



## IRA Insights

# Now is the time to avoid the 'procrastination penalty'

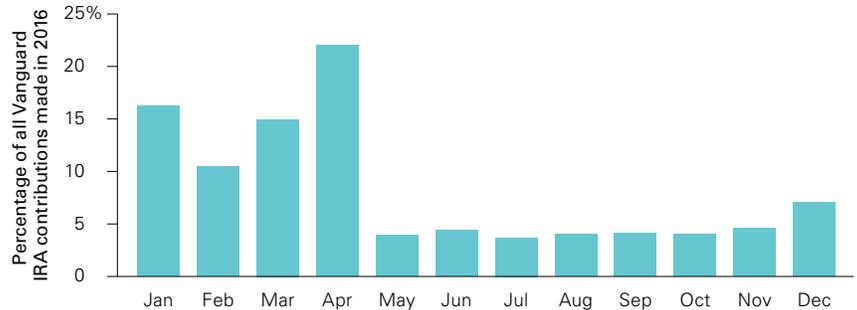
Vanguard Research | March 2017

### 'Tis the season to contribute

In retirement-planning circles, the first few months of the year are known as "IRA Season." When the calendar turns and Tax Day approaches, investors begin to contemplate taxes—and the benefits of tax-advantaged accounts like IRAs.

In 2016, Vanguard investors overwhelmingly chose to fund their IRAs during this period. In fact, almost two-thirds of the Vanguard IRA contributions made during 2016 were made in the first four months of the year.

### The early-year spike in IRA contributions held true in 2016



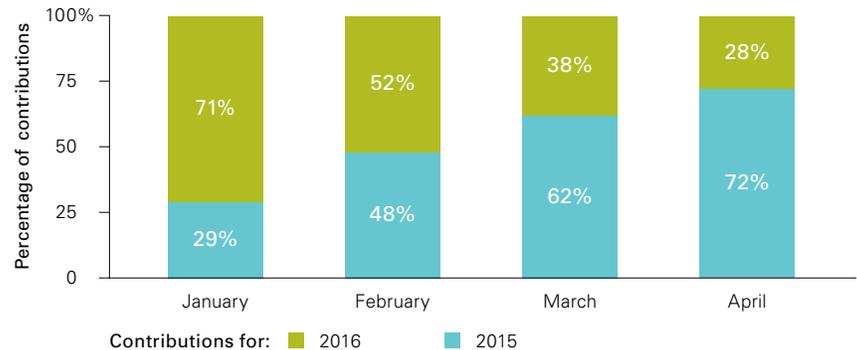
Note: Includes all contributions to Vanguard traditional and Roth IRAs made during 2016.

Source: Vanguard.

### Many 'early' contributors are actually late to last year's party

Not all IRA Season contributions are alike. January 2016, for example, was the first month that IRA holders could contribute for 2016—and many did so. However, most IRA contributions made in April 2016 were for 2015; these investors didn't contribute until 16 months after they had first been able to do so. Why? Part of the reason is that Tax Day is the last day contributions can be made for the prior tax year.

### As Tax Day 2016 loomed, 2015 contributions became the norm



Note: Includes all contributions to Vanguard traditional and Roth IRAs in the first four months of 2016.

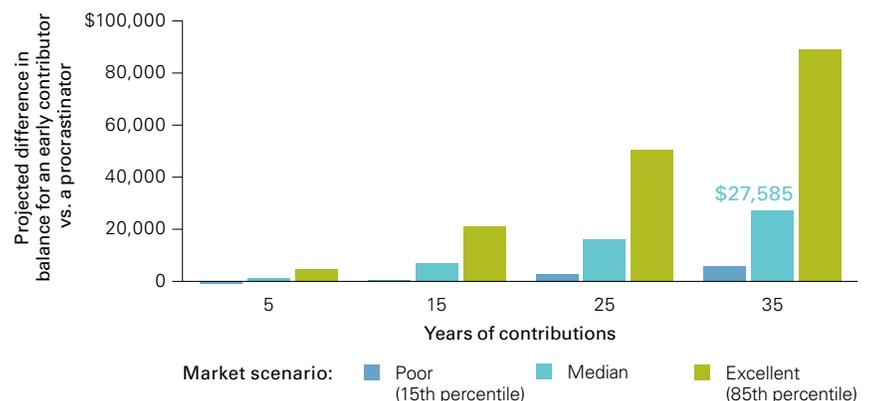
Source: Vanguard.

### Procrastination has a cost

Missing out on tax-advantaged compounding is like paying a "procrastination penalty." Of course, the actual amount of that penalty depends on market conditions. As the chart on the right illustrates, Vanguard's projections show that a 30-year-old procrastinator could easily miss out on more than \$27,500 by age 65.

Procrastinators should try to make two contributions this IRA Season—one for last year, and one for this year, to get on the right track for the future.

### The procrastination penalty grows over time



Notes: Amounts reflect the projected difference in balance between an "early" contributor who makes a \$5,500 contribution in January of each tax year and a "procrastinator" who waits until January of the following year to contribute that amount. Projected balances are as of the end of the year following the number of years displayed, after the procrastinating investor has made the final contribution. For more assumption details, see the endnotes.

Source: Vanguard.

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#### Vanguard research authors

Stephen M. Weber, CFP®  
James Dunlap

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For the third chart, projections are shown in real (inflation-adjusted) dollars and assume a 30-year-old investor making a maximum IRA contribution each year, following an asset allocation that mimics the glide path used by the Vanguard Target Retirement Funds. Return scenarios were generated by the Vanguard Capital Markets Model.

**IMPORTANT: The projections and other information generated by the Vanguard Capital Markets Model regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. VCMM results will vary with each use and over time.**

The VCMM projections are based on a statistical analysis of historical data. Future returns may behave differently from the historical patterns captured in the VCMM. More important, the VCMM may be underestimating extreme negative scenarios unobserved in the historical period on which the model estimation is based.

The Vanguard Capital Markets Model® is a proprietary financial simulation tool developed and maintained by Vanguard's primary investment research and advice teams. The model forecasts distributions of future returns for a wide array of broad asset classes. Those asset classes include U.S. and international equity markets, several maturities of the U.S. Treasury and corporate fixed income markets, international fixed income markets, U.S. money markets, commodities, and certain alternative investment strategies. The theoretical and empirical foundation for the Vanguard Capital Markets Model is that the returns of various asset classes reflect the compensation investors require for bearing different types of systematic risk (beta). At the core of the model are estimates of the dynamic statistical relationship between risk factors and asset returns, obtained from statistical analysis based on available monthly financial and economic data from as early as 1960. Using a system of estimated equations, the model then applies a Monte Carlo simulation method to project the estimated interrelationships among risk factors and asset classes as well as uncertainty and randomness over time. The model generates a large set of simulated outcomes for each asset class over several time horizons. Forecasts are obtained by computing measures of central tendency in these simulations. Results produced by the tool will vary with each use and over time.

Investments in Target Retirement Funds are subject to the risks of their underlying funds. The year in the Fund name refers to the approximate year (the target date) when an investor in the Fund would retire and leave the work force. The Fund will gradually shift its emphasis from more aggressive investments to more conservative ones based on its target date. An investment in the Target Retirement Fund is not guaranteed at any time, including on or after the target date.

All investing is subject to risk, including the possible loss of the money you invest.



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#### Vanguard Research

P.O. Box 2600  
Valley Forge, PA 19482-2600

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