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P A R T

RETRO-RETIREMENT

CHAPTER 1

THE SAVAGE NUMBER

The subject of retirement both beckons and repels. If you didn't want to think about retirement before the recent stock market crash and the recession, is it any easier now?

The answer is a resounding *yes*. That's because now everyone is aware that retirement is going to be a problem—*if* we define it in the traditional way. But it's also easier because now there are more resources dedicated to helping you rethink the possibilities for your retirement—whether it's on the near horizon or many years down the road.

Today my original comments about redefining retirement make even more sense. I called this section "Retro-Retirement" to explain that the retirement in your future might look a lot more like your grandparents' situation than the one you were dreaming about. Generations before us worked longer, had fewer years of leisure, and cut back their lifestyles in retirement.

If you're a younger reader, Gen X or Gen Y, you can still remodel your retirement plan. Time is on your side, if you start to plan now. But for baby boomers, who always expected a different and better retirement lifestyle, it's time to face reality. Only if we agree to work longer, save more, and adjust our plans can we enjoy retirement security.

It's time to face an important Savage Truth: Time is money. Time can leverage money, if younger workers save regularly and invest wisely. And time can devastate our retirement resources though a longer life expectancy. That's why it's so important to rethink retirement now, while we still have some flexibility.

There's another fact to face: We must rely on ourselves, and not our government for support above the basic necessities of life. Boomer retirement is likely to be a Category 5 hurricane, sweeping onshore in the United States. Our government simply won't be able to create the resources to fund our retirement dreams, without creating a devastating inflation. No, our retirement lifestyle is definitely up to us. And what one generation demands will impact the next.

We may avoid thinking about retirement because we assume we can't make our dreams come true or because we're too busy surviving the present to worry about the future. Or maybe we fool ourselves into thinking that something will come along to save us. After all, it always has. But those aren't realistic approaches.

We all share that lingering worry: *Can I possibly retire?*

There's a simple answer to that question. We can, and will, retire at some point. Or the job will retire from us! The challenge is to make the most of those retirement years by making sensible decisions now.

Most retirees will need to continue to earn extra money, even during their "retirement" years. Leisure time and work time will require a different sort of balance. But we're living longer—and that leaves us more time to divide between work and play. And the sooner we start thinking about that new retirement reality, the easier it will be to shape it.

Shaping Retirement Reality

Thinking about the Savage Number can be overwhelming. It includes not just the money you need in order to retire, but also the money you must continue earning—either on your investments or by other income—while you are *in* retirement. It involves deciding how much you can withdraw to spend and still make your money last as long as you do. And it carries the responsibility of investing to meet your goals amidst uncertainty about everything from inflation to health-care needs.

Retirement will take on an entirely different meaning for the baby boomer generation. We'll live longer, need more money, have less security from Social Security, pay more for medical expenses, and generally face more financial challenges than any other generation. Retirement no longer means whiling away a few years in a golfing community or enjoying the sun on a park bench, as it may have for our parents or grandparents. Longevity adds to uncertainty.

But don't fear. Just as the baby boomers redefined society from kindergarten to college to the job market, the power of this huge generation will redesign retirement. We will work longer, though probably at different jobs than our life careers. We will be flexible about our lifestyles and more concerned about our health than about our material possessions.

Boomers chose the Beatles and the Rolling Stones. Boomers were fueled by McDonald's and Coke. And, in turn, companies that catered to boomers became profitable investments. That will happen again, as retiring boomers demand new products and services. Because of its size, the boomer generation will always impact the economy. And the economy will find a way to accommodate us.

Boomers are reaching age 50 at a rate of more than 12,000 a day—one person every eight seconds. That statistic comes from AARP—the organization that sends you a birthday greeting and a membership application on the day you turn 50. They should know!

Over the next decade, the 76 million members of the baby boomer generation will start reaching the traditional retirement age of 65. Today, there are more than 35 million Americans over the age of 65. By 2025, that number will nearly double. (See Figure 1.1.) Seniors will comprise a voting pool with more clout than ever.

That power of the baby boomer generation will last a long time because people are living longer. Today, when a man reaches age 65, his life expectancy is another 16.3 years. A 65-year-old woman today can expect to live another 19.2 years. But those are just averages. That means half of us will live longer, and half won't make it that far. And we'll never know in advance which half we fall into. We worry when we hear of friends dying from cancer or suffering with infirmities. Suddenly we feel our mortality. But statistics show that the fastest-growing population cohort is people over age 100. You might be one of them!

