Retired: Can You Afford the Risk?
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Introduction

If typical, you've worked 35 years or longer to be prepared for retirement. During these working years you probably married, purchased a home, raised a family and hopefully accumulated enough savings and investments to assure a worry free lifestyle during your non-working years. Along the way you've experienced personal challenges, probably made a few mistakes with your investments as well as some personal choices, struggled at times to provide adequately for your family and wish you had the chance to redo a few things differently.

But, all this is now history and you're fully prepared for 25 to 30 "golden years" of doing what you want and living the good life. Even though you've saved religiously during your working years to provide for your retirement, it's too early to let down your guard because there will be new challenges. You will be retired three or more decades when you'll have to manage your money and space your dis-savings so that you don't use it too fast or not fast enough. You may be faced with the reality of converting your retirement savings into a sustainable lifetime stream of income. This challenge is complicated since you don't know exactly how long you'll live nor do you know what your future expenditures will need to be. If you have a life partner, the task is doubly complicated. All the emphasis leading up to retirement is placed on savings, portfolio choices and wealth accumulation with little attention being paid to how you convert your savings into a retirement income that will last a lifetime for you and your spouse.

The ominous cloud hovering over Social Security further exacerbates your dilemma since this source of lifetime income may no longer be sufficient or reliable to sustain you in retirement. Additionally, there can be pitfalls and surprises along the way - some out of your control but others under your direction which require you to make the "right" decisions. If you decide to "go it alone", retirement is a time of self-reliance as you grapple with these problems without outside assistance.

At the risk of raining on your parade, let's look at some of the new risks that you'll now face as "retired" and explore the ways that you can either afford these new risks or avoid them. Before launching into this area, let's establish that everyone is unique, has special circumstances, and that there is no one retirement investment or solution that fits everyone all the time. Some of you are better prepared for the risks we'll discuss because you have larger "nest eggs" to carry you through retirement, enjoy better health and have a family network that you can rely upon. So while all the risks presented may not apply to all of you, rest assured that you'll face new risks during retirement regardless of how well you've prepared.

Retirement is the most important financial event in your life and is the only major purchase that you cannot borrow money to finance. Furthermore, retirement is not a dress rehearsal - it only happens once. Unfortunately, Americans are increasingly less prepared for retirement and this development is now the focus of national attention. Additionally, the baby boomer generation has begun to enter retirement and their new demand will have earth shattering consequences on all things retirement related. Not everyone makes it to retirement in as good a shape - financially, physically, emotionally or spiritually - as you have. So, rather than being negative about the new risks you face as retired, just count your blessing that you've accomplished retirement - not everyone does. Your goal is now to have the best retirement possible given the savings you've accumulated over a lifetime of working. Retirement is a time to safeguard what you have rather than trying to "beat the odds" by taking risk with the only money you will have to sustain you during retirement. Your financial goal in retirement should not be to make money but rather keep from losing money.

What are the Risks?

Even though not all risks will be specifically discussed in detail, it is important to present a comprehensive list of the risks you'll face in retirement. In what follows, we'll discuss several of these - some specifically and others only in passing. Just by identifying the risks of retirement you'll be better prepared to address them before you feel their sting. Of course, some are beyond control and you'll simply need to cope. Here's the list of retirement risks as assembled by the Society of Actuaries:

Financial Risks:

Inflation - a constant drag on purchasing power
Interest rates - big impact on your future income
Stock market - a risk that many can't afford
Business - your retirement may depend on its solvency
Employment - a real problem if needed in retirement

Information & Public Policy Risks

Lack of information - options not always known
Public policy changes - Could complicate retirement

Care and Housing Risks

Changes in housing needs - almost a certainty
Lose ability to live independently - increases with age
Health care - rising prices and scarcity will worsen

Personal and Family Risks

Longevity - outliving your money is the greatest fear
Change in martial status - women more at risk
Unforeseen needs of family - can be a real drain

I believe that one of your major risks in retirement will be one you've not even considered as a risk: do-it-yourself retirement planning and investing. With years of experience of working with financial advisors and retirement, I can tell you this is a complex area where serious mistakes are easily made. Get help for this important aspect of your life!

The World Has Changed

Since your retirement can last 25 to 30 years, a good indication of the changes to come can be gleaned by looking at what has occurred over the past three decades. Think back to the late 1970's and try to remember how things were! Prices were a lot lower - from gasoline to houses to food - but were rising at a double-digit annual rate. The inflationary pressures were so great by the early 80's that the Federal Reserve had to put the country through stringent economic times to get runaway inflation under control.

You'll recall that these years witnessed interest rates well into the teens which choked off housing, stymied business activity, created chaos in the financial markets and dragged the economy into recession. In fact, times were tough in many sections of the country, especially for retirees living on fixed incomes, until the late 80's when the inflationary excesses were finally brought under control. The 80's were followed by a dynamic surge in economic activity, a rapidly rising stock market fueled by the dot.com craze, and a forecast of doomsday because of Y2K.

