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# Retirement Planning Insights

*(special edition)*

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# Special Update

## My thoughts on COVID-19's impact on retirement planning and investment portfolios

I sincerely hope you and your family are healthy and coping as well as possible given our country's current state of normal. Even if most of us never get COVID-19, it will inevitably affect us all in one way or another. I'd like to share my thoughts on how it has thus far affected our financial lives.

Just a month ago, the major U.S. stock markets were at or near their all-time highs. As of today, those indices have since dropped about 30%. And I suspect further decreases are likely. However, the current turmoil will eventually end and markets will rebound. Though admittedly I have no idea how long the current problems will persist or how bad things will get during that time.

It's now clear to the entire world how serious of a global health crisis the COVID-19 virus is. It's also clear that the only way to minimize its potential impact is to shut down large swathes of the economy. This is nothing short of catastrophic for the affected industries, companies and employees.

I have zero medical credentials, so I won't pretend to know anything about the virus above and beyond what I read in the news. Though I'm confident in saying it's logical to believe it will eventually be under control. Maybe it will take a month, maybe it will take a year, maybe it will take longer. But if the recently announced progress in slowing the virus's spread in China is any indication, the rest of the world should be confident there will indeed be an end.

Once the virus is sufficiently contained, people will again go about their normal lives, businesses will reopen and rehire, the economy will throttle back up and stock markets will recover. In the meantime, I feel the adverse economic impacts of COVID-19 will be very real and very bad. But I'm also of the opinion that the worst of the fallout should be relatively short-lived.

I believe all clouds have a silver lining. With that said, I'd like to share some ideas on how our financial lives could benefit from an otherwise terrible situation. The current financial turmoil is teaching us some very important financial planning lessons. Additionally, there are some potential opportunities to take advantage of right now.

***Lessons to learn***

**An emergency fund should be a top priority**

The speed with which the virus and its economic impacts are jeopardizing many peoples' jobs is unprecedented. While it may now be too late for those

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whose job was already eliminated, the lesson for future planning is very important.

Make sure you have enough cash on-hand to cover AT LEAST 3-6 months of expenses. There is no science behind whether 3 months, 6 month or 12 months is the right number; it will depend on your own personal circumstances. For example, if you are in a two-income household and lose your job, you may not need as much emergency fund as if you are the sole income provider.

The cash you keep in your emergency fund should be 100% safe with no risk of loss. This means it should be kept in a checking account, savings account or a certificate of deposit. Interest rates on such products are jokingly low, but you should view that as the price to pay for the certainty of keeping your money safe.

If you're a retiree, job loss may not be a concern as you presumably have since stopped working. And hopefully you already have a good income plan in place consisting of a combination of Social Security, pensions, annuities, investment portfolio withdrawals, rental property income, etc. However, this doesn't mean you don't need an emergency fund. But you likely don't need as much as someone who is still financially dependent solely on wage income.

**Stocks are risky and don't always go up**

It's been 11 years since the depths of the 2008/2009 financial crisis. Since then, stock markets have basically had a steady march upward, particularly in the U.S. For example, the S&P 500 had a total return of approximately 13% per year over the last 11 years.

Even though most people are aware of the risks of over-allocating to stocks, the fear of missing out - and maybe a little greed - make it hard to NOT over-invest in stocks when stocks seem to only go up. But, in just the last month, the S&P 500 has given up its last THREE YEARS of gains.

If you are investing money you plan on needing in the next few years, the money should most likely not be invested in stocks. On the other hand, if you are investing money you don't anticipate needing for many years, stocks are generally a wise investment and do typically go up over the long-term.

However, when investing in stocks, diversity is EXTREMELY important. Single stocks can dramatically drop in price or even disappear completely like the ill-fated Enron or Lehman Brothers. Even the broader stock market of an entire country can struggle for a prolonged period. For example, Japan's Nikkei 225 is still below the record high it reached in 1989…

If you're a retiree, even if you're already taking distributions from your nest egg, you probably should still have a portion of your portfolio in stocks. Retirement is likely to last multiple decades. As such, even if you're already retired, you still have potentially 20 or 30 years of investment horizon for some of your money.

The concept mentioned above about matching your investment horizon to your investments holds true for retirees just the same as non-retirees. The money you expect to need in the next few years should probably not be invested in stocks. But the money you don't plan on touching for many years should be at least partially invested in stocks.

**Nobody can predict the economy or the financial markets**

I don't know who first said it, but one of my favorite quotes about economics goes something like this: "economists predicted nine out of the last five recessions." There will always be professionals who preach the next big downturn is right around the corner.

