

Rethinking Retirement

A Retirement Realities Study





NEW RETIREMENT REALITIES

The quest for a comfortable retirement is challenging. American retirees are facing the potential of longer life expectancy, rising health care costs and disappearing pension plans. After more than a decade of economic upheaval, market volatility, and low interest rates, individual investors and their financial advisors are seeking solutions that can help make the idea of a comfortable retirement a reality.



RETHINKING RETIREMENT 2021 SURVEY

A survey of Investors on Risk offers valuable insights for individual clients and financial professionals. The survey's results include:

- // **Discoveries** about investors' current attitudes toward risk and their approaches to investing.
- // **Misconceptions** about bond market risk, future market returns, and retirement income levels.
- // **Opportunities** to build portfolios that are better suited to risk tolerance and retirement income needs.

SURVEY DEMOGRAPHICS

This WealthVest survey included 536 respondents from across the United States and has a margin of error of +/- 4%. All respondents were ages 45 and older and were managing their personal assets. Fifty-two percent were female, and forty-eight percent were male. Thirty-one percent had been investing for fifteen or fewer years. The majority had been investing for longer. Fifty-four of respondents earned less than \$100,000 each year, twenty-nine percent earned more, and seventeen percent preferred not to provide an answer.





DISCOVERY #1: AMERICANS ARE MORE RISK AVERSE

In 2001, a quartet of psychologists published *Bad is Stronger Than Good*, a research paper that explored the effects of positive and negative experiences. It concluded that people are more affected by bad outcomes than good ones, and they are more highly motivated to protect against failure than to pursue success.¹ It's a phenomenon that is currently playing out among investors in the United States.

Following more than a decade of negative economic and market events, Americans appear to have lost their appetite for risk.

80%

of investors are less or as comfortable with investment risk today as they were a decade ago.

REGARDLESS OF THEIR INVESTMENT EXPERIENCE, TODAY'S NEAR-RETIREEES WANT LESS OR AS MUCH RISK.

Q: HOW HAS COVID-19 CHANGED YOUR INVESTOR BEHAVIOR?



1. Baumeister, Roy F. Bratslavsky, Ellen. Finkenauer, Catrin. Vohs, Kathleen D. "Bad Is Stronger Than Good," Review of General Psychology 2001, p. 351 <https://bobsutton.typepad.com/files/bad-is-stronger-than-good.pdf>

The majority of people surveyed — regardless of investment experience, affluence, gender, or geographic area — indicated they were more or as risk averse today, than they were a decade ago. In general, **the longer they'd been investing, the more likely it was their investment risk tolerance had declined.** To some extent, this may reflect a natural shift toward asset conservation as retirement nears. However, a percentage of respondents were a decade or so away from retirement, so increased risk aversion may also reflect negative market experiences.

