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A Quarterly Newsletter for Homestead Funds' Shareholders

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You're Retiring (Your Portfolio Is Not)

With the growing trend of self-funded retirement accounts, retirees are more in control of their financial future than ever before.

Yet, that control comes with the responsibility of making key choices. While it can feel complex, it can actually be quite simple. And while you may be retiring, your portfolio is still hard at work to support you in your golden years.

The Downsides — and Upsides — of a Low-Rate Environment

Retirees have historically turned to bonds in retirement, both for the steady interest income and the lower-risk profile. The bad news is that with record-low rates, it's just not feasible to have 100 percent of your portfolio invested in bonds and expect your money to last as long as you need. More bad news for risk-averse investors: low rates are likely to be here for a while. Interest rate policies generally track inflation, which is low today and tends to be "sticky," that is, to stay within its range for long periods.

But is this *all* bad news? Low rates are great for anyone carrying a mortgage. While many rush *(continued on page 2)*

The Power of Perseverance

A number of us are just back from NRECA's INTERACT Conferences, and we are very pleased to have been a part of these thoughtful and vibrant sessions. For me, one of the highlights was participating in a panel discussion, along with colleagues from National Rural Electric Cooperative Association (NRECA) and the National Rural Utilities Cooperative Finance Corporation (CFC), where the questions put to us by benefits administrators centered on today's challenging markets. How does the election year affect retirement investments? What happens when interest rates go up? What should investors do when markets are volatile?

These short-term issues can be nerve-racking. But, when it comes to planning for retirement, the surprising truth is that the actions of the saving individual — you — are much more powerful over the long term than any headline blip for stocks, which is why another question really stuck with me: **What one piece of advice would you have for an employee looking to increase the "success factor" of his or her portfolio?**

My answer is: **payroll deductions.** A tool that automates saving decisions will sidestep so many of the things that block savers from being successful — our procrastination, our emotions, our budgets, even just being overwhelmed by all the small details.

The path to retirement is entering a new era. With the growth of retirement accounts like 401(k)s and IRAs, workers and retirees are in the driver's seat more than ever before. While this comes with benefits, it can also feel overwhelming — a daunting and distant challenge. But for most of us, reaching a significant financial goal is the result of many small decisions, applied consistently over a period of time. Or, as better said by the legendary football coach Vince Lombardi, "Inches make champions."

Stephen Kaszynski, CFA
Director, President and CEO

So in this issue, we take a deep dive into the topic of retirement. You, as workers and savers, have the power to make choices that are right for you, your family and your lifestyle. Read on for more tips on some of the key decisions — including strategies for managing distributions and options for growing your accounts. You can also visit us online for more resources. Just look for the search bar and type "retirement."

Homestead Funds

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to pay off mortgages before retirement, low rates could bolster the case for keeping a mortgage while allowing a higher dollar amount to grow in investment accounts.

More good news about that low inflation: It offers a leg up for anyone living on a fixed income — like retirees. High inflation can eat away at savings quickly.

Portfolio Growth Is Still Key

While conservative bonds are crucial for buffering inevitable market downturns, most retirees still need some mix of stocks for growth. After all, today's retirees expect to live an average of 28 years in retirement.[1] For savings to support you over decades, you need some investment upside.

Stocks can also provide income from dividends, although at a lower rate than bond income. The average dividend yield for the S&P 500 is between 1 percent and 2 percent, and dividends are usually taxed at a lower rate than bond income.

Savvy Steps for the Distribution Phase

When you begin taking distributions from investment accounts, you have to make a few decisions about when and how to access savings. Here are a few guidelines to help you plan:

1. **Tap taxable accounts first.** For the average person, it's best to spend out of taxable accounts first. The longer you can let tax-deferred assets grow, the bigger the benefit, plus you'll lower your taxable investment income at the same time.

