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Retirement Planning In A Changing World

By Tim Begany, provided by INVESTOPEDIA
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"It is change, continuing change, inevitable change that is the dominant factor in society today," the famous science fiction writer Isaac Asimov once pointed out. In the realm of retirement planning, that wise observation is as true now as it was when Asimov related it.

Indeed, the traditional retirement - leaving work at 65, moving somewhere warm and spending your golden years winding down - is quickly becoming a thing of the past. For example, among employed males age 64, the likelihood of retiring at 65 was recently shown to be only 7% for those born between 1943 and 1947. For this group, which is around retirement age right now, the chance of actually being retired at 65 is much lower than the 56% probability for men born between 1913 and 1917, according to a July 2010 Urban Institute report.

Why do Americans have the tendency to retire later? There are a lot of reasons, like a tough economy, which can derail anyone's retirement plans. But it often comes down to a lack of preparedness - a big issue with Americans well before the economy went sour. In an October 2011 study done by LIMRA research, 41% of pre-retirees between the ages of 55 and 64 said they were saving nothing for retirement. While 21% were saving less than $100 a month.

On the other hand, other studies suggest many Americans are choosing to retire later. They've gradually changed their view of retirement from a winding-down period to a new chapter in life, where they take on new challenges. In a 2011 study done by SunAmerica Financial Group, on average Americans say they'll put off retiring until age 69, and two-thirds plan to stay productive, interspersing periods of leisure with periods of work.

Prior generations of Americans were famous for selling the house and retiring to some other location. A 2011 poll done by the Associated Press found that more than half (52%) of those now approaching retirement age say they plan to stay put. A big factor in this decision is a hurting real-estate market. Because so many Americans count on the value of a home to help them fund retirement, falling home prices are keeping many from pursuing the retirement of their dreams and forcing them to make do where they are.

Regardless of what's happening in real estate, retirement may not even be an option for 40% of Americans. That's the percentage who said they'd never be able to retire when polled in 2011 by the American Institute of Certified Public Accountants. Of those polled, 56% said they weren't able to save for retirement, thanks to higher food and gas prices.

Sources of Retirement Cash

The reliance on Social Security has been growing for decades. According to an August 2011 release from the Social Security Administration, Social Security accounts for at least 50% of the retirement income of two-thirds of Americans age 65 and older. More than a third of retirees (35%) get at least 90% or their income from Social Security. With the economic situation in America, the importance of having a retirement account to help supplement social security during retirement is growing in importance. In these cases, the big question is how best to invest their nest egg for income when interest rates are so low.

That's a tough question. The optimal investment strategy is determined case-by-case, so the answer often varies from one individual or couple to the next.

However, retirees who are willing and able to take on some additional risk might consider investing as much as 40 to 50% of their nest eggs in the stocks of very large, financially sound companies with a history of paying dividends. The dividend income from such stocks is often a lot higher than what you'd get from certificates of deposits, U.S. Treasuries and other traditional income-producing investments. The rest of the nest egg could go into an array of high-quality government agency and corporate bonds, a strategy that also typically generates more cash than the traditional income investments.

A Word About Spending

A big no-no, committed by half of all older individuals, is heading into retirement without a budget. That's sort of like taking a road trip without a map. How can you get where you're going if you're driving blindly? Be sure to do a detailed budget well in advance of retirement, and factor in an overall inflation rate of about 3.9% annually, which is the U.S. inflation rate reported from the Bureau of Labor Statistics (BLS).

You'll need to apply a much higher inflation rate to some expenses, though, particularly health care. The cost of health care is projected to rise 8.5% in 2012, according to a study performed by PricewaterhouseCoopers in 2011. It only seems prudent to use at least that rate in your budget. To be extra safe, consider using an even higher health care inflation rate, say somewhere from 10 to 14%.

The Bottom Line

Retirement in America is changing, both because of hard economic times and evolving views of what retirement should be. According to Gallup Inc., two-thirds of employed people say they expect to work part-time in retirement, while The Center for Retirement Research at Boston College says 51% believe their standard of living in retirement will be lower than that of the prior generation.

In the face of such dramatic changes, it makes a lot of sense to seek the help of a qualified professional. Consider working with a diligent, reputable financial planner to create a budget, develop an investment strategy and take whatever other steps are necessary to make your retirement the best it can be.

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