year to $10,000 a person, down from $30,000 a person annually. Apparently the government feels it's better for foreigners to own the debt than our own citizens. The disadvantages of Savings I Bonds are small. You can't cash them in within the first year and you lose one quarter's interest if you cash them before five years. The interest on I Bonds is taxable when the holder decides to cash them, so they don't quite keep up with inflation to the extent of your tax bracket at the time.

TIPS can be bought in funds, from brokers or treasurydirect.gov. I don't like buying them in funds because the principal value will go down when prevailing interest rates go up. That isn't true if you buy the bonds themselves and hold to maturity. If the bonds are bought in an IRA or Roth, the principal will fully increase with inflation. If bought in taxable accounts, the inflation increase will be taxed each year, depending on your tax brackets during the time you hold the bonds.

Both Savings I Bonds and TIPS offer protection from depression and inflation. This is a unique situation. I like to ladder TIPS so that they mature in successive years. That offers (1) the opportunity for cash each year if needed and (2) the opportunity to invest in more of them or what might appear to be a more attractive investment at the time they mature.

Whether a Savings I Bonds, a TIPS ladder or any other investment will last a lifetime is largely dependent on the withdrawal rate. I feel that there is no "safe" withdrawal rate and that it's absurd to quote a probability of how long it will be before you've consumed your savings. If you really want investments to last a lifetime, then the only "safe" thing to do is to make a new withdrawal calculation each year using whatever are your current expectations for life expectancy, returns, inflation and tax rates. The result will be more budget fluctuations year-to-year than a fixed withdrawal rate or simply inflating last year's budget. But your investments will truly last a lifetime. Unless you use projections with very long life expectancies, once you get into your eighties, the longer you live, the smaller will be the withdrawals. This is the only way to stretch your funds over an ever increasing life expectancy.

Nor is there a perfect allocation formula that will maximize your lifetime investment value. There are too many things that can happen, not only in the economic field, but also events in your personal lives that will require substantial funds sometime in retirement. I personally think that it's wise to be well diversified and gradually reduce stock type investments so as to favor fixed-income investments as we age. For well over four decades I've kept my stock holdings as a percentage to a minimum of 100 minus my age and 110 minus my age as a maximum. It has served me well.

Once I've made the decision to invest in an immediate annuity, I do not make the pretense of counting it in my allocation, just as I don't calculate the present value of Social Security or my pension for an allocation analysis. Nor do I count my house as an investment when calculating a retirement budget or allocation. I personally feel that our house is our ultimate reserve, and we shouldn't be prematurely "spending" down its value in retirement.

I am confident that my investments will last a lifetime because I make a new calculation each year. Now approaching my eighties, I feel comfortable with reduced stock holdings in my investment allocation. I also feel more confident that I'll get my Social Security payments than my immediate annuity payments, although I hope that both will last my lifetime.

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