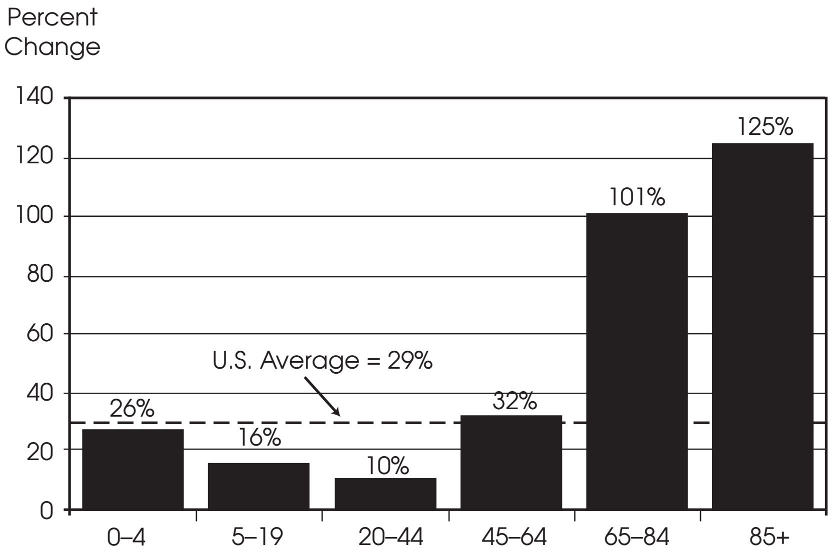

Figure 1.1 The United States Is Aging: Projected Change in Population by Age Group, 2000–2030
Source: Milken Institute. Reprinted with permission.

We can assume, on average, that we'll live longer than our parents because of advances in medical science that prolong life. And given our influence, we'll be heard in the halls of Congress when we demand more attention to our needs—from nursing homes to drug benefits.

Boomers will also be teaching their children a living lesson about saving and spending. If you're a member of Gen X or Y, you've seen firsthand the dangers of living on credit card debt and home equity. You've also seen unprecedented volatility in the stock market. But that shouldn't scare you out of investing in America—and the world. After all, once you've finished taking care of your aging parents, you're going to need investment growth to fund your *own* retirement.

This gap between the generations has the potential to cause great social stress. So we must be aware of how dependent we are on each other to solve the multigenerational retirement issue.

Avoiding Generation Warfare

Government can't take care of boomers if the younger generations refuse to be taxed to pay for our care. Unless boomers plan for our own secure future, we risk creating generation warfare in the United States. If your own children aren't willing to take care of you, how can you expect other people's children to do the job through their tax dollars?

It's not just a question of morality. Even in a growing economy, there simply won't be enough of the next generation to support us *and* educate their own children. During the baby boomers' peak working years, 1980 to 2000, there were almost four people of working age for each person over age 65. But as we boomers retire, that ratio will shift. By 2035, there will be fewer than three people working for each person over 65. And remember that those workers—our children—will be trying to care for their own families on what remains of their paychecks after taxes.

As you can see in Figure 1.2, unless cuts are made in government programs, retiree benefits will soon consume the majority

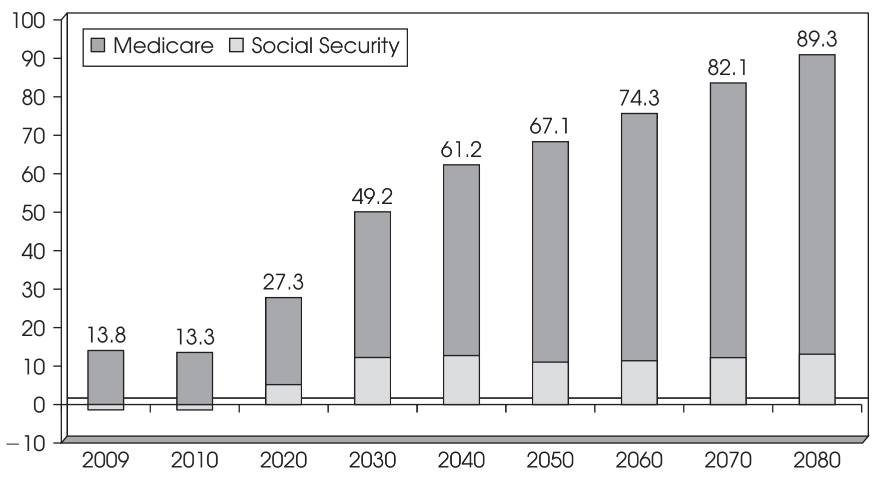

Figure 1.2 Percentage of Income Tax Revenues Needed to Meet the Payroll Tax Shortfall on Social Security and Medicare