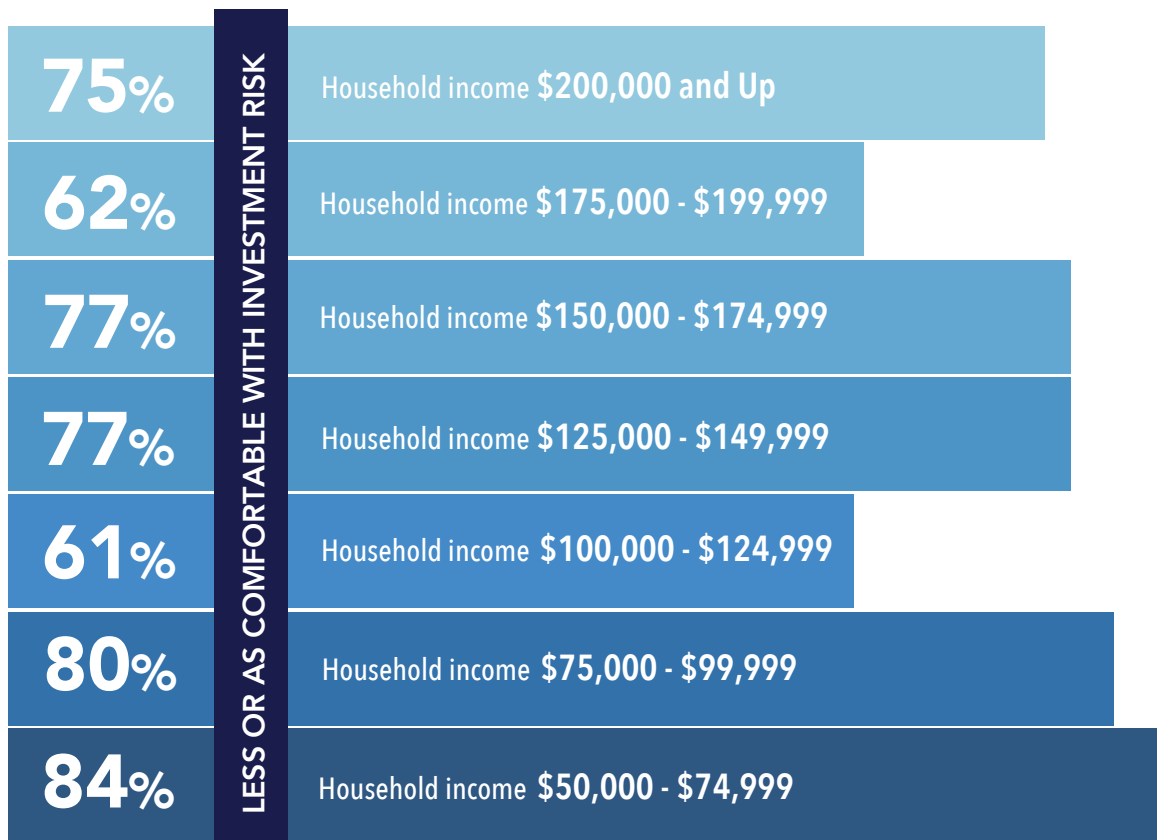
75%

of Americans earning \$200,000 or more are less or as comfortable with risk as they were a decade ago.

In the third quarter of 2020, 28.6 million baby boomers were retired, with 3.2 million more retiring in 2020² from the same quarter of 2019. Increased risk aversion creates some significant retirement planning challenges.

ALL INCOME GROUPS WANT LESS OR AS MUCH RISK TODAY AS THEY DID 10 YEARS AGO.

Q: HOW HAVE YOUR VIEWS OF RISK CHANGED DURING THE PAST DECADE?



2. Fry, Richard. "The Pace of Boomer Retirements Has Accelerated in the Past Year." Pew Research Center. Pew Research Center, November 10, 2020. <https://www.pewresearch.org/fact-tank/2020/11/09/the-pace-of-boomer-retirements-has-accelerated-in-the-past-year/>.



DISCOVERY #2: MANY INVESTORS WANT NO-RISK INVESTMENTS

Americans want to keep their retirement savings safe. About 26% of respondents would not be comfortable losing any of their retirement savings, and 38% were willing to lose 5% or less. Principal risk was slightly more palatable to respondents with higher earnings; however, **a significant percentage at each income level are unwilling to risk any savings at all.** With larger stock market gains since our last survey came out, respondents are more willing to take a loss, but would still prefer little to no loss.

Risk and reward can be related, but during periods of market volatility, and for investors nearest to retirement, risk can prove to be disruptive of retirement peace of mind and destructive to retirement assets.

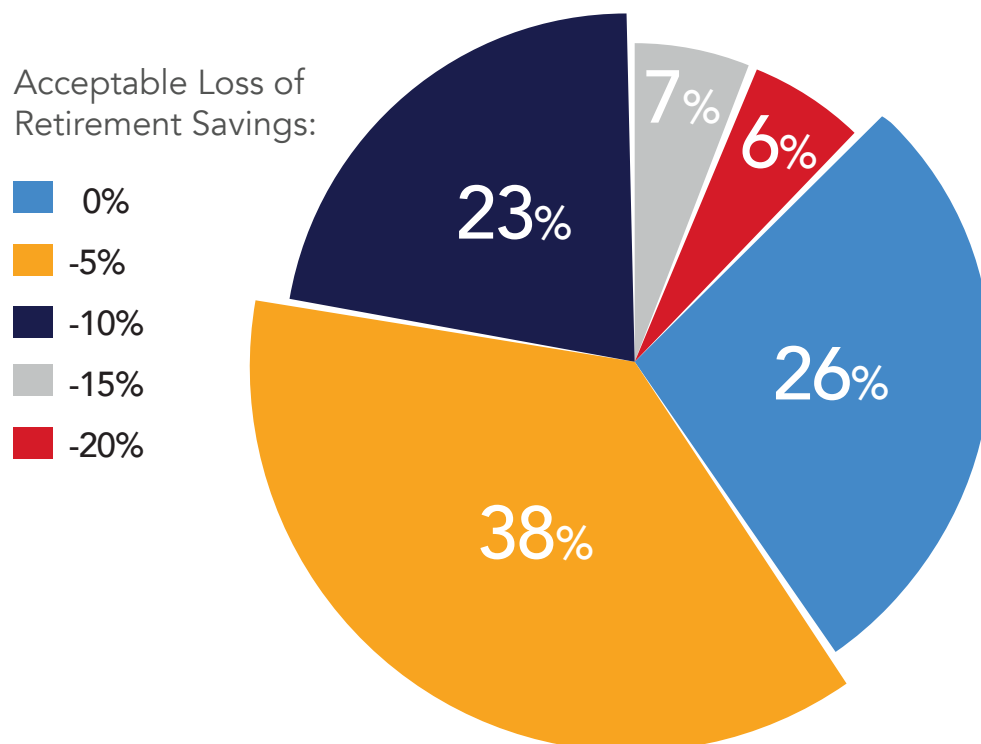
59%

of investors have a greater fear of outliving their money than death

64%

of investors want 0% to 5% retirement savings risk.

