Avoid a Polly Shortts Moment

Even for those who have not run the Comrades Marathon, the name Polly Shortts is well known. It is a mere two-kilometre stretch of fairly steep tar on the outskirts of Pietermaritzburg. On the up run it arrives some eighty kilometres into the ultramarathon, with about seven still to go.

Few outside the elite participants summit it running. Most have to walk.

But then there are those who are simply undone by the last of the Big Five, even though many still felt good at the halfway stage. For these runners, it's what happened in the opening hour or two that determines the last stretch.

The up run is front-loaded, with three of the Big Five inside the first thirty-seven kilometres and more than five hundred metres of ascent in the first twenty-two. However, early in the race, the legs are willing and the crowds are loud, leading many runners to overreach. But that "banked time" is a loan, and Polly Shortts is where it is called in.

The parallel with retirement drawdowns

In 1994, the US financial adviser William Bengen ran some calculations to determine how much a retiree could safely draw from a portfolio each year. His answer: four percent. This number has been widely quoted, and is known as the Bengen rule.

What is less often quoted is how he arrived at it. No single market crash set the limit. One cohort did, the retirees of the late 1960s, who met weak markets and high inflation simultaneously in their opening "kilometres". They could sustain 4.15%, and everyone else could have afforded more. The rule was written by the unluckiest runner in the field.

That is sequencing risk. Two retirees can earn identical average returns over thirty years and finish in entirely different places, purely because of the order in which those returns arrived.

The maths is fairly settled and translates well into the South African environment. South African living annuity holders may draw anything between 2.5% and 17.5%. The industry average sits at approximately 5.6%. But what tends to derail a sensible drawdown rate is not necessarily arithmetic. It is behavioural. Many retiring into a strong market with 15% to 20% gains, similar to what we have experienced over the last three years, may feel justified in materially increasing their drawdown rate.

Like the elevation profile of the Comrades marathon, returns from investments are not evenly distributed. At some stage every investor will face a Polly Shortts moment, and those who pull through strongly will be the ones who kept something in reserve for the tougher stretch.

The runners who finish Comrades are not the strongest in the field. They are the ones who chose a pace before the gun and stayed unmoved by how good they felt at halfway. Retirees would do well to manage their drawdown levels the same way.

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If you have any questions, Ian and our team would love to hear from you on investmentteam@seedinvestments.co.za.