The new millennium opened with a loud pop that was later identified as the bursting of the dot.com bubble. Immediately, the stock market veered south through 2002 with the economy in tow. For the past few years the Federal Reserve has been attempting to engineer first a soft landing and then a smooth take-off of the economy by micro-managing interest rates. The backdrop for these economic maneuvers has been a rising federal deficit, inflating energy prices, a war against international terrorism and despotic rulers that has bloated the expenditures of government, a huge and rising trade deficit, continued erosion of the dollar internationally, and numerous other events that have muddled the eco-financial environment. There is every reason to expect a similar economic history to repeat itself during the coming 30 years that you'll be in retirement. You live in a very uncertain world and there are simply too many possibilities for economic trouble. You may be assured that during your retirement there will be good and bad economic times, high and low interest rates, continued inflation, new taxes and developments that should have been foreseen but weren't.

During these same past decades, giant strides were made on other fronts that have complicated retirement. Better medical procedures, diagnostic techniques and new medicines increased life expectancy. As a result, you're expected to live a longer, healthier life and experience a much longer time in retirement. A by-product has been an aging population in America and around the world. Technological advances have led us into the information age and currently we're all connected worldwide with instant access to a mind-boggling volume of information. You can easily obtain information on virtually any topic and this allows you to make better decisions and live a fuller life. This global communication connection will foster more collaboration among medical, pharmaceutical, nutritional and health care researchers to keep the longevity expansion moving forward at a blistering clip. As the globe shrinks, unforeseen opportunities and challenges will emerge and have a bearing on your retirement.

What will the next thirty years bring? You may be certain there will be major changes on all fronts and your life will be influenced - both positively and negatively. It seems logical to expect periods of economic and financial upheaval that will spawn recessions, price inflation that will hurt the purchasing power of your fixed dollar savings, and policy changes by your governments will be not be in your best interest. For example, one of the most profound developments that will occur is the aging of the population. This rising trend will be accelerated dramatically with the 76 millions baby boomers reaching retirement age at a rate of one every eight second each year between 2006 and 2024. This demographic bulge is sure to foster public policy changes because the relative number of workers will decrease and the relative number of retirees will increase. Today there are approximately 4.8 working age people for every person over age 65; however, when the last boomer reaches age 65 there will be only 2.8 workers for every retiree - a reduction of 42% in two decades. This baby boom phenomenon has been characterized as a "pig moving through a python" because it is very visible and has caused problems at every stage of its development. When the "boomer bubble" reaches retirement it will create new challenges for society, government and for retirees.

The increased demand for benefits from programs like Social Security, Medicare and Medicaid will be beyond the reach of current tax levels. Add this costly trend to an ever expanding size of government administration and a relatively smaller work force to tax, and you have an unstoppable juggernaut. The outcome: a dramatically increased tax burden on the working, a sizeable cut in social benefits, or both. The dramatic demographic shift is sure to place inordinate demands on the country's resources.

There is a finite limit to the amount of taxes that can be levied on the working generation if social unrest is to be avoided; thus, it seems logical to expect dramatic cuts in benefits to program that you have begun to expect as part of your birthright. This will happen during your 25 or more years of retirement. All experts who study the national demographic future know that within the time horizon of your retirement there will develop a conflict of interest between the younger, working population who need to prepare for their own retirement and the retired population who face many years of remaining retirement. If governments react true to form, you can expect them to postpone the hard decisions until the latest possible moment with the procrastination being paid for with more deficit financing and higher taxes which point toward more inflation and unsettled interest rates. This coming demographic clash has profound implication on your retirement years.

Four Trends Impacting Your Retirement

While you have been busy saving for your retirement years, there have been four major developments that have come together like the perfect storm to complicate your retirement. Here they are:

1. Defined benefit pension plans funded by employers have been largely replaced with defined contribution plans funded by employees.
2. Real rates of interest have fallen dramatically so that it now takes more savings to generate the same amount of retirement income.
3. Life expectancy has increased so that it now takes more money to carry you through your retirement years.
4. Heath care costs have accelerated at an alarming pace and now take an ever increasing portion of your retirement income - and, the end to this rising trend is nowhere in sight.

All of these developments mean it is going to take more money to support you during your retirement years if you aspire to continue your pre-retirement lifestyle. It has been established that you'll need 80%-85% of your pre-retirement income in retirement and many advise women to shoot for 100% because they live longer, their Social Security benefits are lower due to fewer years in the work force, sadly they have been paid less, and they spend more on health care costs. By the time women reach age 80, only 16% of them will be married whereas 80% of men are married at the same age. Also, once widowed or divorced women oftentimes experience a dramatic decline in income without a comparable reduction in their expenses. This is a by-product of living longer than their spouses and losing one Social Security check, sometimes having pension benefits reduced by 50% or devoting more of their income toward medical expenses.

Accordingly, it is very important that the ladies be brought into the financial planning process early and often as they will be in retirement longer and are therefore a larger stakeholder in this event. Let discuss each of the above risk trends in turn.

