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Wealth Matters Newsletter

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Don't Be Your Own Worst Enemy

One of the most well-known investors of the 20th Century, Benjamin Graham, said, "the investor's chief problem – and even his worst enemy – is likely to be himself."

What Graham understood – and modern research is catching up to – is the idea that we all have emotions and biases that affect our decision-making. The innate wiring built to survive premodern times can be counterproductive in our modern world, especially when it comes to investing.

Let's take a quick look at a few of the human emotions and biases that can adversely impact sound investment decision-making.

Fear and Greed – These are the two most-powerful emotions that move investors and investment markets. Each emotion clouds our capability for rational and dispassionate decision-making. They are the emotions that lead us to believe that prices may continue to rise (think the tulip price bubble of 1636) or that everything has gone so wrong that prices may not recover (think the credit crisis of 2008-2009).

Some investors have found a way to conquer these emotions, be brave when everyone else is fearful, and resist temptations within a too-exuberant market.

Overconfidence – Peter Bernstein, a noted economic historian, argued that the riskiest moment may be when we feel that we are right. It is at that precise moment that we tend to disregard all information that may conflict with our beliefs, setting ourselves up for investment surprise.

Selective Memory – Human nature is such that we tend to recast history in the manner that emphasizes our successes and downplays our failures. As a result, we may not benefit from the valuable lessons failure can teach. Indeed, failure may be your most-valuable asset.

Prediction Fallacy – Humans have an innate desire to recognize patterns and apply these patterns to predict the future. We erroneously believe that because "A" occurred and "B" happened, if "A" happens again, we can profit by anticipating that "B" will repeat. Market history is littered with examples of "rules of thumb" that have worked, until they no longer did.

Financial markets are complex and unpredictable. Our endeavors to tap their opportunities to pursue our financial goals are best realized when we don't burden the enterprise by blindness to the inherent behavioral obstacles we all share. Don't be your own worst enemy.

Keeping a Strong Cash Flow: Evaluate Your Retirement in 3 Steps

Whether your retirement is just around the corner or years away, ensuring your preparations are in order can be the centerpiece of an effective retirement strategy. This is especially critical when you consider that approximately 4 out of 10 households are predicted to run short of money in retirement.

While you may feel like you have a nest egg prepared for retirement, even those with a large amount of savings can be derailed without proper planning. Do you know what your budget will be in retirement and are sure your savings can meet your spending needs? Have you planned for things, such as healthcare, which may be out of your control? Are you spending nearly every dollar that comes in?

The question becomes not how much money do you have saved for retirement, but how can you assess your approach? Read on for 3 steps you can take to find out.

Cash Flow is King
It's important to understand the principle of cash flow. Cash flow is the net amount of cash moving in to and out of your accounts at any given time. The key word here is "time." Cash flow can be best understood through the lens of a given timeframe.

Keeping a close eye on your cash flow may provide you with a better understanding of your financial flexibility. The biggest balancing act retirees face is "money in" versus "money out." Knowing this metric is central to building a strong retirement strategy.

There are 4 main types of cash flow to consider when creating a retirement strategy: the interest your accounts accrue, the dividends you may receive, the capital gains you may receive from the sale of an investment or property, and finally, your original investment.

Step 1: Identify Your Retirement Vehicles
If you've been saving and contributing to your retirement funds over the years, you should be on the right track! You may find it a helpful first step to identify and evaluate the strength of your savings from those years. Gathering this information can take a bit of effort, but it's an important undertaking.

If you have been through the death of a spouse, a divorce, or have been working for many years, there may be accounts that you have forgotten, left behind, not consolidated into your new accounts or didn't realize existed. Try to identify prior jobs, banks, insurance policies, etc. that might have been overlooked as the years passed to help you locate any potential missing assets. Many states have a way to find unclaimed funds from old bank accounts, etc. Check the Treasurer's office in your state or other states you have lived to see if they offer a way to find unclaimed funds. This is a good place to start, but don't hesitate to contact your accountant or financial advisor for help.

There are 4 general sources of retirement income in retirement:

- Social Security
- Personal Savings and Investments
- Retirement Accounts
- Continued Employment

Step 2: Estimate Your Costs
With your income sources in mind, it's time to think about expenses. Knowing how much you expect to spend in retirement is crucial to establishing a strategy that works for you. However, estimating future expenses and creating a pragmatic budget for a lifestyle you don't have yet can be difficult, even for the math whizzes among us. Luckily, there is a simple method that doesn't require a spreadsheet.

First, take a look at your current annual income. In general, retirees spend about 80% of their current income per year in retirement, so if your estimated pre-retirement income is a hypothetical $100,000 a year, you can plan on spending about $80,000 annually in retirement.

Sounds simple enough, but you still have to budget beyond that amount. Think of your 80% as a place to start. This idea is for informational purposes only and should not be considered a substitute for a more comprehensive retirement strategy.

