Is Living Off Shares A Realistic Retirement Strategy?

Description

It is the goal of many people to retire at a relatively young age and then live off the income from investments. For many retirees, shares form the backbone of their retirement portfolios. In the long run, they are expected to offer high returns and can offer above-inflation income opportunities in many cases. However, is the idea than an investor can retire and live off their shares simply unrealistic? Or, is it possible to own a diverse range of stocks and lead a comfortable retirement?

Return potential

As mentioned, the returns on shares generally exceed the returns on all other mainstream assets in the long run. Holding assets such as cash, bonds and even property is likely to mean a lower terminal value than if the cash had been used to buy a diverse range of stocks. Therefore, in the long run it seems logical to invest an entire retirement portfolio in shares. After all, it is likely to lead to a higher valuation and potentially more spending power in the long run.

Volatility

However, the main problem with shares is their volatility. At the present time, global stock markets are generally high. Therefore, investing in shares probably seems to be a sound idea to most people. The reality, though, is that a bear market will inevitably surface at some point in future. No stock market has ever risen in perpetuity, and so there will be a fall in the value of portfolios which are dominated by shares at some point in future.

Of course, the same could be said for most assets, but perhaps the difference with shares is that they are more volatile than other assets. For example, bond prices do not usually fluctuate to the same extent as share prices. Similarly, property valuations tend to move much more gradually than share prices, while the real value of cash is often only eroded gradually by inflation.

This high volatility can present problems to retirees – most of whom seek a reliable, stable and consistent income with which to enjoy their retirement. If the value of their portfolio is rising and falling dramatically, it may cause worry regarding its future valuation and the potential for a fall in income returns in the short run.

Pragmatism

Due to the volatility of shares, it may be prudent for retirees to keep a portion of their portfolio in lower risk, less volatile assets such as short-term bonds. They may offer lower returns than shares, but they may also provide more stability and greater liquidity. This should ensure that a retiree has sufficient cash with which to survive in the short run in case share prices and dividends decline. And in the long run, they are still likely to benefit significantly from the capital growth and income return which shares have historically provided.

As such, the idea of living off shares in retirement is a realistic strategy to adopt. However, a consideration for short-term cash flow must also be factored in.

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