Source: National Center for Policy Analysis (NCPA). Calculations based on data from the 2008 Medicare and Social Security Trustees Reports. Reprinted with permission.

of our tax revenues, leaving little for defense, education, or other national needs. According to the trustees of the Medicare program, by 2019, 24 percent of all income tax revenues will be needed for the Medicare program. The curve grows exponentially. By 2040, 51 percent of all income tax revenues will have to go to Medicare. Social Security trust funds are expected to have a negative outflow of cash by 2017—and to become insolvent by 2041.

Actually, Social Security has for many years been a system of transfer payments. Even as you get a statement from Social Security listing your contributions and promised benefits, you should realize that those benefits are being funded each year out of general tax revenues. There is no trust fund, no shoebox in Baltimore with your money inside it. The deduction from your paycheck this week will pay for a retiree's check next month.

According to the Congressional Budget Office, the $659 billion in benefits that Social Security paid out in the 2009 fiscal year exceeded payroll taxes collected ($653 billion) for the first time since 1984, when that huge Social Security tax increase was enacted to fix the system for the boomer generation.

Now they predict that there will be only an $83 billion surplus in the fund by 2018. And that prediction will be impacted by declining payroll taxes caused by prolonged unemployment. The bottom line: There simply isn't enough money coming in to pay for all those promised benefits.

Social Security is likely to undergo major changes before or during your retirement. The benefits you expect to receive will be postponed to a later retirement age—and could even be means-tested—to keep those payments from sinking the entire federal budget. Social Security is *not* your safety net. And no matter how much you've saved for your retirement, the biggest hole in your personal safety net is the rising cost of health care.

Medicare cannot continue to fund the current level of health benefits—including the newest treatments and prescription drug benefits—for this growing population of seniors. Don't look to your previous employer for help. Companies are cutting back on retiree health benefits at a time when costs for medical services are rising twice as fast as traditional measures of consumer price inflation.

Neither Medicare nor Social Security covers the cost of long-term custodial care, either in your own home or in a nursing home, except for a very limited number of days after a hospitalization. Government tries to provide custodial care for impoverished seniors through state-run Medicaid programs, but the facilities that offer that care will be sorely strained by the huge boomer generation.

Planning to become impoverished by gifting assets to your children so that Medicaid will cover your care is a recipe for disaster. You'll give up the freedom of choice you get when you purchase long-term care insurance to cover those costs.

Some people are hoping that the government will simply print enough money to fund the promised government retirement benefits. But creating more money through inflation destroys the value of everything you've saved. We learned that lesson in the 1970s, when the government tried to create enough new money to have both guns and butter. We certainly don't want our government to try to give us both bridges and benefits in 2030, just when both are wearing thin!

Government is not the solution. It will contribute, but not enough. Sometimes it's even part of the problem. State and municipal pension promises are under attack by taxpayers who refuse to authorize state income tax hikes. Even some corporate pension promises are being called into question. It's up to us to rearrange current lifestyles and expectations for the future. And we have to do it now, while we have flexibility.

Hoping for a Miracle?

There will be no miracle solutions to make your retirement dreams come true—not the government, the stock market, the family home, or a windfall inheritance.

For a while, it seemed like the stock market would bail out boomers' retirement dreams. Employees were admonished for decades to save and invest money in company retirement plans or individual retirement accounts, but many failed to do so. Those who did had unrealistic expectations. The stock market crash has destroyed their hopes that outsized investment returns would offset a lack of diligence in savings.

If history is a guide, stock market investments should outperform other alternatives over the long run—at least 20 years. But even the recent experience with stock market losses should not be an excuse to stay away from stocks. In fact, it's the reverse: You'll need even more exposure to equities in your retirement investment assets to rebuild your financial plans. It's a paradox, but just when people are most scared of the market, they should keep in mind that it has always offered the greatest opportunity to profit over the long run.

For some people, hopes for a financial miracle rested on residential real estate. But real estate is a market just like stocks—and far less liquid. By now, you should have learned that when any market's gains exceed historic trends, the bubble will burst. Housing prices in many areas collapsed by a greater percentage than stock prices. And it will take years for housing prices to recover—unless a major inflation psychology takes over. But don't give up on using your home equity: Reverse mortgages will still offer seniors a way to create tax-free retirement income, if they've paid down almost all of their mortgage balance, as explained in Chapter 14.