2. **The 4 percent rule is a good starting point.** For portfolios invested in a mix of stocks and bonds, statistical modeling suggests you could withdraw about 4 percent of assets each year and have a very high probability that your portfolio will last 20 – 30 years in total.[2] But this is just a starting point. If you expect to rely on your savings for longer than average, or if you have a very conservative mix of investments, plan on taking less. If you have other long-term sources of income, you might be able to take a little more.

3. **Don't take out too much too soon.** The most common mistake our financial planners see is that retirees withdraw too much right when they retire, often anxious to pay off a mortgage or other debts. But depleting accounts means that those assets can't keep growing to support you in years 10, 15 or 20.

4. **Watch for and plan Required Minimum Distributions (RMDs).** While we recommend spending taxable accounts first, you also have to be mindful of the RMD rules. Those apply to investors age 70½ and older who have money in tax-deferred retirement accounts like IRAs and 401(k)s. The IRS penalty for not taking at least the required amount is substantial — 50 percent of the amount you should have taken. Another consideration is that investors with substantial assets in tax-deferred retirement accounts who have deferred distributions may be looking at a hefty income tax liability when they do take their RMD.

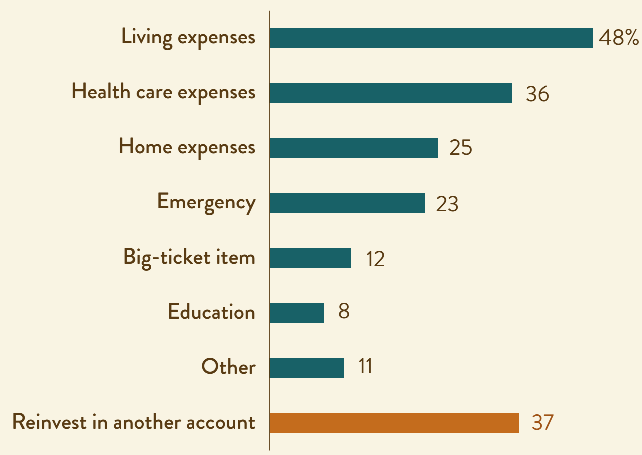
Retirees Can Save, Too

Many retirees are surprised to find that their retirement costs are lower than expected, and they even have cash flow to save. But, you need to have earned income in a calendar year to be eligible to contribute to 401(k)s or IRAs.

Retirees who continue working in retirement may still be able to save in a tax-advantaged retirement account. For the rest, you can always consider putting extra dollars into education accounts for grandchildren, or save in a regular taxable investment account (see figure below).

Many IRA Investors Reinvest Some of Their IRA Withdrawals

Use of withdrawal, percentage of withdrawing retired traditional IRA-owning households, 2015



Source: Investment Company Institute IRA Owners Survey.

While Your Portfolio Works, You Can Relax

A thoughtful mix of investments and a savvy approach to distributions are the key ingredients to good financial management in retirement. These two elements position your hard-earned savings to keep working, long after you've retired.

[1] Collinson, C. (2015). *The Current State of Retirement: Pre-Retiree Expectations and Retiree Realities:* 10. Transamerica Center for Retirement Studies. Retrieved from www.transamericacenter.org.

[2] Bengen, W. P. (1994). "Determining Withdrawal Rates Using Historical Data." *Journal of Financial Planning* (October): 171 – 180.

Retirement by the Numbers

62

IS THE MEDIAN AGE OF RETIREMENT AMONG CURRENT RETIREES

But those age 50+ who are still working expect to retire at 67. Nearly 70% of age 50+ workers are planning to work past age 65, or do not plan to retire.[1]

60%

OF RETIREES RETIRED SOONER THAN PLANNED

But not always by choice. In a recent survey, retirees cited several reasons for retiring early:[2]

Employment reasons: layoffs, reorganizations, early retirement buyouts or job dissatisfaction — 66%

