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The Opening Bell

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Are You Guilty of Self-Induced Poverty?

by Jim Bell, CFP®, President and Founder, Chief Investment Officer

Believe it or not, there is a new concern afoot that retired Americans are not spending enough money!

This runs completely counter to the dominant conversation that Americans are in a retirement crisis and woefully unprepared for life after work. Finance professor Meir Statman writes about the "Consumption Gap", which he defines as the gap "between people's actual consumption and their potential consumption made possible by their wealth." The assumption here seems to be that the purpose of life is to consume, which I believe many of you would challenge. Dr. Statman does include charitable giving in his concept of the consumption gap, but consumption is hardly the right word for philanthropy.

Retirement Crisis or Not?

In his article "Are Your Clients Not Spending Enough in Retirement?" (November 2017 *Journal of Financial Planning*), Dr. Statman argues that the drumbeat of retirement crisis is much too loud. He asserts that the degree of saving

> ***The transition from saving and preparing for retirement to spending and experiencing retirement can be difficult for many people.***
> — Jim Bell, CFP®

and spending is regulated by the human capacity for self-control and that *excessive* self-control is as prevalent as *insufficient* self-control. In a study published by the Vanguard Group based on extensive polling, 55% of American retirees believe there is a national retirement crisis, but only 4% describe their own retirement situation as a crisis. This same study found that 90% of retirees report that they are able to spend freely, and only 10% report that they are on a strict budget.

An important aspect of retirement planning is the variance in spending that occurs between the early years of retirement and the later years. The Howe Institute reports that the average spending by college-educated American couples at age 84, adjusted for inflation, is 23% less than it was at age 62. Social Security tables indicate that only one in ten of today's 65 year-old men will live to age 95. It is a common reality that we may die sooner than we expect and that our health will restrict what we want to do with our wealth.

MORE COVERAGE INSIDE

In July 2016, Forrest Bell, CFP®, wrote about retiree spending in *The Opening Bell* with regard to the three periods of retirement, go-go, slow-go, and no-go. The old assumption was that retiree spending keeps rising over time at least at the rate of inflation. New research shows that retirement spending trails the rate of inflation by as much as 20% to 30%. At age 65, if a couple spends $100,000 annually, normal inflation would expand their spending to $158,000 by age 80. But research by Jonathan Guyton, CFP® reveals that on average, spending drops to $146,000. This $12,000 per year decrease has a powerful impact on financial planning results in terms of recommending what retirees can spend in the go-go years.

Ready for Big Medical Expenses?

Of course a long-term care event or other medical expenses can disrupt the scenario above. Financial planning helps determine how prepared people are for such contingencies. Do they have long-term care

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Are You Guilty of Self-Induced Poverty? *(continued)*

insurance? How effective is the policy? Do they have enough capital to cover an expensive development?

Another area that influences the level of spending from investments is the amount of guaranteed income retirees receive. Social Security benefits, pensions, annuities, and disability insurance are some of the categories of guaranteed income. The more income retirees receive from guaranteed sources, the less they need to receive from investments for their core living expenses. Research continues to support the 4% level of annual spending from investment portfolios. This is a good starting point to generate retirement cash flow, and the beauty of an active financial plan is that we continually refresh and test the probability of success for each client based on their spending and investment returns.

In a recent post, Michael Kitces, CFP® reports that bankruptcy rates for retirees over 65 are shockingly low — only 3 per 1000 — and that rate declines as they get older. This is another way of pointing out that the American retirement crisis is overblown. The assumption here is that people in duress are able to make spending adjustments so that they avoid the bankruptcy process. Of course, making radical spending adjustments is not the goal of financial planning, but it can be the reality. Plans distinguish between core living expenses and discretionary spending, and the discretionary part is the first place adjustments are made if necessary.

Prepared to Start Spending and to Stop Saving?

The transition from saving and preparing for retirement to spending and experiencing retirement can be difficult for many people. It is a real sea change, and it often takes time to become oriented to the new rhythms of retirement. The concept of self-induced poverty refers to people who may be afraid to spend when they have spent their whole life saving. We hope that financial planning will help support appropriate and sustainable spending, and will reassure retirees that they can enjoy their life and wealth with confidence as we keep their plan up to date. ■

UPCOMING EVENTS

WEBINAR

Why Is the Market So Strong, and What Could Go Wrong?

