
Understanding Reluctant Retirees: Money and Meaning

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What does “old” mean?

Who has had Professor Methuselah in class?

He spoke with such authority on Medieval
European History –

Because.....HE WAS THERE!

Life Expectancies

Contingent upon reaching the “normal” retirement age of 65 and...

Being in the upper half of the income brackets in the US

Men: 22 years

Women: 25 years

Why Do People Retire and Return to Work?

The Top Reason...

Is not MONEY

Is not BENEFITS

Is DISSATISFACTION with retirement*

*Lahey, Kim, and Newman (2006, *Financial Services Review*)

Money and Meaning – Both Matter

Advising the reluctant retiree involves two steps..

Eliciting Preferences

Making Recommendations

There is a tendency to omit the first step in practice as no one is getting “paid” for it

Focus is on technical recommendations...

How much \$\$\$ do I need; asset allocation

Exploring Meaning First

What would an ideal day in “retirement” look like to you?

List the activities...

Some draw meaning from their occupation that cannot be replaced...loss of identity can be especially severe if the change is dramatic

The rise of the “retirement coach”

Economics of Happiness

Summarizing what is now a large literature...

Factors most commonly connected to happiness:

Faith

Family

Freedom

Meaningful Work

Charity

Diversifying Life Activities

Construct pie chart of activities

Time the scarce resource

Going from all work to all play...really?

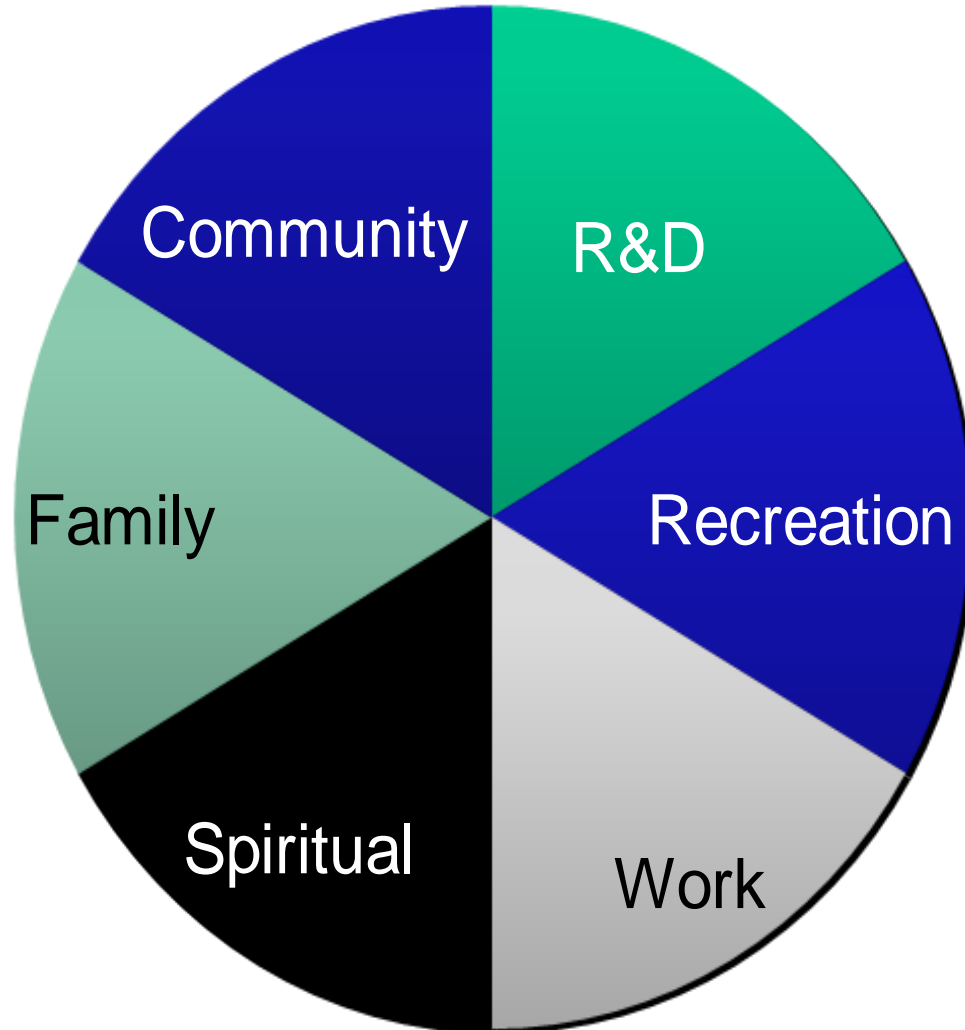
What do these activities cost....