Q: WHAT AMOUNT OF YOUR RETIREMENT INVESTMENTS ARE YOU COMFORTABLE LOSING?

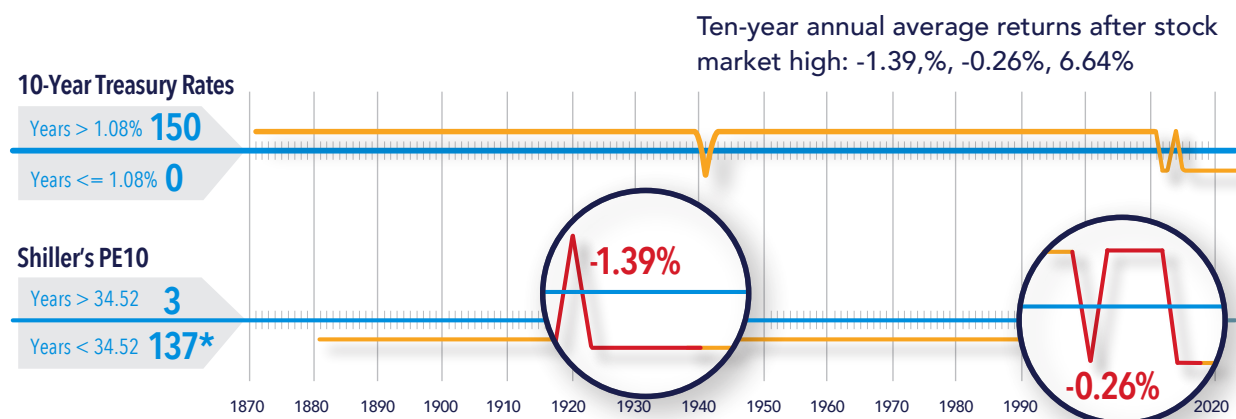


The current combination of high stock valuations (P/E 10)³ and low bond yields (10-year Treasury rates) is unprecedented in U.S. history. Stock valuations have reached these levels three time periods during the past 150 years (1929, 1997-2002, 2004-2007), and outside the last few years, bond yields have been this low just once before. Never during that period have both events occurred simultaneously. We're in uncharted territory.

Investors face the possibility that stock valuations may move lower, and interest rates may push higher. Because rising interest rates tend to lower the value of a bond portfolio, retirees now face a market environment where stocks and bonds may present a more-than-average level of risk.

SHILLER P/E 10⁴: "The P/E 10 ratio is a valuation measure, generally applied to broad equity indices, that uses real per-share earnings over a 10-year period. The P/E 10 ratio uses smoothed real earnings to eliminate the fluctuations in net income caused by variations in profit margins over a typical business cycle. The ratio was popularized by Yale University professor Robert Shiller, who won the Nobel Prize in Economic Sciences in 2013. It attracted a great deal of attention after Shiller warned that the frenetic U.S. stock market rally of the late-1990s would turn out to be a bubble."

FINANCIAL MARKET ENVIRONMENT AT THE START OF THE YEAR, 1871-2020



Over the past 150 years, interest rates have only been this low one previous period, in the 1940s. Stocks have been this expensive three other times in the past 150 years. Investors were deeply disappointed during the aftermath of each market high. The following ten years for each period resulted in low investment returns. Our recent bond and stock markets are the only time that both stocks and bonds have been this overvalued at the same time. **2008 is a particularly interesting case as 10-year returns after the great recession average only 6.64%. Despite a 10-year bull market, these returns are only slightly above average stock returns since 1871.**

*PE10 can only be calculated since 1881, since the years 1871-1880 are required to calculate smoothed earnings.

CHART SOURCE: Own calculations from Robert Shiller's financial market data <<http://www.econ.yale.edu/~shiller/data.htm>>

Past performance may not be used to predict future results

- Robert Shiller, U.S. Stock Markets 1871-Present and CAPE Ratio, January 13, 2020 <<http://www.econ.yale.edu/~shiller/data.htm>>
 Yale professor Robert Shiller developed a price-to-earnings ratio that is based on average inflation-adjusted earnings from the previous decade. It is known as the Cyclically Adjusted PE Ratio (CAPE Ratio), Shiller PE Ratio, or PE 10. The higher the PE10, the more expensive stocks are relative to their 10 year average earnings. 2020 was one of only eight years in U.S. stock market history when the PE10 began the calendar year above 28.38. The PE10 has averaged just 16.69 since 1881.
- Will Kenton, "P/E 10 Ratio," Investopedia, January 9, 2018, <<http://www.investopedia.com/terms/p/pe10ratio.asp#ixzz4YtmafJaB>>.



