Managing Key Risks to Make Your Retirement Income Last

Special Report

For most, retirement is considered a goal, a reward for a lifetime of hard work. People "dream" of the "Golden Years" picturing a time they can do all the things they never had the chance to do. Whether traveling the world, playing golf, or just relaxing and enjoying the grandkids, retirement dreams vary for everyone. The last thing you want to worry about during this time is outliving your income.

Will you have enough?

Retirees are faced with what may be the most important issue of their lives: Will they have enough resources to live comfortably during their retirement? If you're concerned about outliving your income, you're not alone. Lifetime income planning has become more complex than ever. Traditional sources of income, such as Social Security and defined benefit plans, have become a smaller part of the equation.

Did you know that:

- Social Security replaces only about 40% of pre-retirement income.[1]

Today's retirees must increasingly rely on personal savings and investments for their retirement income. Sound financial planning is no longer an option – it's a necessity for economic survival.

[1]Understanding The Benefits. SSA Publication 2019

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What will retirement look like to you?

The days of leaving the company at age 65, gold watch in hand, and retiring to the rocking chair on the porch is no longer a typical retirement scenario. The "new" retiree expects to be active, involved and engaged in life. Baby Boomers, in particular, may be less willing to give up the life of money, power and prestige to which they've become accustomed.

What will you need in retirement?

Once you understand your expectations and how you envision your own retirement, you can begin to make decisions regarding your retirement income planning.

Consider the following:

- Living expenses. From housing and food costs to vacation and recreation expenses, determine your monthly or annual budget. A rule of thumb is 70% to 80% of current income may be sufficient in retirement.
- Health care. The cost of medical coverage continues to increase. Determine how you will keep up, particularly as your health becomes a factor.
- Emergencies. In addition to your day-to-day needs, set aside funds for an emergency. Three to six months worth of expenses in a liquid account is generally recommended.
- Long-term savings. Life spans continue to increase. Plan on living longer than you might expect.
- Retirement date. Determine when it's time for you to move from accumulation of assets to using those assets to supplement income.

What are the threats to your savings?

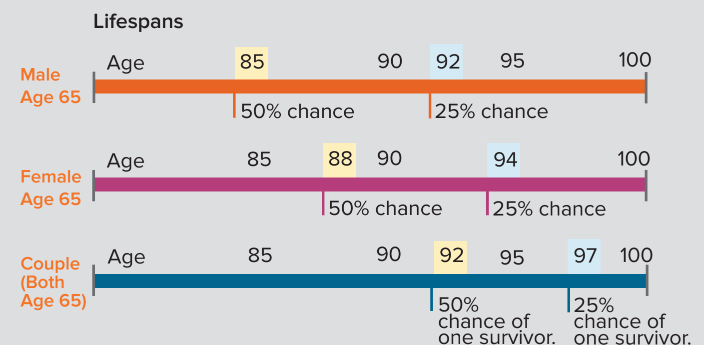
While knowing and understanding your retirement needs is a first step towards lifetime income planning, even more importantly, you must also consider the following factors that could put your retirement income goals at risk:

Longer Living

It's no secret that people today are living longer than prior generations. The Society of Actuaries reports that a 65-year-old male has a 50% chance of living to age 85, while a 65-year-old female has a 50% chance of living to age 88. And the odds of at least one member of a 65-year-old couple living to 92 are 50%.*

Estimating life spans is tricky at best. Many people underestimate how long they will live, which increases the likelihood that they'll run out of savings. The best approach is to plan for longevity, considering the possibility that you'll need income into your 90s. Based on this long-term need, you may want to consider greater exposure to equities for increased growth potential-keeping in mind that investing in equities involves assuming market risk too.

Retirees need to plan for possible longer life expectancies*



* Source: Annuity 2000 Mortality Table; Society of Actuaries. Figures assume a person is in good health.

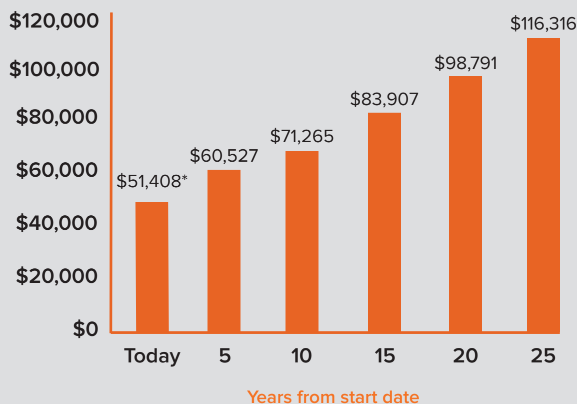
Inflation Risk

Inflation increases future costs of goods and services and may erode the value of assets set aside to meet those costs. Even low inflation can damage purchasing power. For example, with just a 3.32% annual inflation rate over 25 years, your expenses could more than double what they are today.

