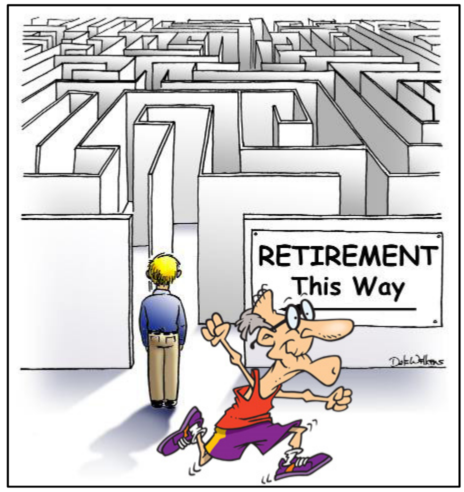
On your mark… Get set… Ready to retire?

Navigating the Retirement Maze



"A goal without a plan is just a wish."
– Antoine de Saint-Exupéry, French author, aviator (1900 – 1944)

Back in 2010 when I published my first column entitled "Not Your Father's Retirement," I described how the present-day version of retirement was markedly different from that of our parents. They entered the workforce at a time when the rest of the world was still rebuilding after a devastating war. US companies flourished with limited global competition, and employees received generous pensions that could carry them through retirement. Working for a single employer your entire career was typical, and the burden of retirement planning fell upon the employer and the US government. Life was good.

Today, it is the employee's responsibility to prepare financially for retirement. Defined benefit pension plans have been mostly replaced by defined contribution 401(k) plans and IRAs. Increased longevity, rapidly rising health care costs, and employment uncertainty have left many soon-to-be retirees concerned about their ability to financially survive retirement.

A study by Genworth highlights this issue. Three out of five adults believe that there is a correlation between financial literacy and retirement readiness, yet fewer than half actively seek financial knowledge. Lack of time, confusion about how to go about it, and the complexity of financial products were all cited as reasons for this. Yet entering retirement without a plan is like running a marathon with your eyes closed. And retirement could well turn out to be a marathon, lasting 30 or more years.

Developing a plan

Everyone ought to have some sort of plan prior to entering retirement, whether done with a financial planner or on their own. And whereas our parents' retirement typically entailed quitting their jobs for good, nowadays it might be a more gradual process of reduced hours or even a new career. No single approach works for everyone, and is highly situation dependent. However, there are a number of common issues that should be addressed well in advance of this transition.

I'm a believer in the power of checklists so that important items don't fall through the cracks. Let's review what should be included in planning for the so-called "golden years." I like to break it down into three categories: your finances, your protections, and your activities. Each is a critical element of your retirement plan.

Your finances

This is the part that usually gets the most attention, as it tends to cause the most anxiety. "Do we have enough to retire?" Income for retirement will come from several sources. Social Security and pensions, for those who are fortunate enough to have the latter, are the lifetime income sources that form the base of your retirement. It is important to time your Social Security claiming strategy to maximize your income, and assuming a long life is the safest approach here. Annuities, both immediate and deferred, can be used as supplemental lifetime income sources.

The other source of retirement income is your investments. Don't be obsessed with thinking that you need to hold mostly income generating assets like bonds and dividend stocks. What matters is total return, coupled with a safe withdrawal strategy and an investment strategy that is resilient to market shocks I caution people who move too heavily to safety in the form of cash and bonds that they are sacrificing future asset growth that might be needed for the long term. Similarly, I counsel retirees who have too large an allocation to equities and other highly volatile investments to diversify their asset classes and manage portfolio risk, as well as having low volatility assets from which they can draw, such as cash and short-term investment grade bonds. This is particularly important in case markets correct near the time of peak asset accumulation.

Your plan should be flexible throughout your retirement to accommodate the unpredictability of markets. Most comprehensive financial planning software can run thousands of scenarios using a technique known as "Monte Carlo" analysis, which will help give you a sense of how robust and resilient your portfolio is. Tied to this is budgeting your retirement expenses to match your income over the different phases of your retirement. Early years will likely have higher travel and recreation spending, while your later years will see health care costs increase.

Your protection

While the need for life insurance will diminish over time – mortgage, child care, collage – other types of insurance become increasingly relevant. As longevity increases, so does the need to plan for the likelihood that some sort of long term care might be needed. Long term care insurance policies have become quite expensive, though I have recommended in a previous column how a reverse mortgage is another way to financially prepare for this.

Be sure to maintain adequate coverage for auto, home/condo/renters, and umbrella insurance. The latter is particularly important, as a single lawsuit can devastate your nest egg. It is inexpensive, so don't neglect it.

A major financial concern of near-retirees is the cost of health care. Studies have estimated the out-of-pocket cost of healthcare for a newly retired couple at between $260,000 and $400,000 in current dollars, and you should build this into your retirement budget, particularly in the later years. Medicare comes with various copays and deductibles, and subscribing to a Medigap or a Medicare Advantage Plan (Medicare Part C) can help reduce the risk of being hit with exorbitant bills in the event of a health crisis.

Your activities

Are you emotionally ready for retirement? For some, the transition from a structured work week to scheduling freedom can be unsettling after the first few weeks. Again, advance planning should help alleviate any angst about how to spend the rest of your life. Write down your specific goals for the next five years. You might include working part time or as a consultant to bring in additional income and create a balance between work and leisure time. There is no shortage of volunteer positions out there for skilled people with time on their hands. Non-profit boards, town committees, arts organizations, and charities are all ways to fill up your available time while giving back to your community.

Your retirement years are a major portion of your life. Treating it as an ongoing project rather than just letting it happen will not only help you make the most of it, but give you something to look forward to.

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