DISCOVERY #3: MANY AMERICANS ARE INVESTED IN RISKY ASSETS

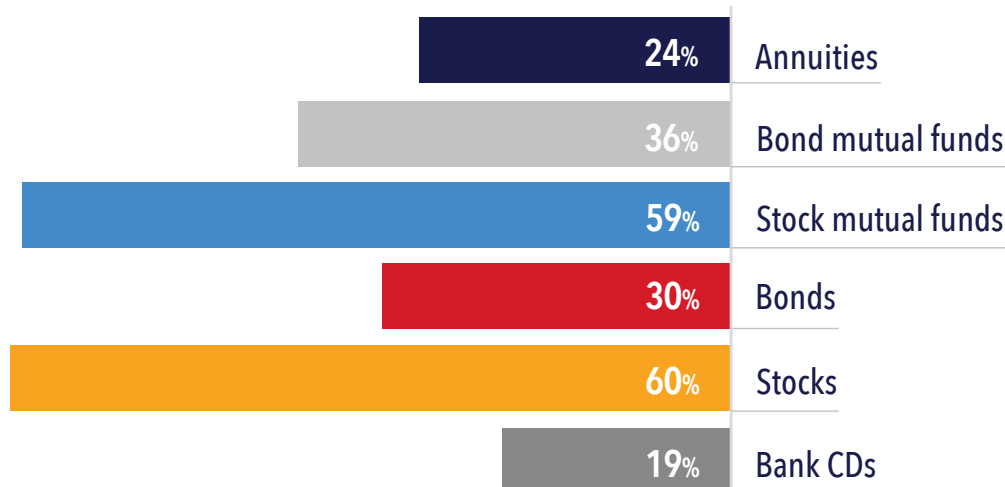
Despite investors' aversion to putting their savings at risk, the most widely held investments were stocks and stock mutual funds. More than one-half of investors who were risk averse and two-thirds who were willing to risk 5% of their portfolios, held stocks. Just 19% held bank CDs and 26% were invested in annuities — investment choices that normally are linked to principal protection.

A diversified portfolio designed to minimize volatility may include stocks and bonds, but both are risk assets, and both can fall in value. It also may include lower risk investments that offer guaranteed income streams during retirement.

Americans' current portfolios are not in concert with their fear of principal loss.

Q: WHAT TYPES OF INVESTMENTS DO YOU OWN?

Just 24% of respondents held annuities, which may offer principal or income guarantees. Additionally, only 19% owned bank CDs.



Bank CDs are insured by the Federal Deposit Insurance Corporation and offer a fixed rate of return. Annuities are typically a contract issued by an insurance company. Principal protection and income stream guarantees on annuities are backed by the financial strength and claims paying ability of the issuing company.

60%
of investors hold
stock positions –
investments that
may lose value.

MISCONCEPTION #1: BONDS ARE SAFE EVEN WHEN INTEREST RATES RISE

The bad news was that 75% of respondents didn't realize that the secondary market value for bonds declines when interest rates increase. There is an inverse relationship between interest rates and bond prices.

When rates rise, the secondary market prices for bonds fall, and vice versa. The longer a bond's maturity, the more its value may fall.⁵

The good news, since we may be in a rising interest rate environment for some time, was that relatively few respondents held bonds or bond mutual funds in their portfolios.

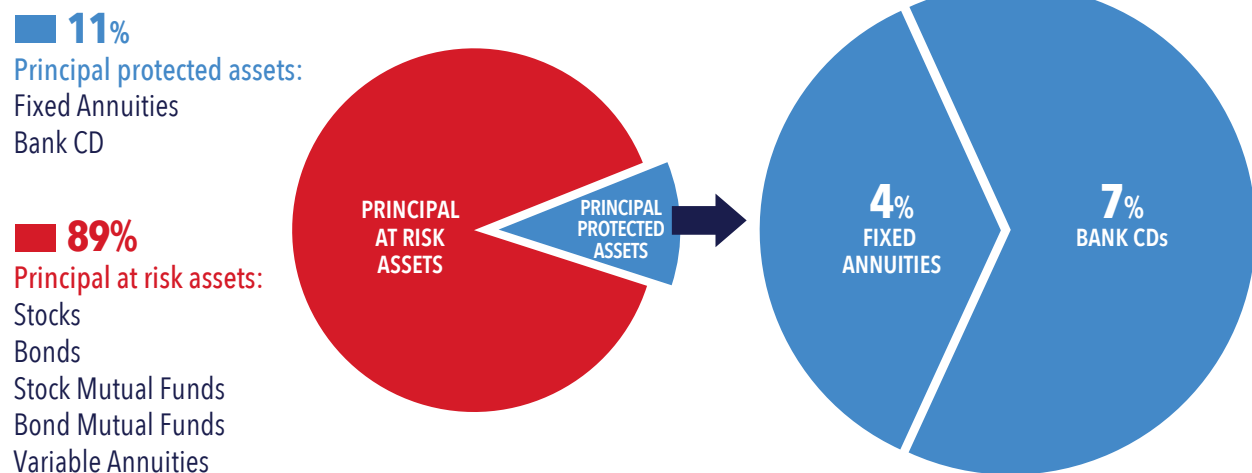
26%

of respondents are completely risk averse, yet

The Majority

of them hold investments that can suffer declines in principal value.