Or another way to look at it: If you bought a gallon of milk today for $3.62, if you project a 3% projected inflation rate over the next 25 years, that same gallon could cost you $7.58 in 2039. Therefore, in your retirement savings plan, consider including investments with the potential to keep up with inflation.

Even low inflation can slash your buying power

In 25 years, at just a 3.32% annual rate of inflation, your expenses could more than double what they are today.



* $51,408 was the reported annual expenditure for individuals from the U.S. Department of Labor, Bureau of Labor Statistics, Consumer Expenditures 2013 report. All other numbers were calculated based on a hypothetical 3.32% rate of inflation (historical average from 1914 through 2013) to show the effects over time; actual inflation rates may be more or less.

Rising Health Care Costs

Rising health care costs have become one of the greatest threats to retirement income planning, particularly as the cost of prescriptions, preventive care and major medical coverage increases each year – faster than the general rate of inflation. Studies show that retiring elderly couples will need $200,000 in savings just to pay for the most basic medical coverage. Many experts believe that this figure is conservative and the amount is even higher and it will of course will grow over time with inflation.

Long-term care and other health insurance may be helpful in dealing with these increasing costs. Even so, the rising premiums or covering deductibles and uncovered medical expenses may need to be considered.

Most experts agree that addressing rising costs in retirement is an important element of any income plan.

Poor Asset Allocation

Studies have shown that asset allocation decisions, far more than any other factor, affect the long-term performance of an investment portfolio.[2] A poor asset allocation strategy can have a significantly negative impact on your retirement income:

- A portfolio with too much concentration in conservative investments may increase your risk of outliving your assets.
- A portfolio that's too aggressive can increase your exposure to market volatility.

By striking the right balance between equity and debt securities (stocks and bonds), you can potentially reduce your overall portfolio risk. Even in retirement, the key to long-lasting income may depend on a balanced portfolio weighted toward stocks. Using asset allocation as part of your investment strategy neither assures nor guarantees better performance and cannot protect against loss in declining markets.

Withdrawing Too Much, Too Soon

Once you've reached the distribution phase of your retirement, the rate at which you withdraw your assets can have a dramatic effect on your retirement income. For example, if you withdraw 10% of your portfolio it may only last until age 74. However if you were to only withdraw 3%, it could last until age 100 or more. Excessive withdrawal risk can be magnified even further if a sustained market correction – similar to what happened in 2008 – occurs early in retirement. See chart below.

Withdrawal rates much above 4% begin to increase the likelihood that you'll deplete your assets too soon. While it's tempting to withdraw more than 4% annually, a smart strategy is to use as conservative a withdrawal rate as possible, particularly in your early years of retirement.

[2] A landmark study, "Determinants of Portfolio Performance," by Brinson, Hood and Beebower, presented in Financial Analysts Journal (May – June, 1992), and its update in 1996

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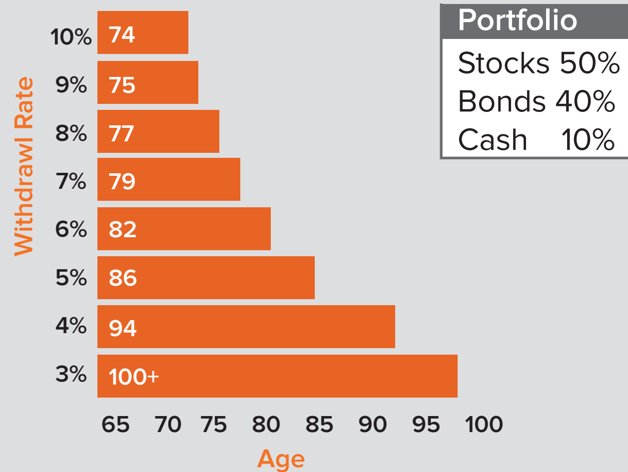
Excessive Withdrawal Risk

Retirement Assets Deplete Faster with Higher Withdrawal Rates. Below is the age to which a portfolio may last based on different withdrawal rates (90% confidence level).



IMPORTANT: Projections generated by Morningstar regarding the likelihood of various investment outcomes using the Ibbotson Wealth Forecasting Engine are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Results may vary over time and with each simulation. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © 2014 Morningstar. All Rights Reserved.

What can you do?

The good news is – you have many options to help you build your retirement savings – from participating in your employer-sponsored retirement plan, to taking advantage of any available catch-up contributions, to various forms of IRAs, to variable and fixed annuities, mutual funds, CDs and bonds.

Each investment vehicle has unique advantages. To learn more, see our Special Report on “Investments 101.” Or, contact a Voya representative who can explain all of these options in detail and help you determine what is right for you.

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