Poor health or family responsibilities — 38%

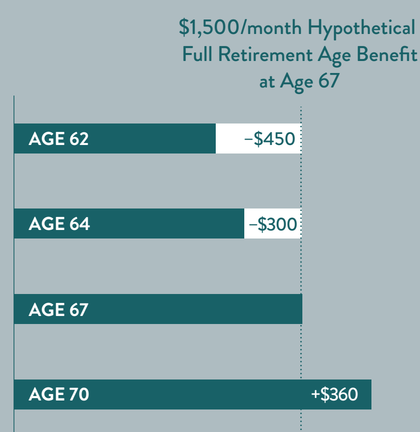
Realized they were financially able to retire — 16%

77%

HIGHER ESTIMATED MONTHLY BENEFITS, between starting Social Security at 62 (at a discounted rate) versus 70 (at a bonus rate)[3]

Hypothetical monthly Social Security benefits for a 55-year-old who is projected to receive $1,500/month at 67 (Full Retirement Age)

However, taking benefits at 70 instead of 62 means eight fewer years of payments. Our projections suggest that for a retiree who lives to 90, cumulative benefits are **only 26.5% higher** when waiting to age 70 to start.



A message for the younger folks

76%

OF RETIREES WISH THEY HAD SAVED MORE CONSISTENTLY IN WORKING YEARS

What's more, 68% of retirees said they wish they had been more knowledgeable about retirement saving and investing. Nearly half said they waited too long to concern themselves with saving and investing for retirement.[4]

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[1] Collinson, C. (2015). The Current State of Retirement: Pre-Retiree Expectations and Retiree Realities. 22. Transamerica Center for Retirement Studies. Retrieved from www.transamericacenter.org.

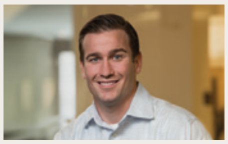
[2] Collinson (2015): 26. These percentages add up to more than 100% because respondents could select multiple reasons.

[3] For illustrative purposes only. Hypothetical benefits calculated using discount and bonus rates provided by Social Security for someone born in 1961. Source: https://www.ssa.gov/OACT/ProgData/ar_drc.html

[4] Collinson (2015): 57.

Retiree Playbook: Planning for the Knowns and Unknowns of Retirement

Homestead Funds does a lot of work with retirees, giving us a pretty clear view of the challenges investors face. We sat down with our financial planners to talk through the tools and services most important for managing accounts in retirement.



Will Cunningham and **Alaina Schrager** are Certified Financial Planners and Registered Representatives.

Q: What are the key financial planning decisions for retirees, typically?

ALAINA: Retirees have to work on parallel tracks, in a way. When you're not working, you are most likely going to be taking money out of your accounts — distributions. But retirement could last 20 or more years, so you also need to be thinking about growing your portfolio.

WILL: Yes, and when you combine that with the fact that most retirees can tap income from various sources — employer-sponsored retirement plans, IRAs and Social Security, all with different rules and tax implications — the puzzle gets even more complicated.

Q: So someone who's built a comfortable nest egg can't simply access that money on demand?

WILL: In some cases no, and in some cases yes — but they may not want to. For example, for money held in employer plans, like 401(k)s, there are typically plan rules that govern the frequency of distributions. A retiree may not be able to access his or her money on demand. So, for those unplanned big expenses that could arise — a car repair, a medical bill — retirees will need to be able to tap savings or IRA accounts. And with IRA accounts, even though you have on-demand access to your money, there are tax implications to consider. An investor who would end up with a hefty tax bill or penalties for early withdrawals might want to look at another income source before tapping an IRA.

ALAINA: Right, and with Social Security — a source of income for most retirees — it may be advantageous to delay receiving benefits. So that's another opportunity to think strategically about the different pools of money you might have access to and the best way to manage those income streams.

Want more info? *Visit the **Investment Planning** section of homesteadfunds.com or give us a call at 800.258.3030.*

Q: And then there are times when distributions from retirement accounts are mandatory, right?