PRINCIPAL PROTECTED VS. PRINCIPAL AT RISK



5. FINRA Investor Alert <https://www.finra.org/investors/alerts/duration-what-interest-rate-hike-could-do-your-bond-portfolio>.

Bank CDs are insured by the Federal Deposit Insurance Corporation and offer a fixed rate of return. Principle protection and income stream guarantees on annuities are backed by the financial strength and claims paying ability of the issuing company.



MISCONCEPTION #2: INVESTORS OVERESTIMATE SAFE WITHDRAWAL RATES

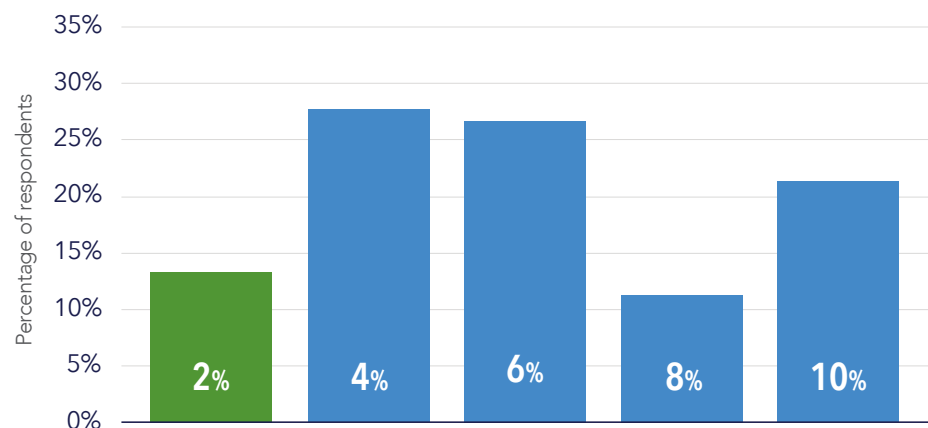
The vast majority of individual investors overestimate the amount of income their retirement savings will generate in retirement. Roughly one-third believes they'll be able to withdraw 8% or 10% of savings each year during retirement without depleting their assets!

For many years common wisdom, supported by Bill Bengen's research, suggested that 4% was a safe withdrawal rate. If investors took no more than 4% of portfolio assets (adjusted annually for inflation) each year, they could generate income that would last throughout retirement.

Rapidly evolving economic and financial circumstances have affected that assumption. In fact, new analysis showed that a 1.63% withdrawal rate had a high probability of providing retirement income for 30 years without depleting assets (5% probability of failure), if 60% of a portfolio was invested in stocks.⁶

Q: WHEN YOU RETIRE, WHAT PERCENT OF YOUR SAVINGS DO YOU EXPECT TO BE ABLE TO SPEND EACH YEAR (ASSUMING THAT YOU TAKE OUT MORE MONEY EACH YEAR FOR INFLATION) SAFELY, SO THAT YOU DO NOT OUTLIVE YOUR SAVINGS?

For many years, the American public has believed that 4% is a sustainable annual withdrawal rate from their nest egg during retirement.



6. Sustainable Withdrawal Rates for New Retirees in 2021.



Unfortunately, a 1.63% withdrawal rate might not provide enough income for many retirees. A combination of international comparative analysis, current low interest rate environments, investment management fees and increased longevity, serve as reasons why the 4% rule should be reevaluated.

Longevity Misconceptions about longevity may be another reason for the confusion about withdrawal rates. The majority of respondents said the life expectancy of a 65-year-old man was 10 to 15 years. Just over one-third knew the right answer was about 20 years. New estimates project that the average 65-year-old man in the U.S. is expected to live to be 84.3, and the average 65-year-old woman is expected to live to be 86.6.⁷



The average 65-year-old man in the U.S. is expected to live to be 84.3 years old.



The average 65-year-old woman in the U.S. is expected to live to be 86.6 years old.

However, the new analysis showed that a 1.63% withdrawal rate had a high probability of providing retirement income for 30 years without depleting assets. Investors who spend more than 2% a year during retirement today, have a relatively high probability of running out of money.⁸



7. Grant, Kelli "If you're expecting a long life, take time to adjust your financial plan" <<https://www.cnbc.com/2018/01/12/failing-to-plan-for-longevity-can-hurt-your-finances.html>>
8. Pfau, Wade. "An Efficient Frontier for Retirement Income," Social Science Research Network, September 24, 2012. <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2151259>



MISCONCEPTION #3: INVESTORS EXPECT HIGHER FUTURE RETURNS THAN ANALYSTS PREDICT

Investors' estimates for stock market returns over the next 10 years demonstrated their uncertainty about markets. A mere 10% of respondents believed that stock market returns would depreciate over the next ten years, while one-half of respondents estimated that stock market returns would average 4% to 6% over the next decade. This may prove to be overly optimistic.

