RETIREMENT INCOME STRATEGIES

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After a lifetime of saving, making the transition to retirement means facing a whole new set of challenges. Today's retirees face a retirement landscape that is very different from the one their parents saw. Americans are living longer and enjoying active lifestyles, and may need to rely on their retirement strategies for longer.

Recent changes to Social Security claiming rules, rising health-care costs, and turbulent markets make maintaining a comfortable retirement lifestyle more challenging than ever. This article answers some common questions about retirement income preparation and presents you with ideas to guide your own thinking.

WHAT IS A RETIREMENT-INCOME STRATEGY?

A retirement income strategy is designed to allow you to pursue your retirement goals while helping to ensure that your money lasts as long as you do. An ideal income strategy will cover your basic expenses through guaranteed income, hedge against longevity and rising costs by pursuing growth, and give you enough flexibility to adapt to changing circumstances. For most retirees, Social Security benefits and withdrawals from personal savings will account for a significant percentage of their retirement income. To create a personal retirement-income strategy, start by answering two questions:

How Much Income Will I Need to Live Comfortably in Retirement?

To begin to answer that question, you must have an idea of your retirement goals and their associated financial costs. One way to organize your thoughts about income is to think of them as a hierarchy of needs, wants, and dreams.

Classifying your retirement expenses in these terms can help you understand how much income you will need for essential expenses and how much you will want for discretionary expenses that can be reduced in a pinch. If you can cover most of your basic needs through guaranteed sources of income, you have a lot more flexibility to adapt your retirement portfolio to changing market environments.

It also may be useful to use a top-down approach to estimate how much of your current income you will need to replace in retirement. Though many people worry that they will need to replace their entire pre-retirement paycheck when they retire, that's usually not true. Research by Fidelity found that most high-earning Americans only need to replace between 55 percent and 72 percent of their pre-retirement income.[i] Since that estimate is averaged across different income levels and lifestyle goals, it may not be valid for your personal situation. That's one of the many reasons why it's a good idea to work with a professional who can create a customized analysis of your retirement.

Where Will I Get My Income Retirement?

Most retirees depend on a mix of reliable income from sources like Social Security or pensions and withdrawals from their retirement savings. Others supplement those sources with

How much of your current income will need to be replaced in retirement?

personal dreams

A bucket list of the projects, goals, gifts, and aspirations that you dream of taking on if you have the time and resources.

lifestyle wants

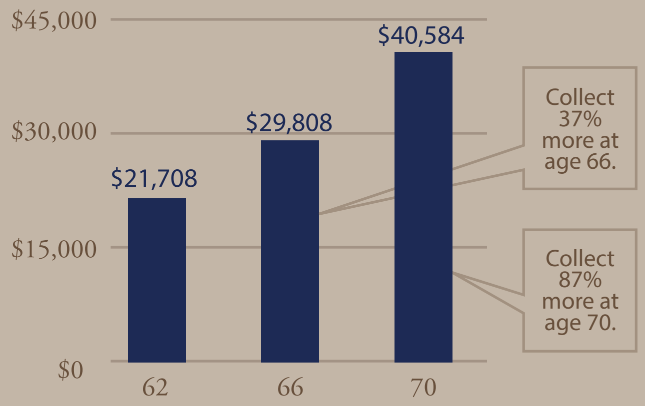
Discretionary expenses that are important to your retirement lifestyle like travel, family vacations, hobbies, education, entertainment, etc.

basic needs

Essential expenses like housing, food, healthcare, transportation, taxes, etc.

"High-earning Americans only need to replace between 55 percent and 72 percent of their pre-retirement income to maintain their lifestyle once they retire.[i]"

should i claim social security benefits now or wait?



Hypothetical calculation assumes claimant turned sixty-two in 2016 and earned $125,000 per year. Benefit amount in current dollars and excludes taxes and inflation adjustments. Source: SSA Quick Calculator

income from rental properties, businesses, or encore careers. There is no one-size-fits-all solution; a diversified income strategy should combine enough guaranteed income to cover essential expenses, with potential growth to fight inflation, and be flexible enough to keep up with changing priorities and market conditions. *

Identifying your known sources of retirement income will help you estimate how much you will need to generate from your investments each year. One study found that workers who earn between $50,000 and $300,000 pre-retirement should count on generating about 45 percent of their retirement income from their retirement portfolio.[ii] Again, this is an estimate that may not hold true for your personal situation, but it may be useful as a starting point for analysis.

Another factor to consider is how much income can be generated by your portfolio without running out during your lifetime. While you may have heard about the "4 percent" rule of thumb for annual retirement withdrawals, research suggests that most retirees cannot rely on a simple yardstick for something so complex.[iii] It's very difficult to know in advance what you can safely withdraw from your portfolio each year, since it depends on many interdependent variables, like market performance, expected life span, inflation, and more. As professionals we use sophisticated software and test many assumptions to help our clients prepare for a variety of scenarios.

