REFLECTIONS

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WINDGATE
WEALTH MANAGEMENT

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To Your Future Prosperity

THE 4% RULE: CAN YOU GET MORE FROM YOUR RETIREMENT PORTFOLIO?

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The dreaded retirement conversation is often avoided, but it doesn't have to be. Seventy-seven percent of adults over 40 don't know how much they can withdraw from their retirement accounts to avoid outliving their nest egg.[1] Here we aim to provide clarity.

Fortunately, determining your safe withdrawal rate isn't as complicated as it sounds. It all begins with a simple, yet often misunderstood, financial rule. It's called the 4% Rule. Let's take a deep dive into exactly what the rule is and its effect on your retirement mindset.

What is the 4% Rule?

When you retire, you're essentially turning your portfolio into a paycheck. The trick is deciding how much that paycheck should be. That's where The 4% Rule comes in. According to this simple rule, when investd with a 60% equity/40% fixed income mix, your retirement savings should last at least 30 years if you withdraw 4% per year, with that dollar amount adjusted upward each year for inflation.

So, if you've saved one million dollars, four percent of your portfolio is $40,000 per year. Add in $20,000 (for example) of Social Security, or any other income, and you have a total of $60,000 to live on in retirement (adjusted for inflation each year). Compare this income estimate to your expected living expenses and you have an idea if your portfolio can sustain your retirement.

INSIDE THIS ISSUE

If you know of any friends or family that might benefit from our services, please give us a call at 844.377.4963

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You can log-in to your personal financial website at www.windgatewealth.com by going to the "see all accounts" tab

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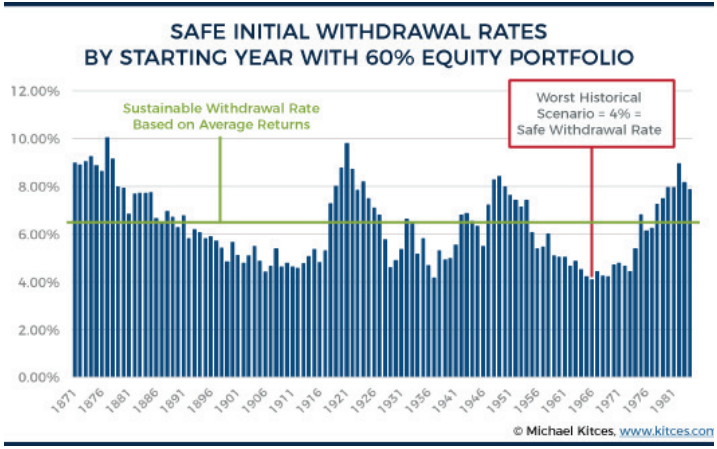
What if the Market Provides Below Average Returns?

It's a common concern that as soon as you stop earning money, your investments will lose value or suffer a long period of poor returns. This concern is wholly understandable. It takes a major leap of faith to stop making money from your work and to trust that your portfolio and the markets – which are essentially out of your control – will carry the load. However, while past performance never guarantees future results, a bit of historical background on the 4% rule may help you rest easy.



The 4% safe withdrawal rate is not based on historical averages, it is based on historical worst-case scenarios.

This is in fact the point of the 4% rule being a safe withdrawal rate. Retirees who took out 4% each year in retirement still had money left over 30 years later if they retired on the eve of the Great Depression, the stagflationary 1970s, or any other terrible period throughout market history.

When we sit down with retirees we can't know ahead of time if the next 30 years will be more like the best periods, the worst periods, or the average. So, the purpose of the safe withdrawal rate is to simply assume that every period might turn out to resemble the worst.

Significant Upside of the 4% Rule

When you plan your retirement to occur during the worst-case scenario, the result is that you will most often end up pleasantly surprised. In fact, over 90% of historical 30-year retirement periods result in significant growth of wealth during retirement, even while withdrawing 4% each year. Using this safe withdrawal rate approach, two-thirds of the time the retiree finishes with more than double what they started with, and the median wealth at the end of 30 years is almost 3x starting principal. Of course, the past doesn't predict future results.

1 https://money.cnn.com/2018/01/18/retirement/4-rule/index.html

How Can I Get More than 4%?

Your retirement planning is not something to put on Autopilot. Although the 4% rule was designed as an easy way to set a static withdrawal rate that will last through retirement, it is also far from efficient, as we have seen. After all, if the goal of retirement is to safely turn your portfolio into a paycheck, you also don't want to pay yourself too little and sacrifice quality of life during your golden years.

