Life Income Management™

Creating income for life.

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Financial Outlook

AUGUST 2022

401(k) Mistakes to Avoid

We all know how important it is to save for retirement, and 401(k) plans have become one of the most effective ways to save. However, many workers who have access to a retirement plan don't participate. That's probably the biggest mistake you can make. If you have access to a plan, you should take full advantage of it.

If you are participating in your employer's retirement plan, you are headed down the right path. But just because you are participating doesn't mean you're all set. There are 401(k) mistakes that can derail an investor's retirement plan. Here are some of the biggest mistakes and how you can keep things on track:

Not Knowing How Much You Need to Save for Retirement

If you don't have a goal for how much you need to save to live comfortably during retirement, you will probably fall short. The first step is to determine how you want to spend your retirement. In addition to paying your basic expenses, do you want to travel? Maybe you want to start a small business that you've always dreamed about. Or perhaps you have a hobby that you would like to pursue. All of these things need to be factored into your estimate for retirement savings so that you can live the lifestyle you want.

Most financial experts agree that you will need at least 70–90% of your preretirement income to live comfortably. But don't just use a rule of thumb; make sure to review your

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Watch Out for Estimating Mistakes

When determining how much to save by retirement age, several variables must be considered, some requiring estimates that will span decades. Err significantly on those estimates and you can end up with little or no money left during the later years of your life. Three of the most significant estimating mistakes to watch out for are:

- **Underestimating how much income you'll need in retirement.** The entire point of your retirement savings is to ensure you have sufficient income to spend your retirement how you'd like, so make sure you have a good estimate of how much that will cost. Various rules of thumb indicate you'll need anywhere from 70% to over 100% of your preretirement income. At first glance, it seems like you'll need less than 100%, because work-related expenses, lunches out, professional clothes, and commuting costs will be gone. But look carefully at your current expenses and how you plan to spend your retirement years before deciding how much you'll need. If you pay off your mortgage, remain in good health, live in a city with a low cost of living, and engage in inexpensive hobbies, you might need less than 100% of your preretirement income. However, if you plan to travel extensively, must pay for health insurance, and carry significant debt, you may find that 100% of your preretirement income is not enough.
- **Underestimating how long you'll live.** Today, the average life expectancy is 84.3 years for a 65-year-old man and 86.6 years for a 65-year-old woman. But don't use those figures without

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401(k) Mistakes

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specific situation.

Not Saving Enough

Most experts suggest that you save 10–20% of your income for retirement. Because many companies auto-enroll new employees into their 401(k) plans using a default dollar amount, many employees fail to adjust the dollar amount and end up not saving enough to meet their retirement goals.

Others may feel they just don't earn enough to contribute 10% to 20% of their income due to competing demands on their money, such as debt or building an emergency fund. If that is the case, at least try to save enough money to get the company match.

Another method that can help you increase the amount you save in your 401(k) is a contribution rate escalator. Many companies now offer this feature as part of their retirement plans. A contribution rate escalator increases how much you're saving by making small automatic dollar increases over time.

Not Paying Attention to Fees

There are typically three types of fees associated with your 401(k) plan, including administration fees, investment fees, and service fees. These fees can eat into your retirement account's potential growth. To understand how much you are paying in fees and expenses, carefully review your regular statements. Also, at the end of the year, you should receive a statement that will show how much you paid in 401(k) fees.

Also, if you have an old 401(k) plan from a previous employer, you should compare that plan's fees to your current 401(k) plan to see if rolling it over to your new plan makes sense. You should also consider an IRA rollover so that you can select the best investment options.

Too Much Stock in Your Company

Having company stock in your 401(k) plan may come with significant growth potential, but it may also increase the volatility of your retirement portfolio. If your 401(k) plan includes company stock, make an assessment of your risk. Most experts agree that your portfolio should not have more than 10% to 15% of any one stock.

Not Rebalancing Your Portfolio

The reason for asset allocation is to balance your portfolio across asset classes such as stock, bonds, or cash so that if one is performing poorly, others will help offset losses. Over time, however, your investments may drift from your original asset allocation.

You should review your portfolio on a regular basis to determine if it needs rebalancing. Some 401(k) plans provide an automatic rebalancing feature that can do the work for you. If you do not have the time or inclination to rebalance your portfolio, you may want to invest in target-date retirement funds or asset allocation funds.

Not Contributing Enough to Get the Company Match

If your employer matches any percentage of your contributions, you should at least contribute enough to get the company match. Look at your benefits package to determine how much your employer will contribute and take full advantage of this benefit.

In 2022, you can contribute up to $20,500 in your 401(k) or up to $27,000 if you are age 50 or older.

Not Considering a Roth 401(k)

With a traditional 401(k), you receive the tax benefits up front because the contributions lower your taxable income during the current tax year. When you begin taking distributions from your 401(k) in retirement, you will then have to pay ordinary income tax on the withdrawals. With a Roth 401(k), you make contributions with after-tax dollars and your earnings grow tax-free, meaning that you will not have to pay taxes when you withdraw your money. Typically, people who don't need to lower their income today or believe they may be in the same or higher tax bracket during retirement benefit from a Roth 401(k) plan.