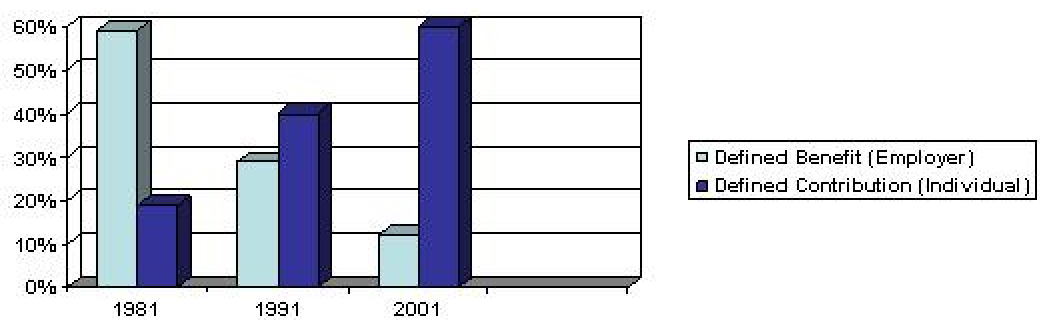
Changing Pension Plan Designs

The fortunate few who retired with a guaranteed lifetime pension income from your employer are a rare breed. Employers have been systematically eliminating defined benefit pension plans for the past three decades. While your lifetime stream of payments may be racked with inflationary rot, you won't be able to outlive them and they will continue in some percentage for your spouse if you chose the joint-benefit option. If you haven't yet had to make the declaration about how to take your lifetime of benefits, you may be tempted to take the single-life option because the monthly benefits are much higher than the joint-life payments. The reason why you should resist this temptation will be discussed later.

Many of you may have missed the defined benefit pension plan because most employers began substituting 401(k) and other defined contribution plans in the early 80's. Granted, many employers made matching contributions to your retirement plan but the responsibility to participate, and the amounts of your contributions, were yours alone. If you didn't have an employer sponsored pension plan you may have used IRAs, SEPPs, Keogh and other forms of retirement accounts to hold your retirement savings. The great advantage of your retirement accounts is that they grow tax deferred, or tax-free if in Roth IRAs, and enjoy triple compounding: earnings on the amount invested, earnings on the earnings not withdrawn, and earnings on money that would have to be paid in taxes if invested elsewhere. Hopefully, each of you prepared for your long retirement years by socking away enough to carry you through. But, there is a major difference in this "new" retirement plan versus the employer paid plan: most of the time you're not assured of a lifetime income you can't outlive with the new plan unless you pro-actively and independently plan to convert to a lifetime income.

The dramatic trend of how pension plans have changed is shown in Chart 1 below. Over a period of only 20 years the pattern completely reversed, and the trend toward

Chart 1



defined contribution plans continues today stronger than ever. This means that your children and those behind you in retirement face an even greater challenge. It also means that you'll have to arrange your own lifetime income from the savings that you have accumulated.

Falling Real Rates of Interest

"Real" rate of interest, or return, means that inflation is taken into account. For example, if the current interest rate on a bank CD is 5% annually but inflation is also measured at 5% annually, the real rate of return is zero. As you are painfully aware, the interest on a bank CD is taxable even if you leave the earnings with the bank; thus, the tax-adjusted real rate of return in this example is negative. You are encouraged to always think in terms of tax- and inflation-adjusted real rates of return because this is the best measure of your purchasing power. After all, it's not how much money you have but rather how much your money will buy. With a zero real rate of return, you may have more money but the same amount of purchasing power. Bear in mind, however, that you'll purchase a unique basket of goods in retirement; therefore, the general level of inflation as measured by the consumer price index may or may not be applicable to you. For example, you'll consume more medical services and health related products, and these prices are likely to inflate faster.

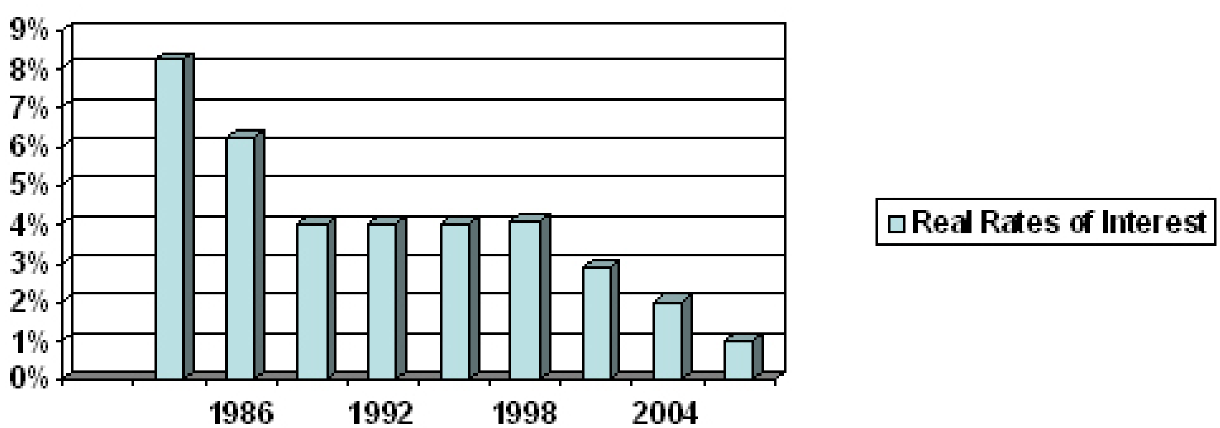
If you're typical you don't worry too much about the real rate of interest but concentrate on the "nominal" rate that is posted by your bank or the return you expect to get from your investments. This is your focus because you know that if you have saved $100,000 for your retirement and it is earning 4%, you're entitled to $4,000 annually as interest income. Retirees are generally delighted when interest rates and earnings expectations rise because annual incomes rise as the principal amount invested earns more. But, in reality when interest rates are rising there is either higher inflation or expectation of higher inflation. For example, as 2006 opened the short-term CD rate at banks was about 2% but by mid-year they had risen to 5%: the reason was both rising prices and expectation that prices would continue to rise. In December of 1981 bank CD rate were over 10% and many living on fixed incomes were absolutely delighted until they discovered that inflation was matching the level of interest rates. Interest rates and inflation move in the same general direction and that's why you must think in terms of "real" rates.