Based on average returns (including dividends) for a balanced account dating back 140 years, an initial withdrawal as high as 6.5% will last 30 years in retirement. Now we surely wouldn't advise you to begin retirement taking 6.5% from your portfolio and hope for average returns over the next three decades (after all, average returns means you would run out of money 50% of the time). But there *are* ways to confidently increase the safe withdrawal rate above 4% when needed.

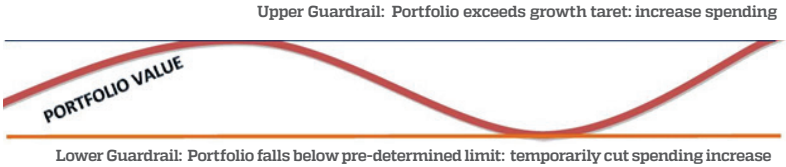
As we have seen, the possibility for portfolio growth to exceed a 4% safe withdrawal rate is very real. The best way to safely and confidently withdraw more than 4% is to develop a process of ongoing adjustments to your portfolio and income stream. Specifically, there are three key elements: 1. Guardrail Strategy, 2. Withdrawal order and asset allocation, and 3. Portfolio design and rebalancing

1. The Guardrail Strategy

What if you could follow a conservative plan based on the 4% rule and still be able to increase spending during bull markets? Well you likely can, if you follow the rules of the Guardrail strategy.

The 4% safe withdrawal rate is not based on historical averages, it is based on historical worst-case scenarios.

When following the Guardrail strategy you vow to follow a set of pre-determined rules which influence the amount you can withdraw from your portfolio each year. If your portfolio value declines to a point which threatens its long-term viability, your following year's withdrawal is reduced by 10%. Conversely, should your portfolio grow above a certain threshold, your planned withdrawal is increased, and your portfolio income is given a "raise."



Historically, adding this pair of decision rules to a retirement scenario allowed for an initial safe withdrawal rate higher than 4% in all previous retirement periods lasting 30 years. That does not guarantee that history will repeat itself, but it does make a strong argument that ongoing monitoring of your retirement plan can add significant value. By committing to the upper and lower "guardrails," you can ensure that your withdrawal rate efficiently matches the reality of your retirement situation. There is a drawback: you must cut back spending during times when the lower guardrail is met. However, in practice this tradeoff is more than offset by the higher initial safe withdrawal rate obtainable.

2. Withdrawal Order and Asset Location

Most retirees have multiple accounts including IRAs, 401(k) Rollovers, Roth IRAs and/or taxable brokerage accounts. Knowing which accounts to withdrawal from, and when, can help you save on taxes and increase the overall longevity or your portfolio. According to a Vanguard study,[2] advisors who create a strategic withdrawal plan for their clients can add up to 1% in annual value over the course of retirement.

There is similar value to be gained in "asset location," which is the answer to the question "what investment goes where?" Knowing which account to use for dividend-paying stocks versus higher-turnover investments, for example, can again minimize taxes and increase portfolio longevity.

[2]Quantifying Vanguard Advisors' Alpha, September 2016

3. Portfolio Design and Rebalancing

Investment principals don't get any better than "buy low, sell high." Yet this idea is much easier said than done. This is simply because it is natural for investors to feel fear and greed and to buy or sell investments accordingly – often to their own detriment.

A better approach is to invest not based on emotion, but according to a disciplined process guided by rebalancing. The sketch below illustrates the idea simply. Start with a general asset allocation target that aligns with your risk tolerance. Then take what the market gives you: if an investment rises, sell a little; if it declines, buy a bit.

Next Steps

The 4% Rule is a simple calculation to help make sure your retirement savings last. But as we've seen, it is far from a one-size fits all strategy. You can very likely gain more clarity and income with your own individualized retirement planning. Give us a call at (844) 377-4963 or email windgate@windgatewealth.com and we would love to help.

Michael Corbett,
Chief Investment Officer
Portfolio Manager

YEAR IN REVIEW

Following 2017, a year where practically *everything* worked, 2018 was disappointing and investors felt that *nothing* worked. In 2018, cash outperformed every type of asset class; stocks, bonds, and commodities. When all was said and done, the S&P 500 Index posted its worst year since the 2008 financial crisis, putting an end to a remarkable streak of nine straight years of positive returns.

