Challenges in Generating Reliable Investment Income

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With interest rates at all-time lows, likely for a few years, generating sufficient income from your investments is more challenging than ever before, particularly for retirees. For those currently, or soon to be, in retirement this can be especially stressful and cause some to take on more risk than they are comfortable with.

Everyone's retirement plans are different, though most people tend to have some similar basic goals including funding their retirement lifestyle, ensuring they don't run out of money, minimizing future tax liabilities, or leaving an inheritance for future generations. Creating a retirement plan that is structured to meet all of those goals can get quite complex, and creating an investment plan to generate the income needed may need active risk management.

With people living longer, income is needed for a longer time frame as well. Unfortunately, the days of 6% GICs and 8% bond yields are likely generations away, certainly not in time for your retirement. Pension plans may not provide all you need. Dividend yields are lower than ever, with the highest quality dividend-paying stocks often generating 4% or less. Overall, stock market returns can provide good returns but come with much higher volatility.

Many Canadians can have several income sources in retirement. These can include employer pensions, old age security, Canada pension plan, registered retirement income funds, non-registered income, annuities, rental property income, or income from part-time work on consulting jobs.

To maximize the income from these sources, it is important to fully consider the tax implication of your withdrawals, the rules under which government benefits may be clawed back, and the optimal withdrawal rate. It can sometimes seem overwhelming, especially when you don't know the key elements determining whether your retirement plan will be successful. How long will you live? What will the markets do? Since no one has a crystal ball and can't predict the future, you need to understand the three issues that will determine your portfolio's sustainability, your withdrawal rate, your investment return, and your income requirements.

In the accumulation phase before retirement, market fluctuations and investment risks can be offset over time, with techniques such as dollar-cost averaging and active management of your portfolio. During the income phase, when you are withdrawing funds from your portfolio, there is far less room for error.

It is vital to create an appropriate portfolio strategy based on your unique cash-flow needs and retirement goals you've defined. Your strategy should guide your every investment decision. A successful strategy and financial plan incorporate several factors, including timing of withdrawals, asset allocation changes and the types of accounts in which your wealth is held. While we all work hard for the money we have earned, our money should also work hard for us! A life well planned will ensure this is the case.