Wednesday, January 17, 2 – 2:30 pm
online

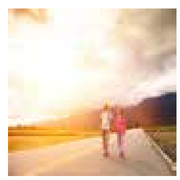
- **What does the tax bill mean for 2018?**
- What impact will Federal Reserve policy and the new Fed Chair have on the bond market?
- International equities are back in favor; will the rally continue?
- Can the low volatility environment we saw in 2017 persist?

Join us as we explore these questions in our half hour webinar.

Jim Bell, CFP®
Founder and President
Corinne Salera Bedford, CFP®
Portfolio Manager, Investment Advisor

Register here: bit.ly/Jan17webinar

A recording of the webinar will be available on our website about a week after the webinar.



LUNCH SEMINAR

Retirement Spending: A Blueprint for Smart & Strategic Distributions

Wednesday, January 24, 12 – 1:30
1111 Broadway, 16th Floor

This is a repeat of the filled-to-capacity October 2017 event!

- Use your investment accounts to create a monthly paycheck in retirement.
- Tailor your distributions to meet your needs before and after receiving Social Security.
- Coordinate distributions to minimize taxes.
- Avoid penalties, and ensure you satisfy your Minimum Required Distribution.

Guest Speaker: **Bob Heywood, Esq.**

Bell Presenters:
Forrest Bell, CFP®
Sr. Investment Advisor, Financial Planner
Jerene Meissert
Sr. Relationship Manager

Reservations for the lunch and seminar: 800.700.0089, ext.100 or rsvp@bellinvest.com

No fee to attend!

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Long-Term Care

by Forrest Bell, CFP®, Sr. Investment Advisor, Financial Planner

Some years ago, a client came to me concerned about his long-term care policy. He purchased the policy through CalPERS. It would cover much of the cost of long-term care for all of his life, but he had just been informed that his premiums would be going up by 85%. The increase made him want to find a better policy, but he couldn't. None of the new polices he could obtain were as good as the one he had. The premiums of long-term care policies in general had begun to rise, and the terms of newer policies were less generous.

Most people assume that long-term care premiums rose for the same reason that healthcare costs increased: the underlying care was becoming a lot more expensive. While the cost of delivering long-term care did increase, the increase was tamer than in healthcare. So why did long-term care premiums rise so much? The primary reason was lapse rates.

Lapse Rates

Lapse rates describe the percentage of people who buy a policy but let it lapse before a benefit is paid out. Lapsed policies are hugely beneficial to insurance companies as they increase the funding pool needed to cover payouts while simultaneously decreasing the company's overall liability. Insurance companies assumed that long-term care policies would have lapse rates similar to other kinds of insurance such as life insurance. But the lapse rate for long-term care policies is much lower. Over time insurance companies learned that consumers cleave to their long-term care policies, and this upset the math. With fewer policy lapses than expected, insurance companies faced higher liabilities. They responded in one of two ways: Many insurance companies — including MetLife, Prudential, Allianz, and John Hancock — stopped issuing new long-term care policies altogether; others responded by increasing premiums and limiting the coverage.

Limiting Coverage

Limiting the coverage of long-term care policies would seem to be a reasonable response. About half of long-term care cases open and close within one year. Nearly

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90% of long-term cases open and close within a four-year period. As the statistics suggest, people who require long-term care either recover or get worse and die. That's why it's statistically rare to have long-term care needs that exceed four years. Companies began issuing new policies that limit coverage to three, four, or five years. While these still cover most long-term care needs, such capped policies are clearly less useful to certain consumers.

Many of our clients can use their existing assets to cover a four-year long-term care need. This approach often proves more efficient than buying long-term care insurance. What many of our clients cannot do is pay for a 15-year long-term care need. But there are no traditional/stand-alone long-term care policies that offer lifetime coverage in California anymore. Instead, this void has been filled in California by hybrid policies.

Hybrid Policies

Hybrid policies are a form of life insurance, but they have two parts: a base policy and a rider. The base policy is a whole life insurance policy or a universal life insurance policy with a specified death benefit. Consider the hybrid policy offered by OneAmerica. A married couple can keep the policy as a traditional life insurance policy, but if one of them should experience a long-term care event, they can draw down the death benefit as a dollar-for-dollar reduction. The base policy only covers long-term care expenses up to the death benefit and that is where the rider becomes meaningful. For the additional cost of a long-term care rider, the couple receives financial support for long-term care for their entire lives. Before you get too excited, however, you should check out the cost of a hybrid policy:

OneAmerica Asset Care hybrid insurance policy Assuming a married couple, ages 60 & 62, non-smokers, in good health:	
Initial Premium	$200,000.
Whole Life Insurance Death Benefit	$285,900.
Lifetime Continuation of Benefits Rider	$8,500/month for life

Will I Need Long-Term Care?

