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5 key risks to lifetime retirement income: what to do in 2008

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If you have been following the markets these past few months, you may be wondering if the strategies that have grown your retirement nest egg in the past are right for you today. Also, if you are approaching retirement or about to retire, you may be concerned that the turbulent investment climate could wipe out a portion of your retirement savings.

The Importance of a Lifetime Income Strategy

My father retired at age 62 with a lifetime income adjusted for inflation that he cannot outlive. He worked in the public sector where employees have a defined benefit pension plan that will provide guaranteed income for life. I always tell him he has a wonderful retirement package because the monthly check that covers his expenses will always arrive. It doesn't matter what happens to the stock market performance or how long he lives.

The rest of us, on the other hand, need to design our own lifetime retirement income plan from the nest egg we have spent decades growing. This is especially important if you do not have any source of guaranteed retirement income besides social security.

Five Key Risks to a Lifetime Retirement Income

In retirement, financial mistakes can be magnified and unplanned events can put much of your nest egg at risk. That's why it is vital to consider - and manage - these five key risks when designing a lifetime income plan. Over 20 years of working with clients I have faced these hazards time and time again.

1. Longevity: Many people underestimate their life span and risk outliving their assets. This is a mistake you obviously want to avoid.

2. Health Care Expenses: You may have seen the recent headlines where it was estimated that a couple who retires in 2008 will need $160,000 set aside today to cover their health related costs (1). And, obviously, this number could get worse as healthcare costs continue to escalate. Rising health care costs coupled with inadequate health care coverage can put big holes in a retirement income plan.

3. Inflation: Yes, it's back. The recent trend of rising energy and commodity prices has brought this risk back into the mix. Inflation increases the future costs of goods and services and may erode the value of assets set aside to meet those costs.

4. Asset Allocation: After decades of saving, many couples can transition quickly from peak accumulation and maximum retirement contribution to preservation and withdrawal. This usually means an entirely different asset allocation strategy. Retirees with a portfolio overly concentrated in conservative or aggressive investments expose themselves to a greater risk of outliving their assets.

5. Withdrawal Rate: Aggressive withdrawal rates increase the likelihood that retirees will deplete their assets prematurely. Withdrawals need to be managed ideally so that you are never forced to

take from the equity side, especially during a correction or bear market.

Now that we see the risks to avoid, let's examine key steps to build a firm foundation for your Retirement Income Plan.

The Foundation for a Successful Retirement Income Plan

One of the first steps a good financial planner usually takes is a personal retirement income audit. Simply, this is a retirement spending analysis. We look at basic monthly essential expenses such as food and housing and monthly discretionary expenses such as travel and entertainment. We then find out how to match your basic expenses with guaranteed sources of income such as social security, a pension, or annuities.

These guaranteed sources of income will last for your lifetime and give you the peace of mind that a check will always arrive.

We than can invest the remaining assets to accumulate for future needs. Although we have a conservative investment strategy, we are able to invest for a greater return because we have the basic expenses covered . . . for life.

Once you feel comfortable with your retirement income plan, you also need to address future long-term health care. If you need "in home" health care or more advanced care, the question is, "How will you pay for it?" There are many strategies available, but it is essential to plan in advance.

Lastly, you will want to make sure that whatever assets are remaining in your estate transfer smoothly to your family. If your estate plan is messy, you could be subjecting your estate to the delays and expense of the probate process and unnecessary estate taxes.

A good retirement income plan will give you comfort that:

* You have covered your basic expenses through guaranteed income sources,
* You have addressed your long-term health care options, and
* You have developed a plan to smoothly transfer your remaining assets to your family.

Surviving the Current Environment and Preparing for a Lifetime Income

A note of caution: If you hire a broker who is still focused on accumulating your nest egg, you may lose out on effective retirement income planning strategies. If you try to do it yourself, you may miss out on the wisdom that comes from having experienced many investment cycles.

Consider a financial planner who specializes in preparing a sound foundation for your retirement.

In summary, a well thought out plan will address your lifetime income needs, protect you from the high costs of long term health care and smoothly transition your remaining assets to your family. You will be able to sleep well at night-through good and bad markets-knowing you can rely on a solid plan.

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