Many analysts believe the Shiller PE 10, which measures stock valuations, provides insight into future market performance. A low PE 10 suggests a higher future annualized return after inflation, while a high PE 10 suggests a lower expected return. In January of 2022, the PE 10 indicated a future annual return of 4% over the next eight years.⁹

Of course, no predictor is completely accurate.

If we are really lucky, returns could average 1% a year. If we are really unlucky, they could average -11.9% a year.

Survey respondents
predict a

4-6%

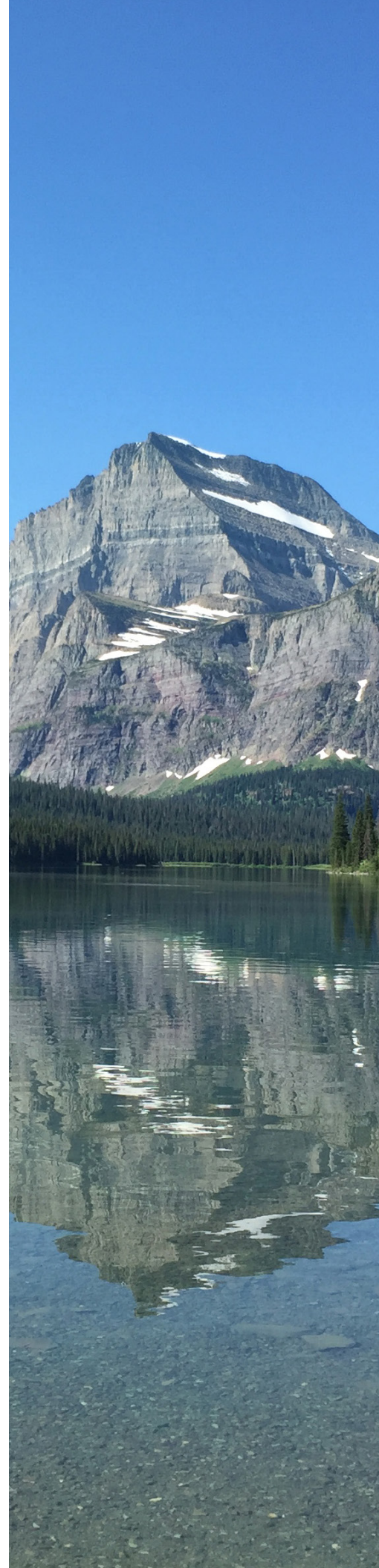
average annual
return.

The Shiller PE 10
implies a

-4%

average annual
return.

9. See source on p. 13 for an explanation of Shiller's PE 10. Data used was from January 27, 2022. Actual PE 10 level for this date was 35.7.



EXPERTS PREDICT STOCK MARKET RETURNS WILL BE QUITE A BIT LOWER

Scenario	Shiller P/E after eight yrs	Annual return from today
Really Lucky	Mean x 150%	1%
Lucky	Mean x 125%	-1.2%
Reverse to the mean	Mean x 100%	-4%
Unlucky	Mean x 75%	-7.4%
Really unlucky	Mean x 50%	-11.9%

Nobel Prize winner Robert Shiller developed a model to better understand when the U.S. equity market is in a period of long term overvaluation, and what future returns are likely to look like. Considering today's higher PE 10 value, a return to historically average PE 10 valuations would result in a -4% annualized return over the next eight years. We can analyze the potential range of returns from this model by looking at returns that would be 50% above and below the anticipated return of -4%. The key point is that during periods of higher Shiller PE 10 ratios, investors should plan on lower 1-10 year returns for stocks.

Past performance is no guarantee of future results.

Source: "Shiller P/E – A Better Measurement of Market Valuation." Shiller P/E Ratio: Where Are We with Market Valuations? January 27, 2022. <https://www.gurufocus.com/shiller-PE.php>