WILL: Yes, the IRS imposes Required Minimum Distributions for Traditional IRA and 401(k) or 403(b) retirement plan accounts. After age 70½, you have to start drawing down those accounts by at least the required amount or there's a hefty penalty: 50 percent of the amount you should have taken but didn't. We send our investors who are 70½ and older a reminder annually and can help with the calculation.

Q: What are the options and considerations for growing retirement accounts? Can distributions be reinvested?

ALAINA: Retirees should definitely think of themselves as actively investing, not just drawing down their accounts. Diversifying your portfolio to maintain an appropriate level of exposure to growth investments is one essential step.

Also, if you are receiving income over and above what you need to cover your living expenses — whether that's from mandatory or scheduled retirement account distributions, an employer pension or Social Security benefits — you can redirect those assets to savings and investment accounts. If you are still working, you may be able to contribute to an IRA if you meet the age or income limits.

Q: What should retirees consider when selecting a financial services partner for their retirement years?

WILL: Being able to get guidance about your investment and distribution options is key. The retirees we work with are able to talk to us about their accounts, their investment options, overall asset allocation and ways to rebalance their portfolio for changing needs. We can create a financial plan and review that with them periodically.

Fee transparency is also important. Advisors have different ways of charging for their services, and you want to be clear about what you will pay for advice and for the investment product.

ALAINA: Access to a range of investment choices that are suitable for your needs is also high on the list. Homestead offers eight different mutual funds, from money market to bonds to stocks. All of our mutual funds are open to IRA investors.

Homestead Funds does not offer legal or tax advice. Please consult the appropriate professional regarding your individual circumstance.

News Briefs

Homestead in the Co-Op Community

We are just back from NRECA's **INTERACT** conferences and representatives are following up with any benefits administrators who had a specific need or question for us. You're always welcome to give us a call at 800.258.3030.

We'll be onsite at NRECA's **regional meetings** and would enjoy talking with any of our shareholders who are also employees or directors of rural electric cooperatives. Stop by our booth to say hello and enter a drawing to win a $100 Cabela's gift card.

Reminder: Resources for Retirees

In addition to IRA accounts — Traditional and Roth — Homestead Funds offers a range of services to help you reach your retirement goals, including:

- Help understanding your retirement account distribution options
- Help setting up a program of systematic withdrawals to meet monthly income needs

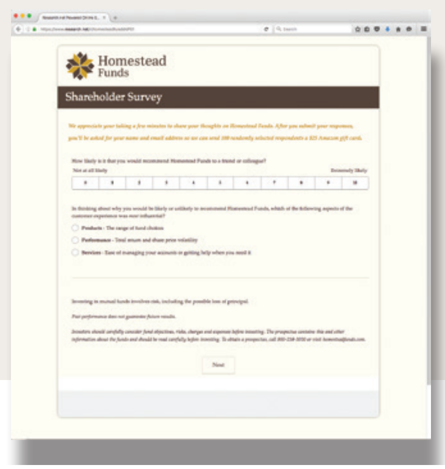
A client services associate would be happy to help you. Please call 800.258.3030.

Please also download the Helpful Tips fact sheet, "Managing Your Savings in Retirement," at homesteadfunds.com. This includes a timeline of steps for those about to retire. You'll find that in the Resources & Forms | Educational Series section of the site.

We'd Like Your Opinion, Please

We appreciate your business and want to continually improve. To help us gauge your satisfaction with Homestead Funds, we've opened an online shareholder survey. The survey is intentionally short — just two multiple-choice questions. Of course we're listening if you'd like to use the comment field to say more! As a thank you for your time, we'll send 100 randomly selected respondents a $25 Amazon gift card.

Take the survey at *https://www.research.net/r/homestead-funds*



Past performance does not guarantee future results.

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Investing in mutual funds involves risks, including the possible loss of principal.

Investors are advised to consider fund objectives, risks, charges and expenses before investing. The prospectus contains this and other information and should be read carefully before you invest. To obtain a prospectus, call 800.258.3030 or visit homesteadfunds.com.

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