Go-Go, Slow-Go, No-Go

First and *third* phases tend to be more expensive

Personal Activities Pie Chart

Activities



Technical Analysis

Unlike the wealth accumulation phase of earlier life...the focus now is on income

Are the sources of income you have sufficient to support the activities you envision?

Will you exercise the option to employ your human capital for pay?

Profiles of Reluctant Retirees

The Business Owner

The Defined Contribution (401-k Type Plan) Player

The Defined Benefit (Pension Plan) Player

Baseline assumptions (for simplicity):

1. Age 65 (Medicare eligible and Soc. Sec. recipient)
2. Need \$80K in income on top of \$20K from Soc. Sec.
3. Not supporting adult children or aged parents
4. No withdrawal restrictions (for those under age 59.5)
5. No liabilities; own home; decent health

Business Owner

Balance Sheet Asset is Enterprise worth \$2M

Illiquid and Undiversified

1. Owner sells business, but...
2. Owner must often stay active in business for the “earn out,” but..
3. Owner must eventually disconnect to allow new owners to assume control

Defined Contribution Player

Balance Sheet Asset is \$2M in a 401k/IRA

Can be diversified as to investments, but might not be

Is liquid, but is entirely pre-tax

Must convert asset to income, and all withdrawals are pre-tax

“Safe” withdrawal rate of 4% of balance annually adjusted for inflation (90% success – 30 years)

Defined Benefit Player

Works 40 years in a plan paying 2% of top annual salary times numbers of years worked

If top salary was \$100,000, now have ready-made \$80,000 in lifetime income (worth about \$2M)

No investment worries

Is pension fund adequately funded?

Pension Benefit Guaranty Corp limit (\$50K year)

Money Portfolio in Retirement

Construct a portfolio of **income** sources

1. Earned (human capital)
2. Investment (pre-, post-tax, ordinary accounts)
3. Intermediated (pension, immediate annuity)
4. Government (Social security)