To give you a flavor for how interest rates and inflation can have a bearing on your purchasing power, let's consider an example. Let's say that at the beginning of 1980 you put $100,000 in a bank CD earning 10% (this was a typical bank CD rate at the time). This meant that you earned $10,000 during 1980, all of which was taxable. Let's now fast forward to 2006 and put the same $100,000 in a comparable bank CD with an annual rate of 4%, which was about average. Your annual interest earnings in 2006 will be only $4,000, or 40% of what you earned in 1980. If you adjust for taxes by assuming a 25% bracket for both years, you are left with $7,500 in 1980 and $3,000 in 2006. Unfortunately for you, during these 26 years the average annual inflation of 3.5% more than doubled the general level of prices and cut your purchasing power drastically. So the $3,000 you have in 2006 will buy what $1,227 would have bought in 1980. In other words, your $100,000 in 1980 earned more than six times as much as it would have in 2006 after adjustment for the change in interest rates and inflation. In retirement terms, that means you would have needed more than six times as much money in 2006 to support the same retirement lifestyle as in 1980. With inflation expected to continue into the future and the uncertainty of interest rates, there is no assurance that what happened between 1980 and 2006 won't happen during the first 25 years of your retirement.

Unfortunately, unless your investments are tax free or tax-deferred, the higher interest rates also mean higher income taxes because you earn more nominal dollars and the tax rates get progressively higher as your dollar income rises. The IRS makes no adjustments for inflation or real rates of interest. When you combine the effects of inflation and income taxes, realizing a negative rate of return is not unusually.

Inflation compounds just like the interest you earn on your savings. Over the past 20 years inflation has averaged 3.5% annually and this means that prices double about every 17 years. If earnings on your $100,000 were $4,000 in 1989, the inflation-adjusted equivalent is about $8,000 in 2006 because inflation has cut your purchasing power in half over this period. Since you live in the real world, it is the "real" rate of return that is important because this is what determines how large your retirement nest egg must be to give you the lifestyle you planned. If real rates of return are falling, that means a larger nest egg is needed but if the trend were rising, you could manage with a smaller amount of savings in retirement. As you can see from Chart 2, real rates have been declining and the needed amount of money to give you a retirement income has been increasing.

Chart 2: Interest Rates after Inflation



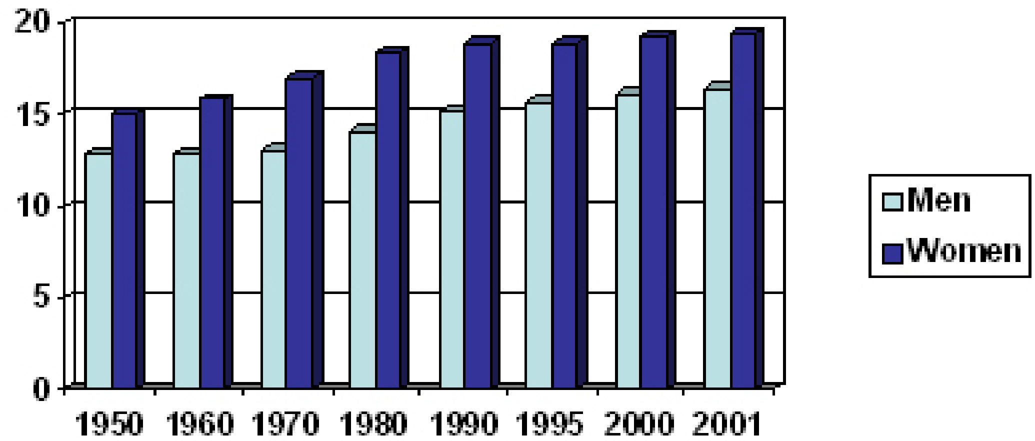
You need a larger nest egg now than you did in the 1980's. What about the future direction of real rates of return? What about your future taxes? Since the taxes on Social Security are not indexed to inflation, it is almost a certainty that you'll pay income taxes on your future benefits if you aren't already. Inflation and taxes are risks you face and are prime reasons why you must safeguard your retirement nest egg from losses because as retirement progresses your nest egg can be expected to purchase less and less. You simply can't afford losses in retirement because taxes and inflation are already shrinking what your money will buy.

Increasing Life Expectancies

Think back to your childhood and try to recall all the people you knew who were age 80 or more. Not many were there? Life expectancy was much shorter back then. In fact, during the 1900's the average life expectancy increased by 25 years. Age 80 is common now and many retirees this age continue to lead very active lives and have their sights on reaching 90 for sure and possibly even 100. During your lifetime the advances in medicine, health care, nutrition and living conditions have added many years to your lifespan. Short of a worldwide pandemic of bird flu or mad cow disease, there is every reason to expect this trend toward longer life to continue. As a group, today's retirees are going to live longer than the generation before them, and your children and grandchildren can expect to live even longer than you.

