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# Evensky's 10 Tips for Retirement Success

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*Harold Evensky delivering keynote address at Think Retirement Income conference in Boston. (Photo: Charles Sternaimolo)*

Harold Evensky promised his audience at the Think Retirement Income conference “9 Things to Consider for Retirement Success,” and actually delivered 10 of them during his 45-minute presentation on Friday.

The president of Evensky & Katz Wealth Management, based in Coral Gables, Fla., and a long-time leader of the profession in multiple ways, had already been referenced multiple times during the two-day conference for his contributions, and as the keynote speaker he did not disappoint.

He gently chided his peers, saying that advisors too often focus on “the probabilities while ignoring the consequences.” Admitting he is a skeptic on some of the retirement income solutions suggested during the conference, he returned to a long-time academic interest of his: determining what exactly the equity risk premium is.

The academics, citing Ibbotson data, suggest that the long-term equity premium is 7.6%, though he believes it's closer to 6%. Perhaps most important, he said that clients think the equity premium is about 12%, echoing a theme that prevailed throughout the conference: the advisor's key role is managing clients' unrealistic expectations. Mentioning in passing that he still uses Bill Bengen's landmark findings on what constitutes a safe

withdrawal rate during retirement (which he still uses with clients), he went on to list his nine, or rather, 10 considerations to achieving retirement success.

### **1. Don't Underestimate Aging Clients' Spending**

Wearing his trademark red bow tie with emblems of Texas Tech University, where he is a professor of personal financial planning, Evensky began by quashing the assumption that retirees will spend less as they age. "People continue spending until they die," he insisted, showing pictures of elderly passengers on a cruise ship getting around with walkers and oxygen bottles.

### **2. Focus on an Optimal Strategy, Not an Optimal Portfolio**

Evensky's second consideration for retirement success is lack of control over returns. Estimating that the net return after taxes, expenses and inflation of a 60/40 balanced portfolio will drop from today's 7.2% to 2.4% over the next 20 years, he proposed Evensky & Katz's signature core-and-satellite portfolio strategy to reduce costs and improve results. Anchored by a large core of tax-efficient, largely passive investments chosen to provide "beta-plus" returns, the portfolio is filled out with tactical bets on sectors, styles and alternatives with the potential for higher alpha.

### **3. Cope With Volatility**

To illustrate that volatility, risk and luck can have a huge effect on how long the money lasts in retirement, Evensky showed charts he uses to educate clients about how portfolio longevity may be affected by loss vs. gain early in retirement, or by pursuing a fixed withdrawal rate in a volatile market.

E&K's solution is to divide the total portfolio into an investment segment managed for the long term and a cash flow reserve (CFR). The CFR's makeup consists of a year's worth of cash flow plus a lump sum that may be needed over the next five years for a planned major expense, such as college tuition or a second-home purchase. Using this strategy, he said, "we've set up a system where the client gets a check once a month, just like a paycheck." As a result, he said the 1987 market crash was "a nonevent" for E&K clients who felt confident it would not affect their current lifestyle.

### **4. Learn the Lessons of Behavioral Finance**

"In classical finance, people are rational," Evensky pointed out. "In behavioral finance, they are normal," making decisions through mental shortcuts known as heuristics. To make this fourth point in his presentation, he cited three examples:

- **Overconfidence:** Men, in particular, tend to believe they are great stock pickers, despite [research](#) to the contrary by Brad Barber and Terrance Odean of the University of California - Davis.
- **Representativeness:** We tend to jump to conclusions, assuming, for example, that an 80% gain followed by a 60% loss should leave a 20% gain. (In reality, it means a net 28% loss.)
- **Framing:** We make decisions based on how information is framed, such as comparing bologna with 10% fat to bologna that is "90% fat-free." Careful framing can help determine clients' real risk-adjusted goals.

### **5. Remember That Not Everything Can Be Made Simple**

Beware of overconfident analysis, Evensky said. "Good software can make it easier to do complex things, but it can't magically transform the complex into the simple." Noting that probabilities furnished by Monte Carlo

analysis can provide a false sense of confidence, he recommended building a margin of safety into retirement income plans.

## **6. It's Okay to Play It Safe**

Clients close to retirement may be driven by what Evensky called “the paycheck syndrome”: “I’m retired so I need X amount of dividends and interest.” Designing a retirement portfolio around this need can limit its longevity. Instead, he advised designing the portfolio first, then developing a strategy to draw out the necessary cash.

## **7. Be Skeptical of Market Timing**

Evensky is skeptical that an actively managed fund’s performance can be sustained over time. He said that E&K chooses satellite investments (which may be actively managed) with a one-year outlook, and makes tactical tweaks as needed

## **8. Don't Neglect MPT**

“Modern Portfolio Theory isn’t dead. Read [Harry] Markowitz if you think it is,” Evensky said, recommending Markowitz’s article on “Portfolio Selection” in the March 1952 *Journal of Finance*. “What many people forget,” he said, “is that MPT isn’t buy and forget; it’s buy and manage.”

## **9. Maximize Social Security**

Even for higher net worth clients, Social Security benefits remain a valuable retirement income tool, but to maximize its benefits you have to become proficient on Social Security’s sometimes complex rules.

## **10. Keep Annuities and Reverse Mortgages in Reserve**

“What must you earn above the pricing interest rate to justify *not* annuitizing?” Evensky asked, answering his own question with a chart illustrating that retirees from age 55 to 100 must earn considerably more. He also suggested using a reverse mortgage as a backup for clients’ one-year cash flow reserve, instead of a home equity line of credit. “Unlike a HELOC, a reverse mortgage can’t be taken away” by the lender, he pointed out.



By [Sherry Christie](#)