And forget about inheriting money from your parents. According to AARP, in recent years baby boomers who had received an inheritance received a median of just under $48,000. Those who received much more than that were wealthier to begin with. Almost two-thirds of inheritances went to families with a net worth of about $150,000. As parents live longer and spend more, inheritances will dwindle. In fact, many boomers will need to provide financial assistance to their aging parents.

You're Not Alone

Not surprisingly, the recession has brought a new sense of reality to the subject of retirement planning. Dreams of early retirement and relaxing leisure have given way to a new understanding of how costly retirement will be—and how ill-prepared most of us are for this reality.

The 2009 Employee Benefit Research Institute (EBRI) survey on retirement confidence hit its lowest level since the survey was started in 1993. Only 20 percent said they were "very confident" about their retirement prospects, compared to 40 percent in 2007!

People tend to underestimate savings requirements, life expectancy, and the rising cost of health care, while overestimating how much they can draw on their savings. Even small miscalculations of those numbers can result in huge errors. The EBRI study reveals that only 44 percent of workers report they and/or their spouse have tried to calculate how much money they will need to have saved by the time they retire. And an equal number simply guess at how much they will need for a comfortable retirement.

Worrying about retirement is fodder for cartoons. There are just so many uncertainties: how long you'll live, how much your money can earn, the rate at which inflation will eat away at your savings, and the rising costs of health care.

Source: From the *Wall Street Journal*—permission, Cartoon Features Syndicate.

The challenge of planning for retirement may seem overwhelming, but you have to face reality. Will you ever be able to save enough to fund a secure retirement? If saving more isn't possible, and if extraordinary investment returns are unrealistic, then working longer—either longer *hours* now or longer *years* later—may be the only alternative. That will allow the money you currently have in savings and investments to grow for a few extra years while you set aside a few more years of retirement plan contributions.

Even a few years of additional contributions and delayed withdrawals can make a big difference. But that may not be enough. It's time to reexamine the entire concept of retirement.

The Likely Solution: Retro-Retirement

Have you noticed that what's old is new again? Vintage is in style—whether in fashion, home design, or even music. Retro-chic is happening everywhere. So what's wrong with a retro-retirement? It's time to take a new look at a vintage idea and give it our own modern twist.

Think about it. Your grandparents, and their parents, worked until they died. They didn't complain. That's just the way it was. Even the stock exchange was open on Saturday, until 1952. Their recreation took place on Sunday. It wasn't until the late twentieth century that the idea of retirement was built around the concept of working less, or not at all, while living on a pension—an unending stream of income that would subsidize a lifestyle. Suddenly, workers could buy recreational vehicles, mobile homes, and cottages at the lake. Our higher standards of living were extended into retirement years.

But in the new reality, we're living longer, and it's costing more. And the stock market crash has decimated IRA and 401(k) assets that might have supported this dream. It's time to recrunch the numbers and revise the plan—if you ever had one.

The first step is an attitude adjustment. Maybe it's sour grapes, but boomers who have worked all their lives might find it a bit boring to play golf or tennis, to sit on the beach, or to drive across the country. We're creating our own concept of retirement that will be every bit as defining of our generation as the Beatles and the Rolling Stones. We'll work, and we'll play on our own schedule. It will be retro-chic to do both—and to do them in style.

It's not impossible for boomers to retire, but we must redefine the term. Almost certainly, it will involve working longer. But then we'll be living longer. Health care may cost more, but we'll probably be healthier than our parents. We may have less money, but we'll have a better chance to enjoy what we have. It all starts with facing up to the choices.

THE STARTING POINT

These three questions require no specific knowledge to answer, but a lot of self-discipline and honesty. There are no right or wrong answers.

1. How old do I expect to be when I die? ____________
2. How do I rank the following three retirement solutions?
   Working longer before retiring ____________
   Lowering standard of living in retirement ____________
   Saving more now ____________
3. If I knew I could get trustworthy advice about how to save, invest, budget, and withdraw, I'd be willing to confront the financial issues of retirement. ____________ (yes *or* no)

With so much uncertainty, how can anyone know the Savage Number? Well, here's a helpful thought: You don't have to hit the number right on the head. Getting close counts more in retirement than in horseshoes!