Living longer is the good news. The bad news is that it is going to take more money to support those extra retirement years. Since 1980, life expectancy at age 65 has increased by 1.1 years for women and 2.3 years for men (see Chart 3). This means that the average man has added 16% to his time in retirement whereas the average woman has added 6%. If everything else had remained unchanged (real rates of interest, inflation, taxes and no more improvements in life expectancy), men need 16% more income to carry them through retirement today than in 1980. A married couple's joint life expectancy is even more favorable and this spells an even larger nest egg to pay for retirement. The increasing life expectancy is no doubt a major reason why the vast majority of retirees under estimate the amount of money they will spend in retirement.

Chart 3: Changing Life Expectancy at age 65



You may now be at the crossroads of deciding which options to choose in taking your retirement money: single or joint life. In making that decision you should assess the probability of the combined life expectancy of both spouses. While age 85 is the normal life expectancy given for an individual age 65, you should know that about one-half of the population is expected to live longer. If you're 65 and male, you have a 40% probability of making age 85 and if female a 50% probability. If both are age 65, there is a 72% probability that at least one of you will reach age 85, a 45% chance one will attain age 90 and an 18% shot of seeing age 95. As we all know, ladies are the stronger gender and the odds shift dramatically in their favor at these older ages. Women need more money to support their retirement than do men, and couples need more than a single person.

Longevity risk is the uncertainty of how long you and your spouse are going to live. This means if you use your retirement money too fast, you'll outlive your money. But, if you don't take it down fast enough you'll deny yourself the fullest lifestyle in retirement. Doesn't it make sense to eliminate this risk by taking some portion of your retirement nest egg and converting it into a lifetime income you can't outlive? If you have a defined contribution retirement plan like a 401(k), can you convert your nest egg into a lifetime monthly income just like you get with the defined benefit plan of old? Yes you can. You could purchase a lifetime annuity by rolling over some, or all, of your 401(k) to pay you a guaranteed lifetime stream of income over a single or joint lifetime. The remainder of your retirement money can be positioned in more traditional investments with risk you can afford.

Whether or not this makes sense for you is dependent upon many circumstances and before you go this route you'll want to obtain the advice of a professional financial professional that can help you assess the feasibility. The point is: if you chose the lifetime income, either from your employer or purchase a lifetime annuity, you'd generally be well-advised to opt for the joint lifetime benefit because of the higher probability of at least one of you living longer than the other. Of course, the single-life option will have a higher monthly payment and will be tempting, but proceed with caution unless you absolutely need the higher amount. Remember, living expenses for one are about 75% of that for a couple and those additional years for the sole survivor means the compounding effects of inflation will erode the purchasing power of the guaranteed fixed income. If you choose the lifetime income with all, or some, of your retirement money, your financial professional can help you integrate the needed amount with your Social Security benefits and other income you have.

Increase in Health Care Costs

If you put retirement in terms of "supply and demand" the picture of inflationary expectation become crystal clear: there will be a larger "supply" of retirees because of the baby boomers. The result will be that goods and services used by retirees will be in greater "demand". What happens to the price of something when demand increases and supply doesn't? Correct, prices increase! Since the supply of medical services is relatively fixed in the near-term (it takes time to educate doctors and nurses, and to build new medical facilities), the increased demand from more retirees spells a continuation of galloping inflation for health care. A government edict to socialize medicine is not going to solve the problem, it will only make medical services harder to obtain and waiting periods longer. If supply and demand are allowed to work, and there is no reason to suspect otherwise, health care costs are going to continue rising dramatically in response to more retirees and an older population. This translates into more money needed for retirement, especially for women who, on average, spend 20% more of their retirement income on health care.

Not to worry you say because you have Medicare! Of course, this is one of those very expensive citizenship benefits that will create an extremely heavy burden on the federal Treasury. Granted you can purchase medi-gap insurance to take care of the cost over-runs but you can expect future premiums for gap insurance to rise precipitously along with the cost of medical services because the issuers of these policies are for-profit companies who will pass forward to users the higher costs of paying for medical services used under the policies. Either way you're going to pay more for health care. If your plans include "spending down your investments" and "giving away your assets" to qualify for Medicaid or other need-based entitlement programs, you're strongly encouraged to assess again your desire to enter a welfare program. As the use of state-run Medicaid increases with the ever increasing number of unprepared retirees, you can expect qualification requirements to become more stringent and care to deteriorate further. A recent survey established that roughly two-thirds of retirees were worried about being able to get and afford medical care.

To get a feel for the inflation of health care, you need only compare Medicare Part B (the program that covers physician's services) to the average Social Security benefits. In 1980 the premiums for Medicare Part B were 6.8% of the average Social Security benefits and in 2005 they were 17.2%. This 250% increase is especially alarming when you consider that Social Security has cost-of-living adjustments to help you keep up with inflation - just like the cost-of-living adjustments that your Congressman has in his or her federal pension benefits. Unfortunately, future health care costs will suffer from the compounding of two simultaneous trends: (a) the increasing costs of medical service driven by more demand and a limited supply, and (b) the increasing need by an aging population. Those still working and covered by the group medical plans of their employers have little understanding of the importance of health coverage for retirees; thus, they, along with elected officials, don't place the same importance on rising health care costs as do retirees. Private coverage is extremely expensive and Medicare has some gaping holes. Hearing, vision and dental coverage are skimpy at best. Nonetheless, you can expect Medicare to continue rising in price and complexity in response to the demographic teeter-totter now underway.