Please call if you'd like to discuss this topic in more detail. ❍❍❍

Estimating Mistakes

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further analysis. Average life expectancy means the woman has a 50% chance of dying before age 86.6 and a 50% chance of living past age 86.6. Since you can't be sure which will apply to you, you should probably assume you'll live at least a few years beyond your life expectancy.

- **Overestimating how much you can withdraw annually from your retirement savings.** With a retirement that could span decades, it's important to withdraw a reasonable amount so you don't deplete those savings too soon. A number of factors can make that a difficult number to calculate. First, as noted above, you can't be sure how long you'll be making withdrawals. Live significantly beyond your average life expectancy and you could find yourself with little in the way of savings. Second, inflation over such a long period means you'll have to withdraw increasing amounts just to maintain the same purchasing power. Third, your rate of return on your investments will significantly affect how much you can withdraw annually. When withdrawals are being made, down markets can have a devastating effect on your savings. Not only will your investment value go down, but you will be withdrawing the same amount from a smaller balance. Thus, when the market rebounds, you'll have less capital available to participate in that rebound. Especially if a major market downturn occurs early in your retirement, withdrawing an amount that may have been reasonable during an up market may quickly deplete your assets. Thus, it's generally prudent to keep your withdrawal percentage as low as possible, perhaps 3% or 4% of your balance.

If you'd like help making these estimates, please call. ❍❍❍

How to Raise Financially Responsible Children

Although you'll have to wait a good while before they'll thank you for it, teaching your children to be financially responsible is one of the best gifts you can give them. Of course, the earlier they start to learn about making wise money decisions, the fewer bad habits they'll have to ultimately unlearn.

Lesson #1: Appreciation for the value of money — Money has to be earned — and when it is, they better appreciate its value. Those of us who had a job like babysitting or mowing lawns in the summertime might remember when a new video game was no longer just $50 of Mom and Dad's money, but the equivalent to 10 hours of work. Perhaps you recall hesitating to purchase a soda for $1.50 and opting to visit the water fountain because you were saving your allowance. Prices are just abstract numbers until time and effort has been spent to generate those coins and bills.

To teach your children about money management early on, consider forming an allowance-for-chores policy. You pay for the basics, but if they want the extras, they will have to save up and use their own money. It's an important lesson on its own, but will also help them focus their priorities and feel a sense of pride in accomplishment.

Lesson #2: Saving the money they earn — Teach them to save a portion of what they earn from the get-go. This habit will make it much easier for them to not spend their entire paycheck as well as leave their savings intact when they are on their own. You may need to encourage them firmly at first, with a fixed percentage or minimum amount. As they grow older and their savings increase, they will need less guidance as they come to appreciate the readiness of available funds for a special purchase.

Lesson #3: Setting goals and staying on track — Helping your children set short- and long-term goals is a key part of getting them to stick to a savings strategy. Most children are not that excited by slowly rising dollar amounts, but when a certain dollar amount represents a desperately desired new toy, their focus sharpens considerably. Make a chart to show them how much they would need to save over a specific amount of time to have enough for their goals…and make sure to reward them when they stay on track.

Lesson #4: The nitty-gritty of a balanced budget — Show your children the day-to-day workings of adult finances. Go through the line items on your budget (with real or simplified amounts) and reveal your own percentage of savings for short- and long-term goals. You can explain the benefits of autopay, managing a bank account online, minimum balances and fees, and even how to fill out a check (some landlords and city utilities still require checks for bill payment). It may seem mundane to you, but depending on the child's age, the desire to be grown up could increase their interest level and make abstract concepts more understandable.

Lesson #5: Understanding debt and loans — When young adults are first exposed to credit cards, they may not understand that purchasing things on credit or taking out a loan ends up costing more money. Explaining how interest can work for you (in a savings account) and against you (in a loan or on credit) can keep them from making bad decisions. Above all, modelling financial responsibility in your own life can help them form the basis for a lifetime of good money habits. ❍❍❍