For every highly educated and highly credentialed expert who makes a compelling case that X is going to happen, there is another equally educated and credentialed expert who makes an equally compelling case that X is NOT going to happen.

In hindsight, it's easy to say what happened and why. And for those who were lucky enough to be on the right side of a big economic or stock market prediction, fame and notoriety are likely to follow. But for every newly minted oracle whose prediction came to fruition, there are scores more who got it wrong and sit quietly in the shadows, often unbeknownst to the public.

I'm not saying we should give up on trying to make sense of the current situation in the global markets. But we need to acknowledge that understanding the financial markets is as much art as it is science. This is especially true in times of stress and turmoil where historical precedents, rationale and fundamentals often go out the window. With that said, we can't get too hung up on listening to the talking heads and pundits in the financial media.

For retirees, it can be especially hard to acknowledge there isn't much which can be done about the unknown. That's why proper retirement income planning is so important. The more of your income that comes from stable and secure sources like Social Security, pensions and annuities, the less you need to expose your future to the risks and unknowns of the financial markets.

## ***Opportunities to take advantage of***

### Consider refinancing your mortgage

Many interest rates are at or near historic lows. Mortgage rates are no exception. While there is no hard and fast rule for when you should refinance, if you are able to get a new annual interest rate that is at least 0.5% lower than your current rate, it may be worth considering.

The ongoing interest savings is the main reason to do a refinance. But don't look only at how much lower your monthly payment can be; refinancing comes at a price. It could cost you thousands of dollars up-front to refinance your loan. Typical refinancing costs include underwriting fees, appraisal fees, administrative fees, new title insurance and "points." Points are a one-time lump-sum interest payment you make at the origination of the new loan to buy yourself a lower ongoing interest rate.

Many retirees no longer have a mortgage, so this may not apply. But if you're retired and do have a mortgage, a refinance is worth looking into just the same as if you weren't already retired.

### Consider doing a Roth conversion

Since stock prices are quite depressed from where they were a month ago, now could be a good time to "convert" some of your investments from your traditional IRA to a Roth IRA.

A Roth conversion involves moving money or investments from your tax-deferred retirement account to a Roth account. Once in the Roth account, investments will grow tax-free and generally come out tax-free after you reach age 59 ½. However, you will need to pay ordinary income tax on the full amount of the conversion in the year of the conversion.

As further discussed in my **October 2019 newsletter**, there are various benefits to doing Roth conversions. In the current financial environment, while we're in the middle of a significant stock market slump, you can get more bang for your buck from a conversion. For example, if you were to convert 100 shares of stock at $10 per share, you would have to pay income tax on a conversation amount of $1,000. If those shares now only cost $7 each, you can convert the same 100 shares and only have pay income tax on $700. Furthermore, if/when the stock rallies back to a price of $10 or beyond, you'll have saved tax on the $300 or more of gains which would have otherwise been taxable had you left the shares to eventually be liquidated out of the tax-deferred account.

Conversions could be just as beneficial for retirees as non-retirees. Regardless of your stage of life, the goal and benefit is the same - to help minimize income taxes over the long-term.

Doing a Roth conversion involves paying income tax on the conversion in the year you do it. Therefore, conversions require careful tax planning before taking any action. Talk with you financial or tax professional before doing a conversion.

**Consider buying stocks (ONLY IF YOU HAVE THE AVAILABLE CASH, RISK TOLERANCE AND TIME HORIZON*)***

As I mentioned before, no one knows when the stock markets will hit their bottoms. But I'm confident in saying the virus will eventually get under control, the economy will steam back to life and stock markets will recover. Maybe it will be couple months or maybe it will be a couple years. Either way, a lot of stocks have been indiscriminately sold off from a combination of weaker fundamentals, uncertainty, panic and fear.

Some companies may never recover from the current crisis, but most will. There will inevitably be heightened market volatility until the virus and its economic impacts get under control. And I suspect both the virus and the financial markets will get worse before they get better. But from a long-term perspective, I feel now could be a very good time to buy into certain parts of the stock market at great prices.

For many retirees, plowing more money into stocks is not likely to be prudent advice. This is especially true for retirees who already heavily rely on distributions from their portfolios. But if you're a retiree who is in the fortunate position to be unlikely to need most of your nest egg and therefore will end up eventually passing it on to your children, charities, etc., now could be a good time to take advantage of some discounted long-term growth opportunities.

If you have any questions about COVID-19's impact on the financial world and what it means for your retirement planning, don't hesitate to contact me at **andy@tenonfinancial.com** or 732-902-0066. Thanks!

-Andy