**On Deciding How Much to Withdraw Each Year from Your Retirement Nest Egg**

By [Austin Pryor](https://www.soundmindinvesting.com/about-smi/author/austin-pryor) | 03/08/13 |

One of the more vexing questions facing retirees (and those planning on joining their ranks soon) is "how much should I withdraw from my retirement savings each year?" We don't want to take so much out that we deplete those accounts during our lifetimes, but on the other hand, we don't want to feel like we're scrimping when we could be living much more comfortably.

I wrote a cover article last year ("[Will Your Retirement Nest Egg Last?](http://www.soundmindinvesting.com/member/2012/apr/feature.html)") in which I concluded that a 5% withdrawal rate (increased by the rate of inflation each year thereafter) was a prudent and reasonably safe starting point. I also pointed out the importance of undertaking retirement-related planning annually so you can take into account changes in your financial outlook, lifestyle, and health. You want plenty of time to make decisions—such as saving more or working more years—that can increase the amount of capital you have as you enter retirement and, therefore, the amount of your annual withdrawals. Many advisers have suggested a more conservative 4% withdrawal rate as being less likely to drain your retirement nest egg prematurely. I can't quarrel with that. Each family has to decide how conservative they want to be in making assumptions about future investment returns as well as their willingness to make lifestyle changes. So it caught my attention today when the Wall Street Journal ran an article titled "[Say Goodbye to the 4% Rule](http://online.wsj.com/article/SB10001424127887324162304578304491492559684.html?mod=WSJ_hps_LEFTTopStories)." It seems that some financial planners now consider even a 4% withdrawal rate a bit too aggressive:

Conventional wisdom says you can take 4% from your savings the first year of retirement, and then that amount plus more to account for inflation each year, without running out of money for at least three decades.... Well, it was beautiful while it lasted. In recent years, the 4% rule has been thrown into doubt, thanks to an unexpected hazard: the risk of a prolonged market rout the first two, or even three, years of your retirement. In other words, timing is everything. If your nest egg loses 25% of its value just as you start using it, the 4% may no longer hold, and the danger of running out of money increases....

Well, of course that last sentence is true no matter what percent you use—a devastating early year is always going to present a problem. Nevertheless, the writer offers three alternate strategies that might do a better job than the 4% rule. Unfortunately, they are also vulnerable to unexpected economic developments and/or a weak stock market. But they're worth a look. **1. Use annuities instead of bonds.** Rather than use bonds for the income-producing portion of your portfolio, purchase a single-premium immediate annuity (one of the annuity types discussed favorably—*for some people*—in 3/1/2013 SMI [cover article](http://www.soundmindinvesting.com/articles/view/making-sense-of-the-annuity-puzzle)). In the WSJ article, it was suggested that a 50% stocks, 50% annuity portfolio would be a good combination. Drawbacks: Losing control of 50% of your money means less flexibility if rising inflation becomes a problem, eroding the value of your monthly annuity check. **2. Calculate withdrawals based on your life expectancy.** Each year you would divide the amount in your retirement fund by the years given in the mortality tables based on your age. For example, if you had $1 million at retirement and you had a 20-year life expectancy, you could withdraw $50,000 the first year. You make a new calculation each year based on your latest asset level and life expectancy. Drawback: Your withdrawal amount will fluctuate, perhaps dramatically, from year to year. **3. Base your first year withdrawal on current stock market valuations.** A formula is offered that suggests withdrawing less in the first year if stocks seem highly valued (based on the market's price/earnings ratio), and vice versa. The idea is that you should be more cautious if the market might be overvalued as you begin retirement because a bear market might be forthcoming soon, and less cautious if the near-term outlook for stocks may be brighter. Drawback: In my experience, the price/earnings ratio is not a reliable indicator of future market behavior. The article is provocative and worth a read. I'm interested in your take on the three alternate suggestions as well as what approach you plan to take (or have taken).

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