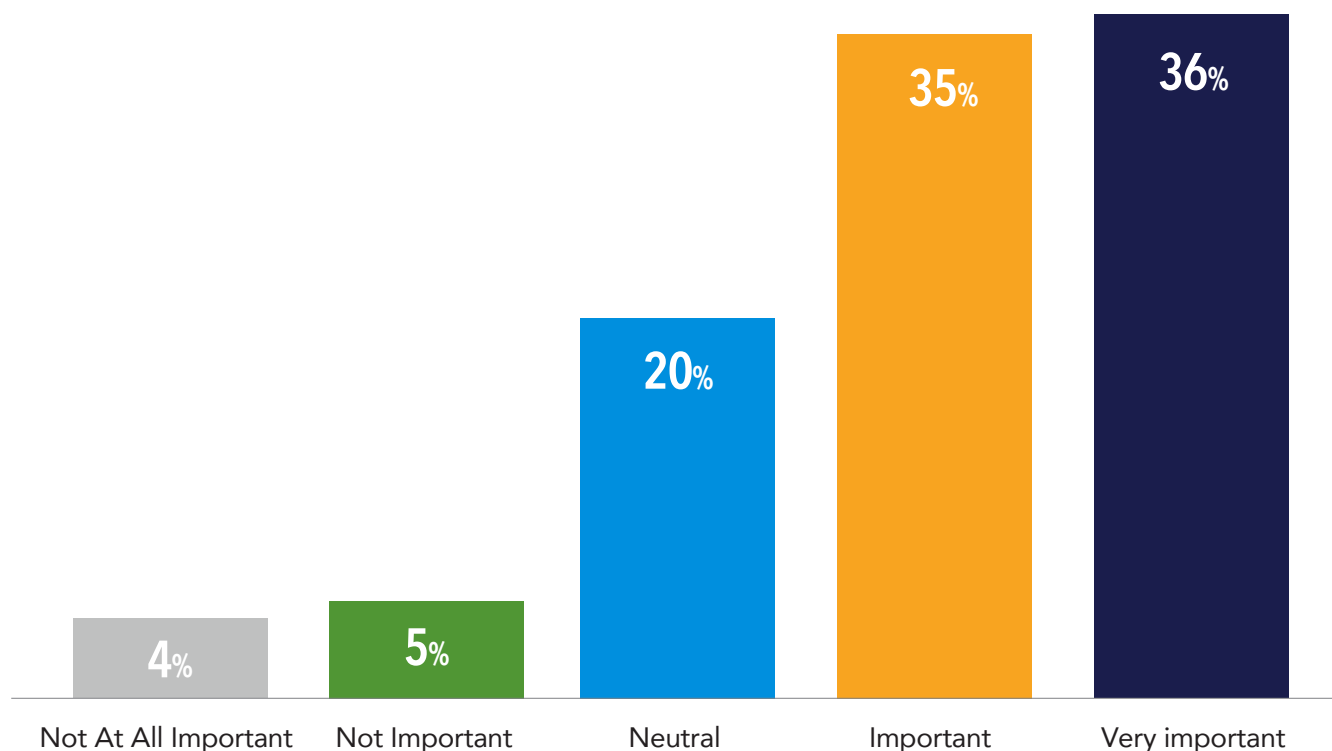


OPPORTUNITY #1: CHOOSE PORTFOLIO OPTIONS THAT PROVIDE LIFETIME INCOME

Stock markets may deliver relatively low returns for years to come,¹⁰ and bond markets are vulnerable to the potential for rising interest rates. When investors' current holdings are balanced with their ability to generate guaranteed retirement income — 54% stated they had a guaranteed income plan.

Many investors want retirement income investments that can never be outlived.

Q: HOW IMPORTANT IS IT TO YOU TO HAVE A RETIREMENT INCOME INVESTMENT WHERE YOU CAN NEVER OUTLIVE THE INCOME?



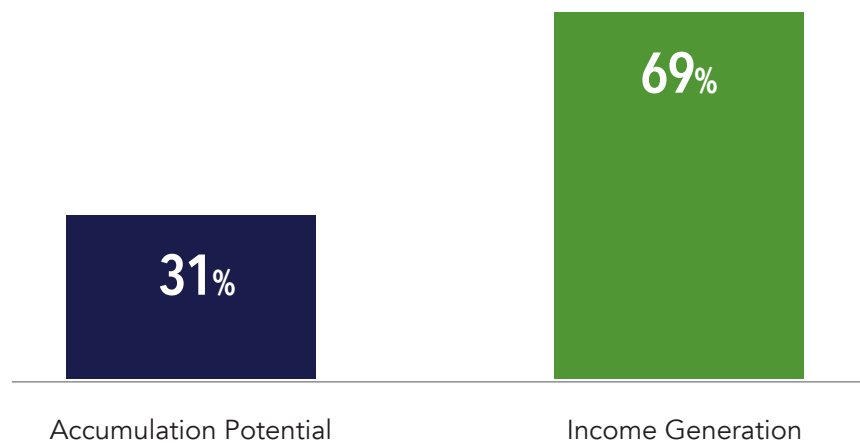
10. See pages 12-13 for an analysis of potential stock market returns based on Shiller PE 10 analysis.



The WealthVest survey clearly shows that Americans are asking for lower-risk portfolio opportunities and are interested in retirement products that protect retirement savings and offer lifetime income options.

Q: WHICH OF THESE IS A MORE IMPORTANT INVESTMENT PRIORITY IN RETIREMENT?

- INCOME GENERATION
- ACCUMULATION POTENTIAL





OPPORTUNITY #2: CHOOSE PORTFOLIO OPTIONS WITH PRINCIPAL GUARANTEES

Clients are more conservative than they once were, and three out of four are unwilling to put more than 5% of their savings at risk. Yet, many continue to hold stocks, stock mutual funds, bonds, and bond mutual funds without the principal protections that might be afforded by diverting those investments to solutions that protect from market downturns while still taking advantage of positive markets.