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Financial Data

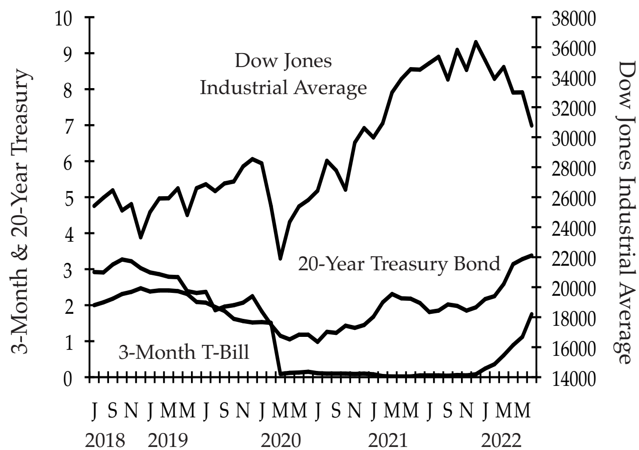
Indicator	Apr-22	May-22	Jun-22	Dec-21	Jun-21
	Month-end				
Prime rate	3.50	4.00	4.75	3.25	3.25
Money market rate	0.08	0.08	0.10	0.07	0.08
3-month T-bill yield	0.89	1.12	1.75	0.08	0.05
10-year T-bond yield	2.89	2.85	2.98	1.52	1.45
20-year T-bond yield	3.14	3.28	3.38	1.94	2.06
Dow Jones Corp.	4.33	4.27	4.80	2.48	2.29
30-year fixed mortgage	4.67	5.30	5.98	2.63	2.44
GDP (adj. annual rate)#	+2.30	+6.90	-1.50	+6.90	+6.30

	Month-end			% Change	
Indicator	Apr-22	May-22	Jun-22	YTD	12 Mon
Dow Jones Industrials	32977.21	32990.12	30775.43	-15.3%	-10.8%
Standard & Poor's 500	4131.93	4132.15	3785.38	-20.6%	-11.9%
Nasdaq Composite	12334.64	12081.39	11028.74	-29.5%	-24.0%
Gold	1911.30	1838.70	1817.00	0.7%	3.1%
Consumer price index@	287.50	289.11	292.30	5.2%	8.6%
Unemployment rate@	3.60	3.60	3.60	-14.3%	-37.9%

— 3rd, 4th, 1st quarter @ — Mar, Apr, May Sources: *Barron's, Wall Street Journal*

4-Year Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

July 2018 to June 2022



Past performance is not a guarantee of future results.

Your 401(k) Contribution Amount

Before deciding how much to contribute to your 401(k) plan, find out three key figures:

What is the maximum percentage of your pay that can be contributed? The maximum legal contribution limit in 2022 is $20,500 plus an additional $6,500 catch-up contribution for participants age 50 and over, if permitted by the plan. However, most employers set limits in terms of a percentage of your pay to comply with government regulations. This limit ensures the plan does not discriminate in favor of highly-compensated employees.

How much of your contribution is matched by your employer? Employers are not required to provide matching contributions, but many do. A common match is 50 cents for every dollar contributed, but many other variations also exist.

Up to what percentage of your pay does your employer match? Most plans only match contributions up to a certain percentage of your pay. For instance, the plan may only match contributions up to a maximum of 6% of your pay.

Assume your 401(k) plan allows contributions up to 10% of your pay annually, with a 50 cent match on every dollar contributed, up to a maximum of 6% of your pay. With a $100,000 salary, you can contribute up to $10,000 to the plan. Your employer will match up to the first $6,000 of contributions ($100,000 times 6%), contributing a maximum of $3,000 (50 cents for every one dollar).

How much should you contribute to your 401(k) plan? If at all possible, contribute the maximum allowed. In the above example, that would be 10% of your pay. At a minimum, contribute enough to receive the maximum matching contribution. That would be 6% of your pay in the above example. Please call if you'd like help deciding how much you should contribute to your 401(k) plan. ❍❍❍

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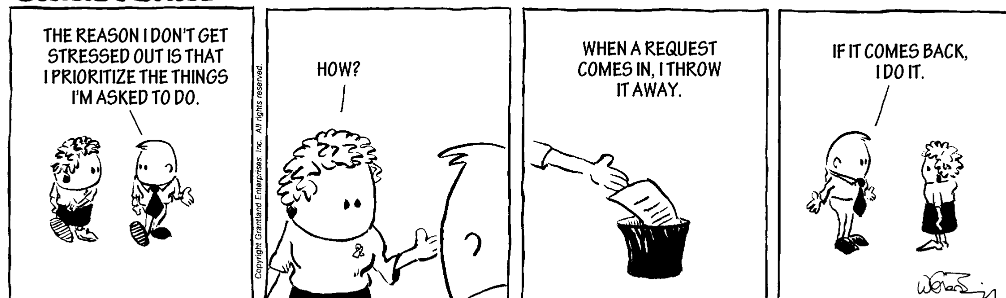

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Indices are unmanaged and investors cannot invest directly in an index. Unless otherwise noted, performance of indices do not account for any fees, commissions or other expenses that would be incurred. Returns do not include reinvested dividends.
The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 actively traded "blue chip" stocks, primarily industrials, but includes financials and other service-oriented companies. The components, which change from time to time, represent between 15% and 20% of the market value of NYSE stocks.
The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. It is a market value weighted index with each stock's weight in the index proportionate to its market value.
The Nasdaq Composite Index is a market-capitalization weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks. The index includes all Nasdaq listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debentures.
The Consumer Price Index (CPI) is a measure of inflation compiled by the US Bureau of Labor Studies