

selling point

The Three Phases of Retirement

The financial services industry is redefining retirement, dividing it into active, passive and final phases.

Retirement used to be considered one long, homogeneous stretch of time. We planned for the Golden Years: basically twenty to thirty years of “vacationing,” with some long-term care insurance thrown in.

Times have changed. The financial services industry has refined its view of retirement, identifying three key stages:¹

- 1 Active** The initial years of retirement, when individuals are full of energy and enthusiasm. In this first phase, many retirees travel extensively, enjoy physical sports such as tennis or golf, or continue working on a part-time basis.
- 2 Passive** The middle years of retirement, when individuals stay closer to home. Still in relatively good health, retirees in this stage may limit their travel, participate more in local events, and choose hobbies that are less physically taxing.
- 3 Final** The last years of retirement, when individuals are battling the physical and mental infirmities of old age. In this final phase, retirees may move out of their homes into assisted care facilities or nursing homes. Medical expenses, including prescription drugs, take up an ever-increasing share of their monthly income.

What are the planning implications of this new view of retirement? Some general guidelines for financial professionals are:

- Recognize that different cash flow needs accompany each stage of retirement, with higher expenses in the early and final phases and lower expenses in the middle.
- Adjust portfolios to reflect changing priorities and living patterns, with a greater emphasis on fixed-income investments as individuals age.
- Watch portfolio withdrawal rates to be sure they are sustainable over the long term (financial experts generally recommend withdrawal rates of under 4 percent per year).²
- Plan for increased longevity with financial products that deliver lifetime payouts, such as annuities.
- Encourage the purchase of long-term care and life insurance policies to help cover high medical costs and burial expenses in the final phase of retirement.

¹Two articles that reference this new perspective on retirement:

1. Michael K. Stein, CFP, “Raging Retirement,” *Journal of Financial Planning*, July 2002.
2. Ed McCarthy, CFP, “The Evolution of Retirement Planning,” *Journal of Financial Planning*, May 2002.

²Two articles that discuss withdrawal rates:

1. Jim Otar, “Live Long and Prosper,” *Financial Planning*, July 2002.
2. Gordon B. Pye, Ph.D., “Adjusting Withdrawal Rates for Taxes and Expenses,” *Journal of Financial Planning*, April 2001.