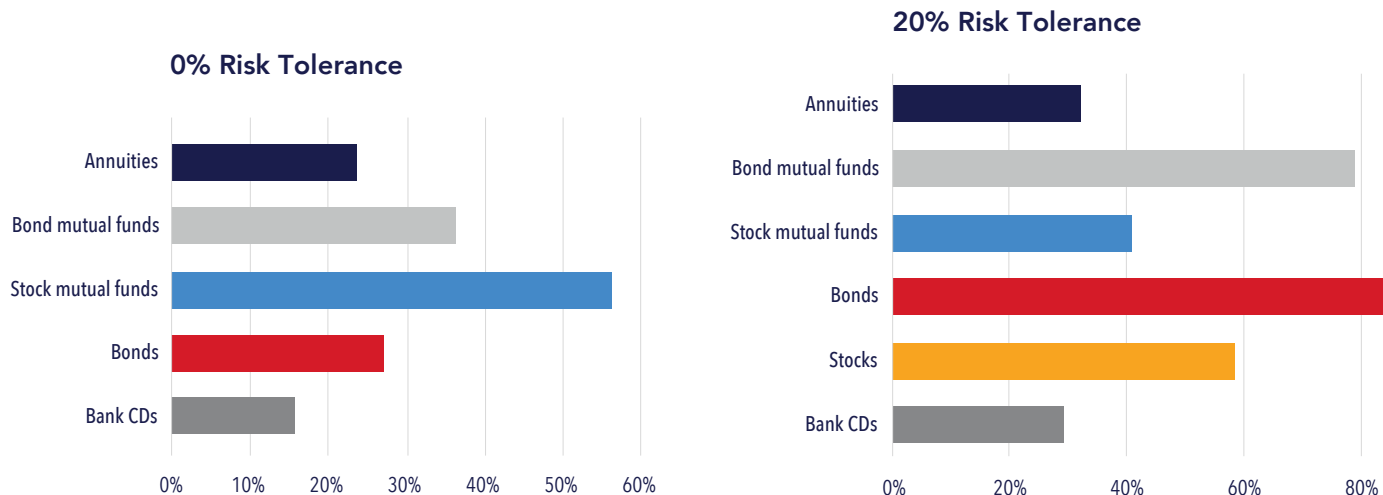
Under half of completely risk-averse participants owned a principally protected asset.

When you consider respondents' generally low-risk tolerance, their proximity to retirement — 55% were age 60 or older — and the potentially low returns anticipated from U.S. stock and bond markets during the next decade, **partially or fully principally protected products could be an attractive portfolio addition.**

Only 40%

of completely risk averse respondents owned a principally protected asset.

Q: WHAT TYPES OF INVESTMENTS DO YOU OWN?



Guarantees are backed by the financial strength and claims paying ability of the issuing company.

OPPORTUNITY #3: WORK WITH YOUR FINANCIAL PROFESSIONAL TO UNDERSTAND YOUR OPTIONS



Building a portfolio that can meet retirement income needs without taxing risk tolerance is a tall order. Today, it may be more complicated than ever before. Instead of relying on employers' pension plans to manage assets and provide steady streams of income throughout our retirements, **we must rely on our own knowledge and that of the financial professionals with whom we work.**

It's important to understand your risk tolerance, as well as the investment options that are available to help you meet your retirement goals. Different people are comfortable with different levels of risk, and the majority of Americans of retirement age are not comfortable with principal risk for their retirement assets. Find the retirement products that match the risks that are comfortable for you. If you have questions about a financial concept or investment option, contact your financial professional.

66%

of women were willing to accept only a 0-5% investment losses as compared to 61% of men.

SURVEY SHOWED THAT WOMEN WERE MORE CONSERVATIVE THAN MEN

		
BANK CDs	19%	19%
STOCKS	51%	69%
BONDS	26%	34%
STOCK MUTUAL FUNDS	56%	61%
BOND MUTUAL FUNDS	37%	36%
ANNUITIES	27%	22%

Bank CDs are insured by the Federal Deposit Insurance Corporation (FDIC) and offer a fixed rate of return. Securities and annuities are not guaranteed by the FDIC or any other government agency. Principal protection and income guarantees tied to annuities are subject to the financial strength and claims paying ability of the issuing company.



NOTES:

[illegible]





NEW RETIREMENT REALITIES

The quest for a comfortable retirement is challenging. American retirees are facing the potential of longer life expectancy, rising health care costs and disappearing pension plans. After more than a decade of economic upheaval, market volatility, and low interest rates, individual investors and their financial advisors are seeking solutions that can help make the idea of a comfortable retirement a reality.



Photo: Outside of Geraldine, Montana.



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