The Other Risks

At the outset, the list of retirement risks assembled by the Society of Actuaries was provided. While the primary ones were discussed, there remain others that could burden you with an increased cost of retirement. You will face many uncertainties that will be new to you during retirement and it is not uncommon for an unknown catastrophic future event to have a major impact on your qualify of life in retirement. It has been estimate that almost 1 in 2 American families are headed toward years of retirement struggle because the average 60 year old has only $60,000 in savings to support them in retirement, and Social Security is simply not going to fund the shortfall.

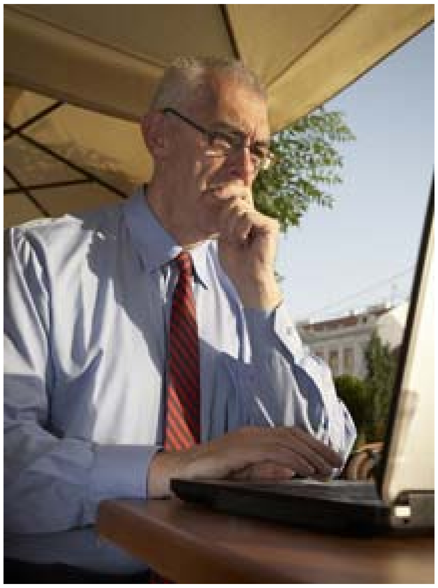
Many of the discomforts in retirement will be rooted in outliving your money, coping with inflation, a higher incidence of medical care and being saddled with supporting a family member or loved one that has run out of money or needs temporary help. In the last two decades there has been a rising trend of divorce among retirees and this generally leaves one or both in worse financial conditions. Women face special circumstances because as the stronger gender they live longer and will spend more years alone in retirement. Before turning to the solutions, let's discuss a couple of the risks that are generally part of everyone's retirement.

Market Risks

Many of you have your investments in risky places because that is where you've always had them. Old habits die a slow death, that’s why you keep trying to beat the market when you should be trying to keep what you've got safe from loss. These risky places include investment real estate, stocks, bonds, mutual funds, variable annuities and other investments that go up and down in value as the market moves. This risk exposure was acceptable during your working years when you had regular income, could increase your savings rate, delay your retirement and also had enough time to recover from market hiccups. Your retirement years are different. You no longer have the same options as when you were working and you simply cannot afford a loss in your investments because these are the source of your retirement income. Just as you protected your job during your working years because it was the source of your income, you must now shelter your investments from loss to assure your future income. If you experience an investment loss, you have to "make do" with a smaller nest egg and that's not a pleasant thought. Yet, more than a few of you continue the old habit of following Wall Street's advice: stocks and bonds regardless of suitability and without regard to your ability to shoulder the risk. When you finish the accumulation phase of the first half of life and move into the second half where you'll be using your savings, you absolutely must limit your risk to what you can afford.

You may think that your diversified portfolio, whether it is in mutual funds or a collection of individual diversified stocks, is safe from risk but history tells you otherwise. If you had money in the "market" between 2000 and 2002 you know first hand the havoc created by a falling market. In mid-2006 the stock market was still trying to reach the previous high set on January 14, 2000 - a full six and a half years earlier. In the meantime your "breakeven" has increased substantially because inflation has eroded a good chunk of the purchasing power of your dollar. In fact, in mid-2006 it takes a dollar to buy what seventy-five cents would buy in 2000 - that's a 33% increases in overall price in just six and one-half years.

The power of compounding inflation is brought front and center when you realize that an investment made in 2000 must now be about 133% of the original amount to reach breakeven in inflation-adjusted dollars. The "real" return you've earned is the difference



in the current value and inflation-adjusted value. For example, let's say you put $100,000 in mutual funds in 2000 and the current amount is $125,000 - you had a loss of approximately 6% in real terms even though you have a 25% gain in the nominal amount. The depressing part is that you are taxed on the real loss because the IRS gives you no credit for inflation. In the 2000-2002 when the stock market was devastated by the dot.com bust, it was common to have a 50% loss in a mutual fund. Even without considering inflation, this means the fund's value has to increase 100% to get back to breakeven. If you earn 10% a year, you're talking about ten years to recover the losses and your money would be worth only about 70% of the original investment after adjustment for inflation. In real terms, you'd need $1.41 for every $1 invested to be at breakeven.

In retirement you should gravitate toward more conservative, low risk or no risk places to put your money unless you have substantially more than you'll need for your retirement. The most conservative approach is to "purchase" a lifetime income, when combined with your Social Security benefits and other guaranteed monthly income it will be sufficient to get you through retirement. You've now got the "basics" covered with a lifetime income and can then allocate the remainder of your nest egg to other investments. In assessing how much you'll need for retirement, please remember that most retirees grossly under estimate the amount of money they'll need - primarily because they discount the risks associated with living longer without employment earnings.

Before you put all your money in bonds, government or otherwise, remember that if interest rates rise you are locked into lower rates that will reduce the amount of income you have for retirement. What's more, if you must sell your bonds due to a need for cash, the lower rates will mean getting less than what you paid. While bonds are fine if you want to lock in a predictable income for a long period of time, they do expose you to the risk of principal loss if you must sell early because the buyer will discount the price to reflect the market rate of interest.