There is a reason why investors earn a premium for investing in equities versus safer investments, like Certificate of Deposits: the acceptance of risk and volatility. U.S. large-cap stocks dropped 9% in December and fell just shy of a bear market (20% decline) from their late September high. Smaller-cap U.S. stocks fell more sharply, losing 20% in the fourth quarter and 11% for the year.

The contrast between the losses of 2018 and 2017's strong market results is striking, and it serves as a useful reminder of the unpredictability of markets. In 2017, the maximum decline during the year was just -2.8% in the month of March – one of the lowest intra-year losses in history – and for the first time ever there wasn't a single down month the entire year. There are many possible explanations for 2018's market swoon: a detrimental trade war, interest rates rising too fast, the possibility of a recession, and so on.

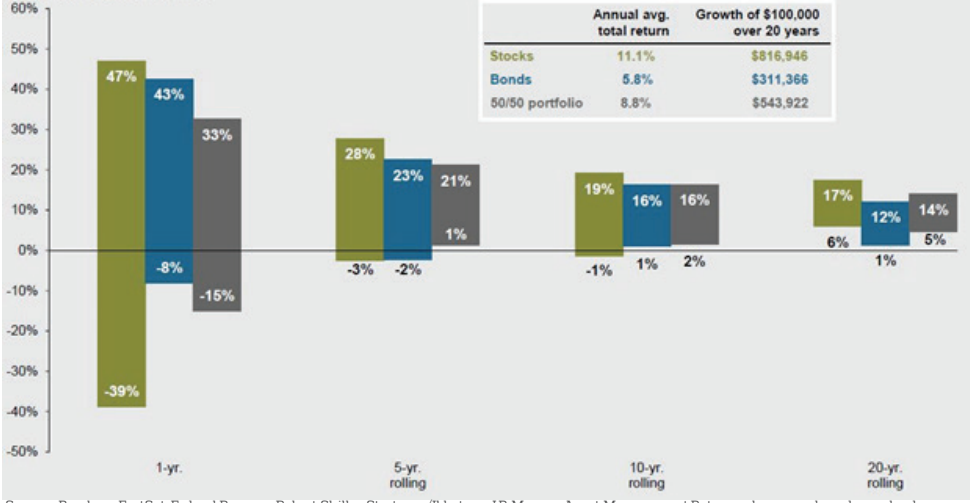
Time Heals All Wounds

Because drawbacks are a normal part of investing, it can be helpful to see through the noise and focus on longer term results. We are including the same chart we shared last year, updated for 2018. Despite the difficult year, the results are nearly unchanged. The chart shows how history suggests disciplined investors are unlikely to suffer large losses over longer periods. The bars represent the range of "rolling returns," that is the average annual return for the holding periods listed below (1-year, 5-year, 10-year, and 20-year).

As you can see, the range of possible outcomes narrows significantly as your holding period increases. While one-year stock returns have varied widely since 1950 (+47% to -39%), a blend of stocks and bonds has not suffered a negative return over any five-year rolling period in the past 67 years.

Range of Stock, Bond and Blended Total Returns

Annual total returns, 1950-2018



Source: Barclays, FactSet, Federal Reserve, Robert Shiller, Strategas/Ibbotson, J.P. Morgan Asset Management.Returns shown are based on calendar year returns from 1950 to 2018. Stocks represent the S&P 500 Shiller Composite and Bonds represent Strategas/Ibbotson for periods from 1950 to 2010 and Barclays Aggregate thereafter. Growth of $100,000 is based on annual average total returns from 1950 to 2018.

The last two years were nothing alike and gave investors vastly different experiences. While painful, it can be a good thing to experience such a sea change in market environments because it offers you a chance to assess your behavior across different situations. It's a good time to reflect and ask yourself: was the risk in your portfolio appropriate? Did you stick to your plan? From our perspective, we kept to our process of maintaining your portfolio via rebalancing and diversifing asset-allocation as the market dictated. Difficult periods in the market are a natural with required tradeoff along the road to building sustainable wealth over decades.

S&P 500 Index is a market capitalization-weighed index of the 500 largest U.S. publicly traded companies by market value. The index is widely regarded as the best single gauge of large-cap U.S. equities.

STEPS TO AN A+ COLLEGE PLAN

There's one key chapter missing from What to Expect When You're Expecting, and it plays to the tune of over $100,000: the cost of your child's college tuition. Regardless of whether your child is two or twelve, it can be all too easy to put saving for college on the back burner. But one thing in life is certain; it moves quickly. Don't get caught unaware and unprepared for college. Your child's education is one of the most important investments you can make, and with today's costs, it pays to plan ahead.

