INVESTMENTS & WEALTH MONITOR

A reprinted article from May/June 2020

The Risks and Challenges of Retirement Planning: An Interview with Robert Powell, CFP®

INVESTMENTS & WEALTH INSTITUTE®

THE RISKS AND CHALLENGES OF RETIREMENT PLANNING

An Interview with Robert Powell, CFP®

To discuss the risks and challenges of retirement planning, we tapped one of the industry's leading experts, Bob Powell, who is editor of the Retirement Management Journal *and a member of the* Investments & Wealth Monitor *editorial advisory board. Powell has more than 30 years of experience in the ever-changing retirement industry.*


Robert Powell, CFP®

***I&WM*:** The retirement industry has changed quite a bit since you began your career. It has evolved in the types of investments available, the movement from defined benefit plans to defined contribution plans, and the challenges it poses for advisors. What do you think the biggest challenges have been for advisors?

Powell: I think the challenges are two-fold.

First, most advisors were trained to help their clients plan for retirement. They were trained to help their clients accumulate—through savings and investing—enough financial capital to retire to a desired standard of living.

They did not, however, receive training to help their clients live in retirement. They were not trained to help their clients "decumulate" their financial capital. They were not trained to construct retirement-income plans that would help their clients create desired outcomes and address multiple goals, such as the need for lifetime income; the need to integrate the multiple sources of income in retirement from financial capital, human capital, and financial capital; the need to manage the risk of longevity and other risks unique to retirement; and the need to create, if so desired, bequests and legacy goals.

The second big challenge is something I'll describe as "over-the-transom" issues that have made retirement a complicated subject, one filled with conflicting and contradictory information that results in confusion and perhaps even inertia.

Consider the following: Over the past 30 or so years, we have witnessed the launch of new products (reverse mortgages, qualifying longevity annuity contracts, and long-term care insurance policies paired with life insurance and annuities, for instance); the enactment of new laws, rules, and regulations (the Pension Protection Act of 2006, the Bipartisan Budget Act of 2015, the Tax Cuts and Jobs Act of 2017, the SECURE Act of 2019, and the CARES Act of 2020, for instance), and the introduction of new types of accounts (health savings accounts, Roth individual retirement accounts, and Roth 401(k) plans, for instance).

And then there's a vast array of research published each and every day that expands the body of knowledge in a much-needed way but also creates bewilderment and befuddlement.

Consider just these two books, one by Jeremy Siegel, a professor of finance at The Wharton School of the University of Pennsylvania, titled *Stocks for the Long Run*, and the other by Zvi Bodie, a professor emeritus at Boston University's Questrom School of Business, titled *Risk Less and Prosper: Your Guide to Safer Investing*. These two books reach entirely different conclusions about how to invest for and during retirement.

***I&WM*:** This issue of *Investments & Wealth Monitor* focuses on managing retirement risks. What are the risks that advisors need to tackle for their clients?

Powell: In the Retirement Management Advisor® (RMA®) curriculum, we examine retirement risks in a comprehensive manner that is different from traditional retirement planning. First, we consider specific risks faced by retirement-income clients (market, issuer/credit, inflation/deflation, household shock, spending, income, healthcare expenses, longevity, and public policy), and then we map the specific risks into four risk categories (political, business, behavioral, and chance). And we also map the retirement risks into systematic and unsystematic categories.

Table 1 shows the retirement risks the RMA curriculum considers relevant.

The RMA curriculum also presents a framework to analyze and present systematic and unsystematic risk exposures in a way that is aligned more with the principles of risk management than with

Table 1

RETIREMENT RISKS

Systematic Risks		Unsystematic Risks	
Political	**Business**	**Behavioral**	**Chance**
Public policy	Market	Spending	Household shock
Inflation	Issuer		Health care
	Income		Longevity

the principles of investment management (see table 2).

For instance, the RMA curriculum suggests that a risk is relevant to an investor when all of the following four questions have affirmative answers:

> *Does the risk involve an identifiable hazard?*
>
> *Does the investor have exposure to the hazard?*
>
> *Are the consequences too severe for the investor to ignore?*
>
> *Is the probability of negative consequences high enough to make the combination of the above relevant?*

Table 2 shows the framework an advisor would use to identify why and when a risk becomes relevant to a client.

Another point about risk with respect to retirement: An advisor should be able to explain the differences between risk tolerance, risk profile, risk aversion, risk exposure, and risk capacity. As I've noted, risk exposures can be identified and integrated into the analysis of the client's household balance sheet. But the key term in the RMA curriculum is risk capacity. An advisor must develop an understanding about how risk capacity can be measured and integrated into the development of a retirement allocation recommendation.

An important component in the calculation of a client's risk capacity is sequence-of-consumption risk, because the present value of consumption in retirement is typically the largest liability on the household balance sheet.

Lastly, advisors need to understand how to integrate risk exposures with available risk management techniques, techniques I should note that have been long established in the world of risk management.

***I&WM*:** Some pundits have indicated that there is a "retirement crisis," saying that investors haven't saved enough to retire and that some retirees have had to go back to work because they fear outliving their savings. Do you think that there is a retirement crisis? How can advisors address retirement more effectively?

