

Posted on Fri, Feb. 16, 2007

Don't Stop Now

Studies showing retirees may have saved more than needed aren't likely to apply to baby boomers

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Just how much should you be saving for your retirement?

Several economics professors have suggested in recent studies and newspaper articles that some Americans are, in fact, saving too much.

But others say that doesn't apply to Baby Boomers, who like to spend more than their parents did.

One study, by John Karl Scholz, economics professor at the University of Wisconsin, is based on data from the Health and Retirement Study, a national panel study of more than 12,600 people born between 1931 and 1941 now in retirement.

Scholz and his co-authors in the study "Are Americans Saving 'Optimally' for Retirement?" said that "over 60 percent of HRS households have accumulated more wealth than their optimal targets." The remaining 20 percent are very close to their targets, the study said.

A study released last week by the Employee Benefit Research Institute supports Scholz's study to a degree, stating that the majority of 65 – to 75-year-old Americans have started their retirements "reasonably successfully" in terms of income and total wealth.

Overall, about 50 percent of those in the study, which was also based on IRS data, showed no decline in household income, while 71 percent had no decrease in total wealth during the 12 - year period of the study.

"That generation has done well so far for the most part," said Craig Copeland, author of the paper and a senior research associate at EBRI.

Another economics professor, Laurence Kotlikoff at Boston University, suggests that the retirement calculators on the Web sites of major investment companies like Fidelity, Vanguard and TJASS-CREF are between 36 percent and 78 percent too high in regards to what a person should need for retirement.

"These Web calculators are telling (you) to save far too much," said Kotlikoff, who has created his own retirement calculator using underlying lifestyle and wealth calculations accepted by economists for decades at www.esplanner.com

For those of us not yet in retirement, paying attention to the HRS studies and downplaying your savings habits would be the equivalent of "financial suicide", said Steve Blankenship, CFP and principal of Heritage Financial Planning in Grapevine.

“One of the major fallacies of this study is it looks at the Bob Hope generation,” he said. “The baby boomers coming up next are on a completely different planet in terms of consumption behavior.”

Instead of cutting back on needs during retirement, Blankenship said, some recent retirees actually exceed their former incomes in spending in the first few years.

“They travel and have pent-up things they want to do,” he said.

Although that spending trend generally calms down after a few years, Blankenship said many of those facing retirement are having a hard time cutting back on expenses.

“You become addicted to your lifestyle,” he said.

So the generally accepted idea that you need a replacement rate just 75 percent and 65 percent of pre-retirement earnings may be the first principle out the window for the boomers and beyond, financial planners suggest. Many are going to want 100 percent or more.

And although they may want to spend more, many boomers have trouble committing to saving 10 percent of what they make, said Burk Rosenthal, head of Rosenthal Retirement Planning.

“Some of my clients come in who haven’t saved anything and we have to start at 5 (percent) or 6 percent, then work our way up to 10 percent,” he said. “I tell people it’s a balance between your enjoyment and lifestyle now and later.”

Steady benefits throughout retirement from pensions, Social Security and Medicare are also not as predictable for the next generation of retirees, said Copeland with the EBRJ. He said 60 percent of those in the study have no pension income, and they aren’t doing as well, he said.

“Those in the study are in a much better situation than the baby boomers will be,” he said. “Baby boomers could have to pay for more out of their own pockets.”

Longer retirements are also a factor to include in retirement planning, Blankenship said.

“We run projections beyond life expectancies, but the average retirement is a 30- to 35- year period,” he said. “For those who retire early, this could be a longer period than they worked.”

The EBRI study found that those who had experienced a decline in wealth had the worst outlook. The median average annual decline in total wealth (assets minus debt) surpassed 5 percent, meaning they are ‘at significant risk’ of outliving their assets.

Research has shown that spending under 5 percent of your assets each year will give you a higher chance of not running out of money in 20 years, EBRI said. But Blankenship cautioned that that annual spending rate should be based on a return of at least 8 percent a year from investments.

“If you’re in CDs, that’s not going to be enough growth,” he said. “Three percent (depletion of assets a year) is the sweet spot – it allows you to grow your portfolio without having to take on a lot of risk.”

Blankenship said many should consider part-time work as part of their retirement planning.

“Even five to 10 years of part-time work as a Wal-Mart greeter makes a huge difference in your financial picture,” he said. “Part-time work will be the saving grace for a lot of people in retirement.”

Blankenship and Rosenthal said they consider online retirement calculators nothing more than a tool to get people to start thinking.

“Most of them assume you get a level rate of return over time,” Blankenship said. “But volatility is Enemy Number 1 when it comes to distributions.”

Blankenship said Financial Engines (www.financialengines.com) has a retirement calculator better than average. Rosenthal provides several free calculators at his Web site, www.rosenthalretirement.com. The EBRI also has a no-cost Ballpark Estimate calculator at www.choosetosave.org.

The planners' bottom line: Most people had better keep – or start – saving for retirement.

“No one has ever said to me, ‘I wish we hadn’t put that much money away,’” Rosenthal said.

Teresa McUsic’s column appears on Fridays. Reach her at tmcusic@savvyconsumer.net

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