Your broker or financial professional may have coached you in the finer points of Monte Carlo simulation analysis, right down to the second decimal place, but no one knows the future movement of the market. If you look at the last half of the 20th century, the market performed better long term than other investments but remember that past results may not represent future performance. What the market sages forget to tell you about is their faulty statistics, management costs, the investments that have failed and the human reaction when investments increase or decrease beyond expectations. The imponderables make the "theoretical" results far different from the "realistic" results. According to Financial Times Dalbar, the average stock mutual fund investor achieved an annualized total return of only +3.9% for the 20 years ending 12/31/05 versus an +11.9% average annual total return for the S&P 500. The shortfall in performance was due to buy/sell timing decisions initiated by the fund owner. The difference is accounted for by the above variables that never get factored into the sophisticated forecasting model that are used to attract investors. If you punish the data long enough it will confess.

Do you find it curious that "Wall Street's" advice is always stocks or bonds, regardless of your age, risk tolerance, or the amount of money you have? The financial pages of newspapers, investment magazines and newsletters, and endless TV programs are devoted to which stocks should be bought and the many reasons for their attractiveness.

What you don't know is that many of these recommendations are "self serving" because the individual recommending the buy or sell may have a vested interest. But even if they are honest brokers of investment information, it is patently obvious that they don't know the future direction of the market and certainly not tomorrow's price of a stock. This lack of knowledge is documented by the fact that the overwhelming majority of professional money managers fall short of matching the gains posted by the market indexes and oftentimes do no better than randomly picking stocks. The fact is that Wall Street makes money only if investors buy and sell investments; thus, the chorus from the champions of Wall Street is always directed at actively updating portfolios, moving from one stock to another, or balancing the mix with something new or eliminating something old. Activity generates commissions and this is the primary driver of Wall Street.

There are also safe money places for your retirement money and it is these that smart retirees turn to as they lower risks to safeguard their retirement lifestyle. Of course, don't expect to read about safe money places in the investment advice column of your newspaper or hear about them on the evening Market Update TV program because far too many of these safe places don't pay a commission, nor do they need to be traded at frequent intervals so new commissions can be generated. If you haven't discovered these safe money places, or if you haven't changed your investments since your working years, you can't get started too soon.

Changes in Housing Needs Risk

Changes in your need for housing can be related to family circumstances or your health status. How many retirees have you known that developed special needs and their current home with stairs, big lawns, and/or need for cleaning and maintenance have created additional expenses? Many times the widow is saddled with these chores due to the passing or disability of her spouse. In this modern age of far-flung families, such situations create real difficulties. The risk of having to relocate to an assisted living facility can add substantially to the cost of retirement. While this contingency can be covered with long term care insurance, unless the policy is in place at a reasonably young age the costs may be prohibitive. Chances are your housing needs will change during retirement and this is a matter you should consider in formulating your plans.

Many retirees desire to remain in their home but escalating property taxes, repairs and utilities adds an unwelcome burden. Heretofore, the solution was to sell the larger-than-needed home and purchase a smaller one or relocate to an apartment, assisted living center or impose on the children. In the late 90's a new option became available and is currently gaining in popularity with retirees. This is the reverse mortgage, or equity release loan, which allows the retired homeowner to obtain cash from the home's equity without having to make mortgage payments during their lifetime and without having to move. While this may complicate leaving the homestead to the children, it does oftentimes allow the retiree to enjoy a better lifestyle in retirement without having to give up their home. If you have equity in your home and need additional money for your retirement needs, the reverse mortgage deserves consideration. While this option is not for everyone, it could be your ace in the hole and you need to discuss it with your financial professional.

What are the Solutions?

There is no one universal solution for everyone all the time. Your first assignment is to acknowledge that you are unique, your needs are unique, and how you address your needs are unique. Most retirees are not overstocked with financial resources to carry them through a longer-than-expected retirement and it is absolutely imperative that what you have accumulated is righteously safeguarding against as many risks as possible. If you are to take charge and make good decisions in retirement, you must be empowered with knowledge. That you have taken the initiative and time to read these remarks is a very good beginning.

If you haven't reviewed your retirement money's exposure to risks and your ability to afford them, this should be addressed without delay. The first question you must ask is: can my retirement investments decrease in value because of changes in the market? If the answer is yes, then you must answer the following question: how much of a loss can I afford without hurting my retirement lifestyle? You simply cannot speculate with your retirement money unless you have more than enough - and you need to purposely over estimate the amount you deem reasonable because chances are you're not taking account of all setbacks that could befall you. If you are taking risk you can't afford, then change is needed without delay. One change that removes the guesswork of managing your money as well as regulating the dis-savings rate is the lifetime annuity that guarantees you an income you can't outlive. If the lifetime income option is not something you deem appropriate for you, then work with your financial professional to "ladder" your investments so that they mature sequentially and give you a predictable income you can't outlive.

