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Setting Realistic Goals for 21st Century Retirement

Given rising healthcare costs, longer lifespans and the growing need for family assistance among both millennial children and elderly parents, retirement is only becoming more costly. However, many early and pre-retirees maintain unrealistic expectations regarding the lifestyles they'll be able to maintain.

“So many clients have just avoided planning altogether and have nonchalant attitudes that everything will work out," said Angie M. Granger, President and CEO of Black Belt Financial and Insurance Services. "People aren't aware how much their lifestyles are costing them."

Still, senior clients want to enjoy retirement, and most are reluctant to significantly change the ways they live once they stop working. With less income and more time on their hands, poor financial planning can lead long-lived clients to run out of money far before their retirements are through. To help recent and soon-to-be retirees find a sustainable balance between enjoyment and saving, advisors need to help these clients understand their current expenses, future expenses and the abilities of their portfolios to cover both.

The Day-to-day Costs of Retirement

Even among clients who've monitored their expenses throughout their working lives, many have unrealistic expectations of how much they'll spend in retirement. "The historical mindset has been that we spend less in our retirement years, but the reality from my perspective is that people end up spending the same, if not more," said Ann Margaret Carrozza, New York-based state and elder law attorney. Early retirees often spend extra on travel, more active social lives and gifts for grandchildren, while older seniors usually face far higher medical bills.

Unaccounted-for expenses also chip away at many retirees' portfolios. Costs such as rent, mortgages, car payments and insurance are easy to track, but even experienced savers may drastically underestimate how much they spend on fuel, food and other month-to-month variables. Coffee shop coffees, take-out and myriad other convenience items also become far bigger burdens on a fixed income. "It's very tough to go from $120,000 per year to having to live on $5,000 or $6,000 per month, even though that's not a small income," said Karen Lee, CFP at Karen Lee and Associates. "It's very hard for people to change spending habits at that age."

Aside from ongoing pre-retirement expenses, the additional free time retirees enjoy presents far more opportunities to spend. "Clients often have the wrong idea of what it's going to mean to have more free time on their hands, and what that's actually going to cost," said Angie Grainger, President and

CEO of Black Belt Financial and Insurance Services. “If your life isn't designed in a way that gives you fulfillment, you're going to end up spending even more.” Shopping and dining trips, extra vacations and impulse buys become far more common for some clients, particularly those who are single or socially isolated.

Family Assistance

Another increasingly common cost among early retirees is financial assistance for adult children. Millennials are still facing a tough job market, and according to Carrozza, roughly 48 percent of all Baby Boomers and older adults are helping their children with housing, loans or other bills.

In fact, retirees are taking on a dramatically rising proportion of student loan debt, typically after co-signing their children and grandchildren's loans. According to the Government Accountability Office, student debt among seniors 65 and older grew from $2.8 billion in 2005 to $18.2 billion in 2013 and now accounts for over 15 percent of the total burden nationwide.

At the same time, longer lifespans and steep medical bills have lead many of the nation's most elderly to depend on their retired and soon-to-be retired children for help. A Pew study found that roughly one in seven adults in this “sandwich generation” is financially assisting both an aging parent and adult child.

Rising Prices

Finally, even among retirees who religiously track their spending, disproportionately rising prices and unpredictable expenses can significantly increase the cost of retirement. These increases are particularly burdensome for those who require extensive medical care. “With healthcare costs we've seen an annual increase of 12 percent per year on the hospital side,” said Carrozza. “Even though most retirees will have Medicare and supplements, out-of-pocket costs still go up every year.”

Long-term care in one form or another is also a likely prospect for most retirees, though many hesitate to spend money on LTC insurance. “It's the elephant in the room,” said Carrozza. “Today's retirees and pre-retirees absolutely need to inform themselves about long-term care insurance, both traditional and hybrid.”

Aside from healthcare and health-related expenses, the prices of goods and services most important to seniors may be outpacing investment returns and Social Security adjustments. Social Security's cost of living adjustment is currently based on the CPI-W, which accounts for items wage earners – not retirees – most often buy. “Inflation statistics don't factor in the items seniors care about, and real costs are outstripping most retirees' portfolios,” said Carrozza.

Planning Ahead

Fortunately, there are plenty of steps clients can take to save money, avoid unnecessary expenses and maintain comfortable lifestyles, particularly if they're still working or have only recently retired. For many, proper planning begins with an honest assessment of current expenses. “Look at the last 12 months of what clients have actually spent before looking at income,” said Lee. Because long-term changes in spending habits can be so difficult – and because pre-retirees may be willing to work longer to provide for more expensive lifestyles in retirement – higher-than-expected costs lead many to work longer, pay down debts and grow investments. For clients already approaching set retirement dates, Lee similarly recommends that they track their total expenses six months in advance, and that they establish solid spending habits by remaining under those numbers for the first six months of retirement.

Clients who begin planning early enough might also be able to avoid reliance on savings and non-guaranteed sources of income. “Fill your baseline needs with guaranteed income,” said Grainger. “Create a 'retirement paycheck' with components like Social Security and pensions.” Lee likewise noted that the “safety percentage” for stock investments hovers under four percent, and that many clients still unsafely assume they'll be able to count on returns of up to ten percent.

In facing the likely costs of long-term care, retirees can choose from a variety of LTC insurance products that don't require them to risk “wasting” their money on policies they may not use. Many hybrid plans allow death benefits to be used towards long-term care if necessary, and older plans may be able to be converted into new ones that include the same provision.

When it comes to the uncertainty of healthcare costs, price increases and other unknowns, many advisors also recommend setting aside a little extra – even if that means downsizing or working a little longer. “The best thing you can do is to go into retirement with a little more than the plan says you need,” said Lee. Medicare means-testing may change, private insurance premiums may rise, and although some legislators are attempting to tilt the cost of living adjustment calculation in seniors' favor, prices may continue to outstrip Social Security increases.

Ultimately, the best thing a client of any age can do is to consult with an advisor as soon as possible regarding their likely expenses and income in retirement. “If you're not saving for retirement, then you're not living within your means,” said Grainger. “The sooner you can take the time to plan and be honest about what your lifestyle is costing, the better chance you'll have at maintaining that lifestyle in retirement.”

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