Have you started saving for your child's future education costs? If you haven't, it's time to consider these four steps.

Step 1: Know What to Expect

College tuition gets more expensive every year. Tuition rates have increased at a faster pace than many other items over the past decade and it doesn't look like they will slow down anytime soon. Over the past ten years, college costs have risen an average of 2.4% a year for private schools and 3.5% for public colleges.

	Private Nonprofit Four-Year	One-Year % Change	Public Four-Year	One-Year % Change
2006-07	$26,380		$6,860	
2007-08	$27,060	2.6%	$7,150	4.2%
2008-09	$27,150	0.3%	$7,220	1.0%
2009-10	$28,760	5.9%	$7,900	9.4%
2010-11	$29,550	2.7%	$8,420	6.6%
2011-12	$29,700	0.5%	$8,820	4.8%
2012-13	$30,450	2.5%	$9,080	2.9%
2013-14	$31,040	1.9%	$9,150	0.8%
2014-15	$31,600	1.8%	$9,240	1.0%
2015-16	$32,600	3.2%	$9,500	2.8%
2016-17	$33,480	2.7%	$9,650	1.6%

If this upward trend continues, in 25 years it could cost $300,000 to obtain a four-year undergraduate degree. The costs will vary depending on the institution attended, room and board, and other educational expenses, but either way, that's a large sum for four years of school. For a 2017 graduate, the average student loan balance was over $37,000 and the average monthly student loan payment is $351. That is a large burden for someone just beginning their career, but it can be prevented with good planning

Step 2: Start Saving

It's never too late or too early to start saving for your child's college fund. By starting early, you can reap the rewards of compound interest. Even if you are starting late, think in relative terms: today's late start is still an early opportunity in the eyes of your future-self, looking back.

Even if you don't think you have enough room in your budget to add another line item, $50 a month is still $50 more than $0. Setting up automatic contributions is a good way to remind yourself that college is getting closer and your monthly account statement will keep this goal in the forefront of your mind.

Step 3: Decide How You'll Save for College

The most common method people use to save for college is through a 529 plan. A 529 plan is a state-sponsored education savings account that allows earnings to grow tax-free. This means that 100% of your growth can be used toward the tuition and is not whittled away paying annual taxes, which can have a large impact on the bottom line.

There are two categories of 529 plans: prepaid tuition plans and college savings plans.

Prepaid plans let you pay future tuition costs at today's prices, which, considering skyrocketing college costs, can be enticing. However, prepaid plans are more limiting because funds can only be used for in-state schools.

College Savings 529 plans, on the other hand, can be used to pay for college in any state (and thanks to new rules in the 2017 tax reform, 529s can now be used for private elementary schools, up to $10,000 in distributions per student each year). As an added benefit, some states (including Illinois) give you a state tax credit for using their plan.

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Section 529 Plans are sponsored and administered by states, meaning that you may have less flexibility and choice regarding investment options, depending on the program. However, you are not required to use the plan offered by the state that you live in, so you are free to shop around. Visit www.collegesavings.org to understand your state's policies.

Beyond 529 plans, some families use Roth IRAs to save for college. Your Roth contributions can be withdrawn at any time and can be used for any purpose. In addition, Roth IRAs can help you avoid the high fees that some 529 plans charge and they also offer virtually unlimited investment options. IRAs will also not have any impact on your financial aid eligibility.

For college savings, Roth IRAs aren't the perfect option, as their primary goal is to fund your retirement (consider that while student loans are always a possibility, there is no such thing as a retirement loan). But Roth IRAs do offer an alternative (or supplement) to the traditional 529 plans. Think about opening a 529 plan for college, but also continuing to contribute to a Roth for retirement. This strategy gives you extra resources to draw on if you need them