The National Retirement Planning Coalition released the results of a study analyzing risk factors faced by all current and future retirees that may cause their retirement resources to run out well in advance of their lifetime. The study was designed to quantify the various risk factors associated with retirement, model them in different scenarios and assess their impact on retirement income. The results indicates that a couple, age 65, with $1,000,000 in retirement investments, and a desire for $65,000 a year in income, had a 10% chance of running out of money by age 84, a 25% chance the money would be gone at age 90 and 50% they'd be of out money at age 100. Most retirees have only a fraction of this amount to last them during retirement and are just one unforeseen risk away from experiencing a major interruption to their retirement years. As a rule of thumb, you can withdraw about 4-6% of your retirement assets each year during your 60's, boost that to 5-7% in your 70's, increase it further to 6-8% in your 80's and draw down 8-10% in your 90's. For example, if you have $500,000 for retirement and use the rule-of-thumb, withdrawals would be $20,000-$30,000 during your 60's, $25,000-$35,000 in your 70's, $30,000-$40,000 during your 80's and then $40,000-$50,000 in your 90's. If you do the inflation math, you'll see that "real income" is steady state to slightly decreasing. Assuming the midpoint amount is taken each year starting at age 65 and you earn 5.5% after taxes on the unused portion, you'd have zero dollars left at age 100. The much easier solution is to "purchase" a lifetime income or structure your retirement investments so that their maturities are timed to coincide when you'll need the money. Putting all your investments in one maturity is not a smart way to manage your retirement income.

Retirement investing requires planning, knowledge of all the options and a periodic review of the plans and adaptation to a changing environment. In every other part of your life this level of complication dictates that you consult with, and engage the services of, a specialist. You don't read a book and then write your own will, diagnose complicated health symptoms, repair your computer or prepare your own taxes; however, the most serious financial obligation of your life - retirement -- is launched without help after completing a book on investing or following the advice of the personal investment columnist in your daily newspaper. Most self-planners make one or both of the most common mistakes with their retirement money: (1) unknowingly taking market risk in seemingly safe investments like mutual funds, variable annuities or diversified stock portfolios, and (2) keeping all their retirement money in highly liquid, short term rock-solid safe investments that over time pay very low interest rates that rarely keep up with inflation. A financial professional will keep you from making these basic mistakes with your retirement money. Additionally, you know that taxes are going to bite into your retirement income and you should do all in your power to minimize the taxes you pay. There are numerous techniques that allow you to do this, but you've got to know the rules about IRA conversions, when to use your regular savings rather than pension savings, how to use tax-deferred safe money places, when to start Social Security benefits and minimize taxes on them and how to time your income so that you optimize your tax liability. While tax planning is perfectly legal and a tool commonly used by the wealthy, it can be complicated for the uninitiated and you need professional help to take advantage.

Here what the smart retirees do: they learn all they can about investing, risks (financial and otherwise), their needs and the various investments that match their risk profile, and then they consult with and select a financial professional from the ones they interviewed. This results in a plan for retirement that is appropriate, understandable, tax efficient and flexible enough to allow changes along the way as conditions warrant. If you have accumulated adequate resources for retirement, they'll be structured in acceptable investments that assure you'll not outlive them. If you're short on retirement assets, your plan will get you as far as possible and you'll know exactly what adjustments you need to make to get the maximum mileage out of the retirement fuel in your tank. Your retirement map will need fine tuning along the way because how much you can afford to spend will be a function of earnings, inflation, taxes, years yet to live, current principal and those unforeseen future events that are likely to arrive. Once established, the relationship with your financial professional will be long term and you'll ask yourself how you were able to get along without him or her for so long. The best golfer, actors, musicians, and professional athletes benefit from coaches and advisors to help them improve their game or profession and you can benefit by bringing in a pro to give you guidance. And yes, they also use professional financial professionals as do most other wealthy individuals. If you're the go-it-along type, remember that one of the risks you face in retirement is "lack of information about options".

If you were expecting to hear some magic balance of investments that were just right for your retirement years, you've probably been disappointed. All savings and investments can be divided into two categories: safe and risky, with each category offering different opportunities and challenges. The ideal retirement plan for you can only be determined by assessing all your unique circumstances and then constantly monitoring your plan in motion, making adjustments based on your circumstances as the world around you changes. While baring your financial circumstances may be difficult, it is absolutely necessary to avoid the risks and pitfalls associated with retirement. If you're at the tipping point in your retirement, seek advice. As the old dictum about advice states: a wise person doesn't need it and a fool won't take it. Which are you?

Conclusion

Retirement has been a long time in coming but can also last as long as four decades. During this time there will be numerous risks that you'll face for the first time in your life: longevity, inflation without an earned income, a finite amount of investments to last you a lifetime, public policy changes, and the higher health care costs. Unless you have more assets than needed to carry you through retirement, you've got to safeguard what you have to assure a respectable lifestyle for you and your loved ones. If you spend too fast you'll deplete your money too soon but if you dis-save too slow you'll deprive yourself of a better retirement. Of course, the speed at which you should spend is unknown because it depends upon another unknown: how long you will live. This longevity risk gives rise to your greatest fear: running out of money too soon. The best approach to ally your fears is to work with a professional financial professional to prepare a retirement plan that structures your money to safeguard your principal with investment risks you can afford, establishes an emergency fund if you have enough, minimizes your tax burden, and provides a lifetime income plan you can't outlive. There is no one plan or investment that fit everyone nor is there one "best" investment because each retiree or retired couple has different nest eggs, risk tolerances, lifestyles and aspirations. Since women can expect to live much longer, they should prepare for a longer and more expensive retirement. If married, the wife should be involved in the retirement planning from the outset because she has the most at risk.