



Briefly Noted

A Simple Formula for Calculating “Safe” Retirement Spending

The Society of Actuaries’ (SOA’s) Committee on Post-Retirement Needs and Risks awarded first prize to Evan Inglis, a senior vice president for Nuveen Asset Management, in a call for essays for his discussion about a simple strategy to determine how much can be safely spent in retirement.

Inglis calls his method the “feel free” spending level. The formula is simply a person’s age divided by 20. The resulting number is the percentage of savings a person can spend over and above any Social Security, pension or annuity-type income. For example, a person who is age 70 can safely spend 3.5% of his or her savings ($70 \div 20 = 3.5$). A 60-year-old would be limited to 3% ($60 \div 20 = 3.0$), while an 80-year-old can spend 4% ($80 \div 20 = 4.0$).

The term “feel free” refers to the fact that a person spending at this level should have little worry about depleting their savings. Inglis believes this rule will not only provide enough money but will also allow a retiree’s portfolio to grow should historical returns be repeated. If returns are lower in the future, then the level of spending should still be enough to last a lifetime.

A modified version of the formula calculates the upper

limit of what can be spent. Dividing one’s age by 10 gives the “no more” level of spending. Spending close to this level (e.g., 7% for someone who is age 70, or $70 \div 10$) will cause savings to “almost certainly drop significantly over the years, especially after inflation is considered.” Inglis adds that “one should not plan to spend at that level,” with the exception of a special circumstance such as a large medical expense.

He added that common sense needs to be applied based on individual circumstances. Having a long-term care insurance policy can allow for a slightly higher spending rate. The potential loss of annuity income, such as a spouse’s pension or Social Security, will alter spending. If interest rates rise significantly, sticking with the divide-by-20 rule would make sense. An expected increase in future income (payments from a deferred annuity) or reduction in spending (e.g., paying off a mortgage) will require adjustments to future spending rates.

Source: “The ‘Feel Free’ Retirement Spending Strategy,” R. Evan Inglis, Society of Actuaries Diverse Risk: 2016 Call for Essays, April 2016.

Data Mixed on Whether Volatility Is Rising

Whether or not stocks have become more volatile depends on whether a person considers volatility on a daily basis or on a monthly basis. This is the finding of an analysis of price movement among exchange-listed stocks for the period of 1926 through 2014.

Not surprisingly, volatility was the highest during the Great Depression. The period of 1931 through 1935 was particularly volatile, with 63% of all monthly price changes exceeding 5% (meaning monthly gains or losses in excess of 5%). In contrast, volatility during the years of 2006 through 2010—which include the financial crisis—was only slightly above average. This more recent period experienced 19 months with monthly price changes in excess of 5% versus the historical average of 16.

When volatility is measured as a daily change in stock prices of at least 2%, the early 1930s still stand out. There were 347 trading days between 1931 and 1935 when price changes were beyond the 2% threshold. In other words, daily price changes exceeded 2% during nearly a quarter of all trading days during that period. Ranking a distant second was the 2006 through 2010 period, when slightly less than 13% of trading days experienced price changes of greater than 2%.

As far as changes in volatility over time are concerned, no discernible trend in monthly volatility exists. Average monthly volatility jumped during the Great Depression, but has both risen and fallen during the years since. Daily volatility, however, has been rising by about 0.007% each day since 1926. Daily volatility has been gradually increasing since 1940.

Of course, most investors don’t mind when volatility occurs to the upside, but are concerned when it occurs to the downside. This is logical since downward price moves reduce wealth. Plus, we feel greater pain from losses than we derive pleasure from gains. Over the long term, there are more downward volatile days than upward volatile days, but the difference is small (a 0.52 ratio, suggesting slightly more downside relative to upside volatility, with a ratio of 0.50 signaling an equal split.) There is no clear trend of downside volatility increasing relative to upside volatility or upside volatility increasing relative to downside volatility, however.

Source: “The Increasing Volatility of the Stock Market?,” Kenneth M. Washer, Randy Jorgensen and Robert R. Johnson, The Journal of Wealth Management, Summer 2016.

What Personal Traits Do Savers Share?

Researchers sought the factors that would explain why some people have a greater propensity to save than others. To find an answer, they used a longstanding survey of Dutch households with extensive information on not only demographics but also wealth and savings. The researchers then added their own survey questions to get the necessary data. In total, more than 1,200 households were surveyed.

Here is a synopsis of the findings:

- **Age:** At the individual level, the willingness to save generally decreases as a person gets older until age 60, when savings patterns flatten and then increase.
- **Economic Hardship Early in Life:** Savings rates are the highest among the Dutch post–World War II generation, who grew up in an economically difficult period.
- **Financial Savings Behavior in Youth:** Those whose savings habits were stimulated by parents or grandparents tend to be better savers throughout their lifetime. Working during youth also leaves a lasting effect on savings behavior later in life. The study's authors opine, "One can teach children the value of money in a way that affects decision making later in life."

- **Interest in Financial News:** This interest has greater relevance for explaining savings behavior than the level of education and numeric ability.
- **Household Administration:** Though the term is not defined, respondents who described themselves as keeping a tight household are more willing to postpone current spending to save for future needs.
- **A Sense of Control:** A person who believes they can influence their financial outcomes is more willing to set aside money now for future spending. The "personal locus of control" also has a greater impact than what generation a person belongs to. It may also be more important than financial literacy in developing strong savings habits.
- **Optimism Regarding the Economy:** Those whose are optimistic about future economic conditions tend to be more willing to postpone current consumption, whereas those who are pessimistic are more likely to spend now.

Source: "Household Financial Planning and Savings Behavior," Dirk Brounen, Kees G. Koedijk and Rachel A.J. Pownall, Journal of International Money and Finance accepted manuscript.

Study Finds Technical Analysts' Recommendations Don't Outperform

One challenge to academic studies of technical analysis—which uses trends in price movement to determine if an asset or an index is likely to rise or fall—is the lack of allowance for subjective decision making. This argument describes technical analysis as having an "artistic aspect" to it.

A study of technical analysis–based buy and sell recommendations on Dutch-listed firms and for the major Dutch indexes found that this assertion does not hold up to scrutiny. Rather, recommendations were found to be "largely in line with simple technical trading rules."

The study tracked more than 5,000 buy and sell recommendations made between 2004 and December 2010. About half of the recommendations were made by individual technical analysts and half were made by automatic technical analysis services. Eight indicators were checked, including moving averages, moving average crossovers, Bollinger bands, moving average convergence divergence (MACD), relative strength index, rate of change, support and resistance and on-balance volume.

The results were critical of the recommendations. Average abnormal returns were found to be negative over each

of the following four five-day periods (day one through five, six through 10, etc.) following recommendations to buy a stock. Average abnormal returns for sell recommendations were barely negative during the first five days, but then turned positive over the following three five-day periods. Commenting on the findings, the study's author observed, "In the event of a buy recommendation on stocks, consistent outperformance is virtually non-existent after the day of the recommendation. The same holds for sell recommendations."

Rather than exhibiting market timing skills, the technical analysts followed merely demonstrated skill in "predicting the past." Buy recommendations were issued on stocks with positive average returns over the short-term period leading up to the day of the recommendation and sell recommendations were issued on stocks with negative average returns leading up to the recommendation.

Source: "Are Chartists Artists? The Determinants and Profitability of Recommendations Based on Technical Analysis," Dirk F. Gerritsen, SSRN, February 22, 2016.