Step 4: Stay On Top of things

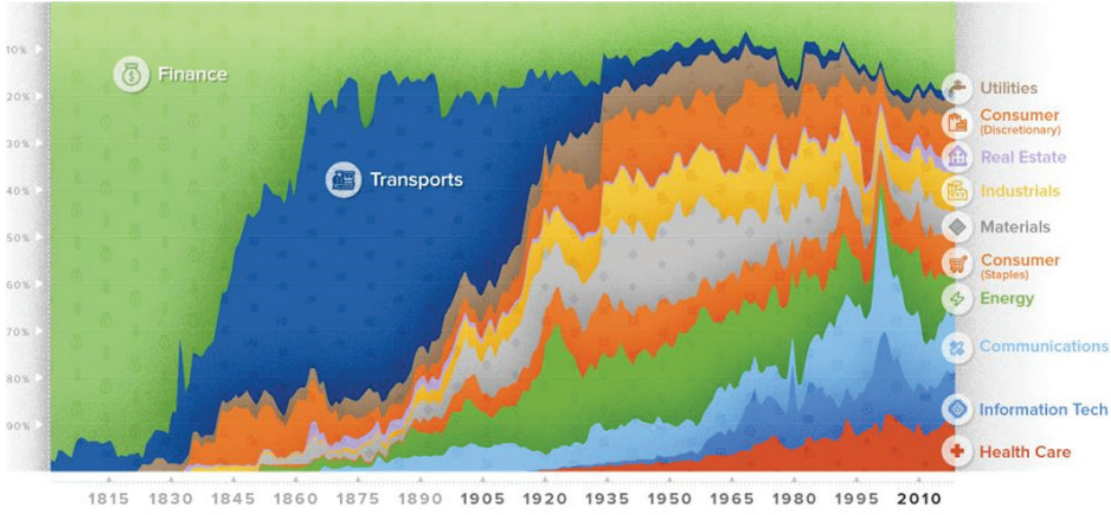
Just like your 401(k) plan, you need to monitor your college planning investments. While in the early days of saving for college you will want to be more aggressive with your investments. As college draws closer, the investment allocation should become more conservative, just like a retirement account. It is also helpful to monitor your balances, keep an eye on the changing college costs, and track your progress towards your goal.

Jumpstart Your College Planning

Let us help you prepare for the future. With our guidance and expertise, you can start saving for your child's future today so you can ease the worries of tomorrow. To get started, you can reach us by calling (844) 377-4963 or emailing windgate@windgatewealth.com.

VISUALIZING 200 YEARS OF INVESTMENTS IN U.S. STOCK MARKET SECTORS

Below is a fascinating look at how stock market sectors have changed over time. There are some takeaways: railroads were the dominant investment in the late 1800's and the tech boom of the 1990s was extreme even on a multi-century scale. Above all, it serves as a reminder how markets are unpredictable and constantly undergoing change.



Source: Visual Capitalist

WINDGATE
In The Community review

Windgate Wealth Management is committed to giving back to the communities in which we live and work. We aim to make an impact by investing our resources – financial contributions, employee volunteering, and mentoring to support outstanding charities, such as those we've highlighted below that we have been involved with since 2017.

Erika's Lighthouse
A Beacon Of Hope For Adolescent Depression

Erika's Lighthouse: A Beacon of Hope for Adolescent Depression is a not-for-profit organization dedicated to educating and raising awareness about adolescent depression, encouraging good mental health, and breaking down the stigma surrounding mental health issues.

Wasmond Center-Little Angels History

In 1958, Pat Wasmond, a registered nurse and mother, was working in a local doctor's office. This doctor had a child who had severe disabilities, requiring 24 hour care. Her family had difficulty managing this challenging situation. Pat offered her assistance and the child came to live with Pat, Bob and their children.

Word spread in the Elgin area of this exceptional family and the wonderful care this child was receiving. Soon the Wasmonds began receiving calls from other families seeking this kind of help.

NMIA, A Neighborhood Event

In 1929, the North Mayfair Improvement Association (NMIA) was formed after most homes were built, railroad tracks were laid, and Elston Avenue was paved. Residents of North Mayfair wanted an Association that would promote the community's vibrant potential while working with government agencies to continue to improve streets and build a grammar school. The mission statement of NMIA was simply stated in the bylaws, "to improve North Mayfair". Several years later, NMIA began publishing a neighborhood newspaper, *The Improver*, which is still published 4 times a year.

Big Shoulders Fund®

Stacie Suhrbur of Windgate Wealth Management and Kathy Schutz of Perritt Capital Management work with the Stock Market Program which brings business professionals into eighth grade classrooms to teach basic concepts related to the stock market, investing, and careers in business. Under the leadership of Big Shoulders Fund Directors Charlie Bobrinskoy and Jim Hoeg, students in the program build a virtual portfolio tied to actual financial incentives for their school. Starting with 3 schools back in the 2008-2009 school year, the program has expanded to 62 schools for the 2017-2018 school year.

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