THE 2 BIGGEST RETIREMENT MISCONCEPTIONS

While the idea of retirement has changed, certain financial assumptions haven't.

Provided by **Renita M. Owens, CPA, PFS**

We've all heard about the "new retirement", the mix of work and play that many of us assume we will have in our lives one day. We do not expect "retirement" to be all leisure. While this is becoming a cultural assumption among baby boomers, it is interesting to see that certain financial assumptions haven't really changed with the times.

In particular, there are two financial misconceptions that baby boomers can fall prey to – assumptions that could prove financially harmful for their future.

#1) Assuming retirement will last 10-15 years. Historically, retirement has lasted about 10-15 years for most Americans. The key word here is "historically". When Social Security was created in 1933, the average American could anticipate living to age 61. By 2005, life expectancy for the average American had increased to 78.[1]

However, some of us may live much longer. The population of centenarians in the U.S. is growing rapidly – the Census Bureau estimated 71,000 of them in 2005 and projects 114,000 for 2010 and 241,000 in 2020. It also believes that 7.3 million Americans will be 85 or older in 2020, up from 5.1 million 15 years earlier.[2]

If you're reading this article, chances are you might be wealthy or at least "affluent". And if you are, you likely have good health insurance and access to excellent health care. You may be poised to live longer because of these two factors. Given the landmark health care reforms of the Obama administration, we could see another boost in overall American longevity in the generation ahead.

Here's the bottom line: every year, the possibility is increasing that your retirement could last 20 or 30 years … or longer. *So assuming you'll only need 10 or 15 years worth of retirement money could be a big mistake.*

In 2010, the American Academy of Actuaries says that the average 65-year-old American male can expect to live to 84½, with a 30% chance of living past 90. The average 65-year-old American female has an average life expectancy of 87, with a 40% chance of living past 90.[3]

Most people don't realize how much retirement money they may need. There is a relationship between Misconception #1 and Misconception #2 …

#2) Assuming too little risk. Our appetite for risk declines as we get older, and rightfully so. Yet there may be a danger in becoming too risk-averse.

Holding onto your retirement money is certainly important; so is your retirement income and quality of life. There are three financial issues that can affect your quality of life and/or income over time: taxes, health care costs and inflation.

Will the minimal inflation we've seen at the start of the 2010s continue for years to come? Don't count on it. Over the last few decades, we have had moderate inflation (and sometimes worse, think 1980). What happens is that over time, even 3-4% inflation gradually saps your purchasing power. Your dollar buys less and less.

Here's a hypothetical challenge for you: for the rest of this year, you have to live on the income you earned in 1999. Could you manage that?

This is an extreme example, but that's what can happen if your income doesn't keep up with inflation – essentially, you end up living on yesterday's money.

Taxes will likely be higher in the coming decade. So tax reduction and tax-advantaged investing have taken on even more importance whether you are 20, 40 or 60. Health care costs are climbing – we need to be prepared financially for the cost of acute, chronic and long-term care.

As you retire, you may assume that an extremely conservative approach to investing is mandatory. But given how long we may live - and how long retirement may last - growth investing is extremely important.

No one wants the "Rip Van Winkle" experience in retirement. No one should "wake up" 20 years from now only to find that the comfort of yesterday is gone. Retirees who retreat from growth investing may risk having this experience.

How are you envisioning retirement right now? Has your vision of retirement changed? Is retiring becoming more and more of a priority? Are you retired and looking to improve your finances? Regardless of where you're at, it is vital to avoid the common misconceptions and proceed with clarity.

«Renita M. Owens, CPA, PFS is a Representative with Capital Investment Group, Inc. and may be reached at www.cpawork4u.com, (864)233-4163 or rowens@capital-invest.com.

Citations

1 – nytimes.com/2008/04/27/weekinreview/27sack.html?pagewanted=print [4/27/08]
2 – usatoday.com/tech/science/2005-10-23-aging-centenarians_x.htm [10/23/05]
3 – usatoday.com/money/perfi/retirement/2010-04-30-401k28_CV_N.htm [5/3/10]