Powell: It's hard to assess whether there's a retirement crisis. On the one hand, experts such as Andrew Biggs, a former principal deputy commissioner at the Social Security Administration and now an economist with the American Enterprise Institute, argues—persuasively—that there is no crisis, that the date researchers use to calculate whether there is a retirement crisis is inaccurate, and not to be trusted.[1]

On the other hand, experts such as Alicia Munnell, director of the Center for Retirement Research at Boston College and co-author of *Falling Short: The Coming Retirement Crisis and What to Do About It*, argues—equally persuasively—that 50 percent of households are at risk of not having enough to maintain their living standards in retirement.[2]

My thought is this: Which would be a worse outcome? To be proven right or to be proven wrong? To say there is no crisis and learn to the contrary years later that there was a crisis and you did nothing to prevent it, or to say there is a crisis and you do all you can to prevent it now while there's still time?

***I&WM*:** Whether or not there is a retirement crisis, a couple issues warrant further attention. Individuals are living longer, more-productive lives; therefore, the financial models need to anticipate a longer time in retirement and the numbers used for modeling need to be adjusted to reflect the current market environment. How do you respond to these limitations?

Powell: All models and assumptions need to change to accommodate the fact

Continued on page 39 →

Table 2

RETIREMENT RISK EXPOSURE MAP

	Systematic Risks					Unsystematic Risks			
	Political		**Business**			**Behavioral**	**Chance**		
Retirement income risk matrix	Public policy	Inflation	Market	Issuer	Income	Spending	Household shock	Health care	Longevity
Hazard									
Exposure									
Consequences									
Probabilities									

INTERVIEW WITH ROBERT POWELL

Continued from page 6

that individuals are living longer, more-productive lives and that the odds of spending not just 30 years but 40-plus years in retirement are increasing. There are limitations to the current software and models. So, advisors—to the degree they can—will have to create retirement-income plans for clients that incorporate a wide variety of scenarios and factors: anticipated age at retirement; whether someone will have earned income in retirement; the degree to which a client will use home equity for retirement income; whether Social Security claiming strategies will play a role in a client's retirement-income plan; which planning horizon to use (age 95 is becoming the standard); retirement risks beyond longevity and inflation; which accounts, investments, and products can be or should be used to produce the most tax-efficient income in retirement; and the list goes on.

Suffice to say I think advisors will have to create multiple plans for clients—a best-case plan, a worst-case plan, and a probable-case plan—and then monitor and revise these at least once per year.

I often like to joke that if you told me your date of death, I could build a bullet-proof retirement-income plan. But in the absence of not knowing that one little fact, advisors will have to employ, as Mad-Eye Moody (of *Harry Potter* fame) used to say, constant vigilance with their clients' retirement-income plans. Setting it and forgetting it will never be an option.

Suffice to say I think advisors will have to create multiple plans for clients—a best-case plan, a worst-case plan, and a probable-case plan—and then monitor and revise these at least once per year.

***I&WM*:** Lastly, how can our members keep informed of the changes in retirement planning? How can members receive more information about the RMA program?

Powell: Keeping apprised of changes in retirement planning is a tall order. Each and every day, there are new laws, regulations, rules, research, and products to learn about. I would recommend a few ways to stay informed: Read the major publications, including the trade publications focused on retirement. Attend the Investments & Wealth Institute's Retirement Management Forum, and read the *Retirement Management Journal* and other Investments & Wealth Institute publications.

Contact Robert Powell at retirementweekly@gmail.com. And, to get more information about the RMA program, visit https://investmentsandwealth.org/rma.

ENDNOTES

1. See Andrew Biggs, "The Phony Retirement Crisis," *Wall Street Journal* (February 28, 2019), https://www.wsj.com/articles/the-phony-retirement-crisis-11551398196; Andrew G. Biggs and Sylvester Schiever, "Is There a Retirement Crisis?" *National Affairs* 42 (winter 2020), https://nationalaffairs.com/publications/detail/is-there-a-retirement-crisis; Andrew G. Biggs, "Fears of a Retirement Crisis Are Overblown," *MarketWatch* (July 21, 2019), https://www.marketwatch.com/story/fears-of-a-retirement-crisis-are-overblown-and-these-numbers-prove-it-2019-07-17?ns=prod/accounts-mw; and Andrew Biggs, "No, Half of Older Americans Aren't Without Retirement Savings," *Forbes* (March 27, 2019), https://www.forbes.com/sites/andrewbiggs/2019/03/27/no-half-of-older-americans-arent-without-retirement-savings/#5df48d8ae664.
2. See "National Retirement Risk Index," Center for Retirement Research at Boston College, https://crr.bc.edu/special-projects/national-retirement-risk-index/; and "Challenges of Retirement Policy, Social Security Reform, and Retirement Income: A Discussion with Alicia H. Munnell, PhD," *Retirement Management Journal* 8, no. 1 (2019).

REFERENCES

Bodie, Zvi. 2012. *Risk Less and Prosper: Your Guide to Safer Investing*. Hoboken, New Jersey: John Wiley & Sons, Inc.

Ellis, Charles D., Alicia H. Munnell, and Andrew D. Eschtruth. 2014. *Falling Short: The Coming Retirement Crisis and What to Do About It*. New York: Oxford University Press.

Siegel, Jeremy J. 1998. *Stocks for the Long Run* (2nd ed.). New York: McGraw-Hill.

INVESTMENTS & WEALTH INSTITUTE®

5619 DTC Parkway, Suite 500
Greenwood Village, CO 80111
Phone: +1 303-770-3377
Fax: +1 303-770-1812
www.investmentsandwealth.org