The three previous examples show lack of diversification of income sources

Income Diversification Examples

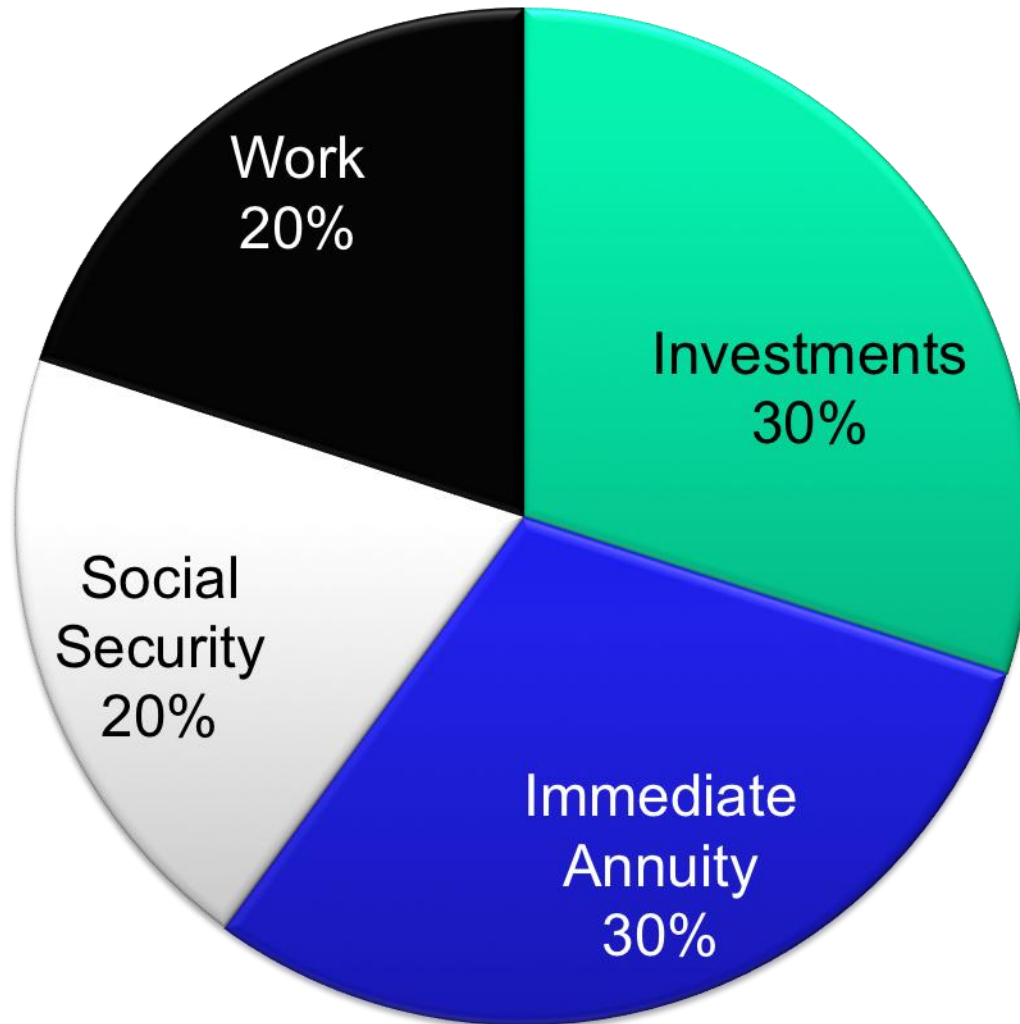
Diversify the *sources of income*

For the retiree, income volatility is the concern

**Volatile asset prices do not necessarily mean
volatile income streams...**

Retiree Income Sources Example

Income



Step Back in Time

Diversifying Income Sources by considering...

Asset **location** diversification

Pre-tax (401k; IRA; SEP/SIMPLE IRA)

Post-tax (Roth IRA; Roth 401k)

Ordinary (after tax) accounts

If your assets are primarily your business, build investments, and vice versa

Business Owner

Business Owner Implications – all human capital

Split proceeds from sale of business into income earning investments and an immediate annuity

In planning for retirement, take some money out of business and invest it

Try to fund both tax-advantaged and ordinary investments during wealth accumulation phase

Defined Contribution (401k) Player

Must produce income yourself and begin retirement largely in pre-tax investments

At retirement, split investment proceeds between investments and an immediate annuity

In planning for retirement, engage in asset location diversification

Have both pre-tax (401k), post tax (Roth), and ordinary accounts

Contribute to 401-k match level than evaluate

Defined Benefit Player

What if your pension plan has funding problems?

In planning for retirement, consider funding some alternative income sources

Contribute to a Roth IRA; home business allows for pre-tax contributions to SEP/SIMPLE IRA

Save in “ordinary” accounts that provide access to capital prior to age 59.5 without tax penalty

Summarize Implications

Business Owner – try to fund investments in pre-, post-tax, and ordinary accounts

401k Player – stop after match stops, fund a Roth IRA, hold money in ordinary accounts, develop a “1099” (home) business

Pension Player – fund investments in post tax locations & develop a “1099” (home) business

What is Retirement?

Really the *flexibility* to choose the activities in the time pie

Does not have to be all work, but is it no work?

Can be the kind of paid activity you enjoy

Change can be very hard for those whose lives are heavily based on routines

Human Capital Going Forward

Fewer pension plans...fewer full-time jobs with benefits

More part-time and project-type work; individuals working three or four jobs at a time

Household much more like a business enterprise bearing risk of future consumption

Begin diversifying income sources early

Money and Meaning Portfolios

“Retirement” is not to step back, but a step forward (into the unknown)

Why reluctant???...don't understand meaning or don't understand income sources or both

A portfolio of activities funded by a portfolio of income sources

Summary and Issues

Demographics...the march of the Centenarians!

Focus on diversification of **income** sources

Fiscal...pressure on Social Security and Medicare; uncertainty surrounding tax policy

Out of pocket medical expenses now about \$250K for average retiree, and likely to grow

Retirement is continuous in nature, better thought of as degree of flexibility than an on-off switch