One major risk that today's retirees have to contend with is the effect of volatility and market corrections on their portfolio returns. If you are forced to withdraw too much from your investments during periods of poor performance, you risk emptying your portfolio too fast. By building flexibility into your strategy and carefully managing risk, you can help reduce the effects of these negative periods on your retirement.

HOW CAN I MAXIMIZE SOCIAL SECURITY BENEFITS UNDER THE NEW RULES?

One of the most important decisions you and, if you are married, your spouse will have to make is when to start claiming Social Security benefits. Since Social Security benefits are guaranteed for life and will increase over time with inflation, they form the foundation of most retirement-income strategies. Married couples have more claiming options to consider, and the right claiming strategy can help increase joint income and leave a larger survivor's benefit to a spouse, though it might mean giving up some income early in retirement or working longer.

The rules of Social Security allow a worker or spouse to begin claiming benefits as early as age sixty-two, but beneficiaries accrue delayed retirement credits for every month they delay claiming until age seventy. By waiting, you can collect up to 8 percent more each year.[iv] Married couples also have the option of allowing one spouse to claim a spousal benefit on the other person's work record if the benefit is larger than their own or they do not qualify for a personal benefit.

Social Security rules recently changed, and two claiming strategies ("file and suspend" and "claim now, claim more later") are going away. Some couples who are already using these strategies or meet age requirements may still be able to take advantage of them. If you believe that you should be grandfathered in under the old Social Security rules, contact your financial professional immediately.

Though the expiration of these two advanced claiming strategies takes away some options for retirees, making the right choice

about when to claim is still critical to maximizing this essential source of income. For most retirees, two main questions will drive their Social Security claiming decisions:

- How long do you and your spouse expect to live?
- Can you afford to delay claiming benefits to accrue additional credits?

In general, if at least one member of a couple expects to live until age eighty, deferring benefits to claim more money later may make sense if you can afford to do so. However, if health issues or family history make a long life span unlikely, claiming benefits earlier may be wiser. If you would like help analyzing your options, a financial professional can run the numbers on different claiming scenarios to help you make a more educated decision.

SHOULD I RETIRE EARLY OR WAIT?

Some retirees are counting the days until they can pack their desks and go. Others identify closely with their work and can't imagine life without a career. Wherever you fall on that spectrum, the choice of when to retire can have an enormous impact on your retirement strategies.

Don't forget about health insurance and medical care as well. If you currently receive health coverage through your employer, you might get sticker shock when you see what it would cost to purchase Medicare or private insurance. Delaying retirement for even a few years can substantially increase your retirement savings and improve your retirement options.

However, there are other lifestyle factors to consider. If you are confident in your retirement preparations and have a strong desire to stop working and start your next phase of life, retiring now might be worth the additional risk. Part of creating a personal retirement strategy is understanding which risks you're willing to embrace.

HOW WE CAN HELP

Saving and investing for retirement is just the first step. Developing an income strategy and maintaining it over time is a very different challenge. If you're not certain about your retirement strategies, you're not alone. A 2015 survey found that just 22 percent of Americans feel very confident about having enough money to live comfortably in their retirement years. [v]

We take an approach to retirement income that is based on an analysis of your personal financial situation and your goals for retirement. We'll work with you to identify sources of income and develop a cash-flow strategy that takes into account the timing of future expenses and balances income with your need for growth to protect against rising costs. If you or anyone you know has questions about building a personalized retirement-income strategy, please contact our office at 919-657-4201; we'd be delighted to be of service.

Potential sources of income during retirement:

- social security
- pension
- workplace retirement plan
- inheritance
- business interest
- post-retirement employment
- rental income
- investments
- insurance products

Footnotes, disclosures, and sources:
Investment advice offered by Capital Financial Advisory Group, LLC, a North Carolina registered investment advisory firm.

Insurance advice offered by Capital Financial & Insurance, LLC - Licensed with the North Carolina State Department of Insurance.

Always consult with a qualified investment, legal or tax professional before taking any action.

[i] "Where will my retirement income come from?" Fidelity. https://www.fidelity.com/viewpoints/retirement/retirement-income-sources [Accessed 16 February 2016]

[ii] "Where will my retirement income come from?" Fidelity. https://www.fidelity.com/viewpoints/retirement/retirement-income-sources [Accessed 16 February 2016]

[iii] "Leveraging Behavioral Simulation to Enhance the Four Percent Rule." PwC. http://www.pwc.com/us/en/insurance/publications/assets/pwc-behavioral-simulation-four-percent-rule.pdf [Accessed 16 February 2016]

[iv] "Social Security Benefits." Social Security Administration. https://www.ssa.gov/oact/quickcalc/early_late.html [Accessed 16 February 2016]

[v] "2015 Retirement Confidence Survey Fact Sheet #1." Employee Benefit Research Institute and Greenwald & Associates. https://www.ebri.org/files/RCS15.FS-1.Conf3.pdf [Accessed 16 February 2016]