Next, consider the factors that will come into play once you retire. Things like changes in your lifestyle. Will you travel more? Take up new hobbies that require extra funds? Remember to factor in your anticipated medical care costs.

For a more precise estimate of your costs, consider repeating this exercise, but over a 3-year and 5-year time period. This may help you see how consistent your spending is, in order to further anticipate the costs, you could accrue in retirement.

Step 3: Time for Some Math
Now for the fun part: you're going to compare your estimated costs against your scheduled retirement disbursements. At this point, you may come to the realization that your cash flow is less than your anticipated retirement costs. While it can be unsettling, this is valuable information that you can use to modify your strategy, with the help of your advisor.

However, if you have been working with a financial professional for a while, you may have a more positive outlook about what's ahead. As always, we are available to help or answer any questions you may have.

Save Enough, Withdraw Enough
With life expectancies growing, it's understandable that Americans may worry about saving too little for retirement, not planning properly for their wealth to sustain them through retirement or running out of money halfway through. But with careful preparation, you can allow for a well-balanced withdrawal strategy. Ultimately, the longevity of your savings comes down to two factors: how much you have saved, and how quickly you take money out of your accounts.

One strategy is to only draw down the investment gains you experience and leave your principal balance alone. Another approach is to follow the 4% rule, which recommends that you withdraw 4% of your account balance in your first year of retirement, then increase your withdrawal rate each year to allow for inflation. So, a retiree with a $1 million portfolio could take out $40,000 in year one. This example illustrates the concept of the 4% rule and should not be considered a substitute for a more-comprehensive retirement strategy.

Keep in mind the Required Minimum Distributions (RMD) you must take in retirement. The Internal Revenue Service (IRS) publishes RMD tables to help determine the amount you should withdraw and illustrate the minimum age one must be to withdraw annually from certain retirement accounts to avoid tax penalties. Are you update to date on the rules regarding RMDs?

Have a Conversation

Whether you've been prudently tucking away your nest egg for years or find the thought of tallying up all those figures overwhelming, it's important to keep the conversation open.
Discussing the future with your financial professional can help you keep a clear picture of what lies ahead and get over any mental hurdles. Together, we can work toward a cash flow strategy that lasts well into retirement and beyond.

Rules Tighten on Stretch IRAs

Washington was busy this holiday season. As many of us were looking forward to some well-earned time off, new legislation was passed, and it affects some of the old rules for traditional Individual Retirement Accounts. These changes went into effect on January 1, 2020.

One of the biggest changes will affect the required minimum distribution (RMD) timeline for IRAs granted to a beneficiary at the time of your death.

So, what does this mean for you?

Unless an inherited IRA meets a very specific set of circumstances, the non-spousal beneficiary is now required to withdraw the money from the IRA within a period of 10 years.

For example, let's say that you have a hypothetical $1 million IRA. The beneficiary is not required to take a set amount. The requirement is the money must be withdrawn by the end of the 10th year following the year of inheritance. So, if you are leaving your IRA to a 50-year-old child, they must take all the money by the time they reach age 61. In the past, your 50-year-old child could stretch the money over their expected lifetime, or roughly 30 years.

The new limits on IRAs may force account owners to reconsider inheritance strategies and review how the accelerated income may affect a beneficiary's tax situation.

Individual situations may change and vary. If you are currently working with our team or are ready to start planning and want to discuss what this new law means for your retirement strategy, you can contact our office anytime. In the meantime, we'll be keeping a close watch on any other pending changes.

Community Involvement

Our team had a great time volunteering with the Johnson County Christmas Bureau! Their Christmas shop provides food, coats, warm items, hygiene products, gifts and more to families who live below 150% of the poverty level. Over 150 volunteers serve year-round and over 3,000 volunteer slots are available seasonally. If you would like to learn more, visit www.jccb.org.

Commitment to Growth

We are pleased to announce that John Fales has earned the CERTIFIED FINANCIAL PLANNER™ certification. The CFP® marks identify those individuals who have met the rigorous experience and ethical requirements of the CFP Board, have successfully

completed financial planning coursework and have passed the CFP® Certification Examination covering the following areas: the financial planning process, risk management, investments, tax planning and management, retirement and employee benefits, and estate planning. CFP® professionals also agree to meet ongoing continuing education requirements and to uphold CFP Board's Code of Ethics and Standards of Conduct.

John has also been chosen as a member of Leadership Overland Park's Class of 2020. Leadership Overland Park is an annual program designed to provide a source of motivated leaders informed about the community and its issues, and trained to accept future leadership roles in the community.

12980 Foster Street, Suite 160 Overland Park, Kansas 66213 | Phone: 913.814.3800 | Fax: 877.808.6353 | www.searcyfinancial.com