The Age Wave Revisited

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In 1990, Ken Dychtwald, Ph.D., published his seminal book *Age Wave: How the Most Important Trend of Our Time Will Change Your Future*. The book detailed how the baby boomer bulge, the pig in the python, would change the marketplace, alter consumer attitudes and buying patterns, and influence societal evolution. With the leading edge of boomers reaching age 66 in 2012 and the trailing edge marking age 48, the impact on retirement and health issues and strained safety nets is becoming obvious as the nation at large—and families and individuals—grapple with tax and debt issues.

Dychtwald's website (www.agewave.com) lists four key factors that will reshape supply and demand as boomers age:

- "Their concern about the onset of chronic disease and their desire to do whatever is possible to postpone physical aging
- Increasing amounts of discretionary dollars (for many) over the long term as a result of escalating earning power, inheritances, and investment returns
- Entry into new adult lifestages, including empty-nesting, caregiving, grandparenthood, retirement, widowhood, and rehirement—each with its own challenges and opportunities

- A psychological shift from acquiring more material possessions toward a desire to purchase enjoyable, satisfying, and memorable experiences"

We have heard for years about the money boomers will inherit. Can we be so sure? Many boomers are helping their aging parents, even as some aging parents bail out their adult children. Have discretionary dollars been eroded by the difficult markets of the past decade, low returns on money market funds and other "safe" investments, and the insidious creep of inflation? Even those tagged as the "most fortunate" are in for potentially large tax hikes as government claims a higher share of individual and national output.

In an October 2011 piece in *Caring* magazine ("Riding the Age Wave: How Health Care Can Stay Afloat"), Dychtwald proclaimed, "The true costs of aging-related health care go far beyond government entitlements. Medicare only covers about 50 percent of a typical elder's health care costs and doesn't even reimburse for many of the expenses associated with either disease prevention or long-term care." Too many searches for "the number" in retirement planning underestimate health care and related costs.

For those with money, we see rising interest in healthy living, everything from dietary changes to a new status symbol—a personal trainer. The leased BMW in the driveway and the mortgaged-to-the-hilt McMansion are out. Dave Ramsey is in. Some boomer clients gleefully brag about driving paid-for, 10-year-old cars.

Dychtwald sees a shift away from more material possessions toward "experiences." Less and less do pre-retirees focus on "more stuff." They want to travel, see grandchildren, indulge in hobbies, and age in place. Increasing numbers want to work past age 65, touching on the age wave theme of rehirement—continued working but on their own terms. This trend alone could take some pressure off of Social Security.

Consider the impact on the second home market. What happens to prices when the boomers want to sell their beach or mountain homes? Or their boats, or businesses? With a "birth dearth" coming up behind the boomers, there will be fewer buyers … something to ponder.

The 4.5 Percent Challenge

In an article in *Financial Advisor* magazine, adviser Bill Bengen took another look at the well-quoted 4 percent rule.[1] With volatile markets, retirement planners continue to seek "the number"—the ideal withdrawal rate from a portfolio most likely to sustain income over one's lifetime (and that of a surviving spouse for married persons). Bengen notes that "the rule" actually is 4.5 percent. Play with that number as you do retirement income planning for clients. Results can be unsettling.

An August 16, 2010, report by Gail Buckner for Fox Business noted that boomers within five years of retirement reflected "average financial and investment assets of $817,000, versus $558,000 among non-retiring members of their generation."[2]

With any average, some will have more, some less. Assume that your client has $817,000 in financial assets that can produce cash flows and income. At 4.5 percent, annual hypothetical cash flow will be $36,765 a year, or $3,064 per month—hardly a princely sum.

After you add Social Security and pension income, if they are among the lucky few to have pension supplements, how does net income match up with projected outgo? Are there health care concerns? Obligations to aging parents or struggling children?

In his research, Bengen acknowledges the problem with inflation in distorting assumptions and inducing failure. As of April 2012, the Consumer Price Index for All Urban Consumers (CPI-U) was up 2.30 percent from a year ago and up 3.24 percent from its level six months prior. Many advisers and investors fear that intense global monetary creation will show up as increased inflation. If the spending target is 4.5 percent and inflation averages 3 percent annually, the total return target net of tax becomes 7.5 percent.

What about taxes? Many boomer retirement assets are in 401(k) plans, IRAs, or other retirement plans. Excluding Roth IRAs, money coming from retirement plans is taxable at ordinary income rates, marking Uncle Sam as a significant partner in investment largess—a cut likely to jump depending on what happens to the Bush tax rates.

Assume a 20 percent to 25 percent average tax rate including state or local income taxes where applicable. Adjusted for taxes, whether realized in the current year or deferred to a later year, the 7.5 percent total return target jumps to 9.375 percent to 10.0 percent.

We mentioned excessive monetary creation. As European worries roil markets, reserves seeking a safe haven are flowing into U.S. Treasury paper, depressing benchmark yields. Nervous investors pursuing FDIC guarantees flood banks perceived to be safe with deposits, even as loan demand remains weak. That produces a classic "middle class squeeze" as yield-starved investors take it on the chin.

As of June 25, 2012, 10-year Treasury paper offered 1.671 percent. Money market rates stood at 0.50 percent; five-year CDs offered 1.39 percent. Adjusted for inflation and taxes, on a real-yield basis, "safe money" is a big loser!

Boomer Education

Retirement is a major life transition. As noted above, boomers are concerned about chronic disease and have a desire to postpone physical aging. That takes money. A retired couple with only simple health challenges can spend $10,000 to $12,000 per year, including Medicare premiums, deductibles, co-pays, and "donut holes." Medicare does not cover things such as hearing aids, eyeglasses, dental work, long-term care, etc. At 4.5 percent, to generate $12,000 to cover medical expenses, the couple has to have $266,667 in assets. That's before consideration of taxes and inflation—and inflation of medical and drug costs will continue to be a major factor in retirement insecurity.

Pre-retirees and retirees clearly do not understand the ins and outs of Social Security and Medicare. Add a Social Security and Medicare expert to your resource team. The Medicare open enrollment period for 2013 runs from October 15, 2012, to December 7, 2012. Announce a seminar to explain Medicare options and you will fill a room.

Gail Buckner noted that boomers are counting on Social Security and Medicare as the foundation for their retirement. Prior to the recessionary meltdowns, 80 percent of those surveyed said they planned to live only on the income from Social Security, bank accounts, and investments. Principal would be tapped only for emergencies. Here again, reality intrudes on Pollyannaish visions. Up to 85 percent of Social Security income can be taxed and Medicare premiums are deducted from the gross amount.

Many will have to work beyond earlier retirement targets, an opportunity for advisers to offer counseling services on what Dychtwald calls rehirement, tutoring clients on passion and purpose within the precepts of appreciative inquiry. Add a Kolbe-certified consultant to your resource team to help clients define their unique modalities and career success factors as they contemplate working to add “gold” to their golden years.[3]

At a time of heightened investor nervousness, low interest rates, and inflationary threats, boomer angst is fodder for creative, empathetic, and fiduciary-based life planning counseling. Holistic and future-focused financial planning is coming into its own, and is integral to boomer peace of mind and financial survival.

Endnotes

1. Bengen, Bill. 2012. “How Much is Enough?” *Financial Advisor* (May).
2. Buckner, Gail. 2010. “The Great Baby Boomer Wake-Up Call.” Fox Business (August 16).
3. See www.FIREPOWERteams.com.