According to a J.P. Morgan study, 35% of men age 65 will need some kind of long-term care at some point in their lives. For women age 65, 73% will need long-term care at some point in their lives. Accordingly, a married couple will likely see at least one spouse need long-term care. These statistics don't mean you should run out and purchase a long-term care policy, but they should cause people to think. And like the expenses for the more beloved aspirations of travel, weddings, home remodels, car purchases, and gifting, long-term care is an expense you should include in your plans for the future. ■

Bell Investment Advisors

We all wish all of you a joyful and fulfilling 2018.

How About a New Year Filled with Resilience?

by Bonnie Bell, MA, MDiv., Principal, and Director of Career/Life Coaching

As you have probably heard — or experienced first-hand — the long-term success rate of New Year's resolutions is pretty slim. Statistics for 2017 reveal that 80% of resolutions set by people in January fail by February. So rather than even spend time on the subject, at all, I'm going to pivot to another subject that doesn't, in my opinion, get the attention it actually deserves: *resilience*.

The definition of the word, as set forth by the American Psychological Association, is "adapting well in the face of adversity, trauma, tragedy, threats or significant sources of stress." In more common usage, *resilience* is often used describe someone who *bounces back, e.g.,* from the flu, a minor car crash, or the break-up with a boyfriend or girlfriend.

Success Despite Stressful Childhoods

In an article I saved from the Review Section of the November 11-12, 2017 issue of the Wall Street Journal, University of Virginia clinical psychologist Meg Jay tackles the subject in an article called *The Secrets of Resilience,* in which she poses the question, "What does it take to conquer life's adversities?"

Significant studies over the past 30 years suggest that surprising numbers of people who faced chronic stress during childhood, later succeeded anyway. A short list of successful men and women who have risen to great heights after experiencing chronically stressful childhoods include Oprah Winfrey, who was sexually abused by family members in childhood; Starbucks' Howard Schultz, who grew up in public housing and was left alone most of the time; Supreme Court Justice Sonia Sotomayor, who suffered from diabetes from the age of 8 and who lost her father when she was 9; and basketball superhero, LeBron James, whose single mother gave birth to him when she was 16 and struggled to keep a roof over his head throughout his formative years.

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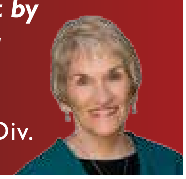
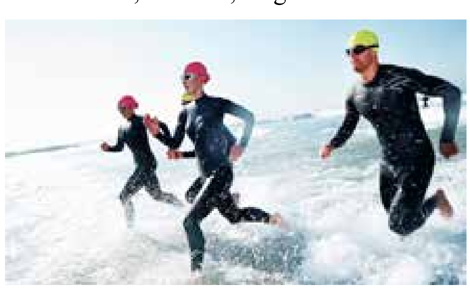


Attributes Associated with Success

How does this happen when so many "at-risk" children who suffer during childhood end up with dismal lives through no fault of their own? The Kauai Longitudinal Study, begun in 1955, continues to track the lives of approximately 700 individuals in an attempt to shed light on the phenomenon of resilience. When participants were asked how they understood their own success in spite of the hardship they had experienced as children, certain commonalities emerged. A majority described themselves as follows: 1) *determined*; 2) *an active problem-solver*; 3) *a fighter*; 4) *someone who sought out help* from friends, teachers, neighbors and relatives who cared about them; and 5) someone who, as an adult, sought out a *supportive partner* with whom to build a loving family.



Read About Adversity and Resilience

In a time of bad news, sad news, and stories of children being over-protected by their over-indulgent parents from ever having a bad day or receiving a bad grade, character matters. And good things can happen in bad places. For more on the subject, check out Dr. Jay's new book, *Supernormal: The Untold Story of Adversity and Resilience*.

Maybe just forget the New Year's resolutions this year, and read a book that will cause you to think new things. Happy New Year! ■