

# Retirement Income

Shape Your Own Reality



**Realities for Today's Retirees**

**47%**

fear declining health that requires long-term care

**47%**

worry about reduction or elimination of Social Security

**37%**

are concerned about outliving their savings

Source: Transamerica Center for Retirement Studies, 18th Annual Transamerica Retirement Survey, 2018.

## New Retirement Reality

Retirement today is not what it used to be. People are living longer and experiencing healthier, more active lives. While that's great news, it also poses challenges for how you will manage the retirement savings you've worked hard to accumulate.

### Planning is crucial, not impossible

No matter how you picture retirement, living in it will be very different from working toward it. You'll move from depending on a steady income to converting your savings into a secure paycheck for the rest of your life.

Developing a transition plan will help you shape your own retirement reality rather than letting circumstances shape your future. Develop your plan in four steps.



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## Picture it

One of the most important, but often overlooked, steps in preparing for retirement is to visualize what you want it to look like and to *prioritize your life goals*.

### Start by asking yourself questions about:


- **Logistics** – Where will I live? What's my retirement date?
- **Lifestyle** – Will I travel, volunteer or get a part-time job?
- **Legacy** – What will I leave to family, friends or philanthropic projects?

### Pick your priorities

Now take your vision a step further and create a list of priorities.

#### Our Retirement Goals


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 Stay in our house throughout retirement


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 Leave a bequest to the kids/grandkids

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 Visit each of our three kids at least once a year

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 Help fund the grandkids' education


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 Visit China and India

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 **His:** Volunteer at the hospital

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 **Hers:** Start a consulting business



#### Establishing a clear picture of your retirement can help you:

- More accurately assess your needs
- Create a more realistic budget
- Decide which goals to defer or eliminate if you don't have the money

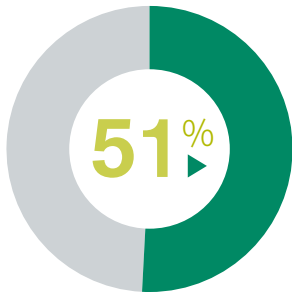
**General savings rule:  
Most advisors say you'll  
need to save between**

**70% to 80%**

of your income to maintain your current standard of living in retirement.

Source: Social Security Retirement Benefits brochure, 2019.

**Health care expenses can  
be hazardous to your wealth**



On average, Medicare only covers about 51% of a typical retiree's total health care costs\*. Dental, vision, hearing, podiatry and routine exams are not covered.

\*HealthView Services Financial, Retirement Health Care Costs, 2018.




## Pay for It

With your priorities in hand, it's time to build a realistic budget.

### 1. Estimate your annual expenses

Start with your current annual expenses and adjust each one either up or down based on your retirement needs. Also add new ones as needed.

#### Decreasing Costs



-  Work-related expenses
-  Retirement savings
-  Taxes

#### Increasing Costs



-  Health care
-  Leisure travel
-  Entertainment

Now separate expenses into essential and discretionary. Note expenses that would only be one-time costs.

#### Essential

-  Food, housing, utilities
-  Healthcare, insurance, taxes

#### Discretionary

-  Entertainment, gifts
-  Travel, dining out

### Be prepared for health care costs

In today's dollars, a healthy 65-year old retired couple can expect to pay:

 **\$363,946**

*to cover health care premiums and out of pocket expenses in retirement. Based on an inflation rate of 4.22% that number is expected to be \$537,334 in 20 years.*

- Explore supplemental health care coverage, like Medigap.
- Purchase long-term care insurance while you are healthy.
- Budget for health care premiums and costs not covered, like dental, vision and hearing.

Source: HealthView Services Financial, 2018.

## 2. Estimate your annual income

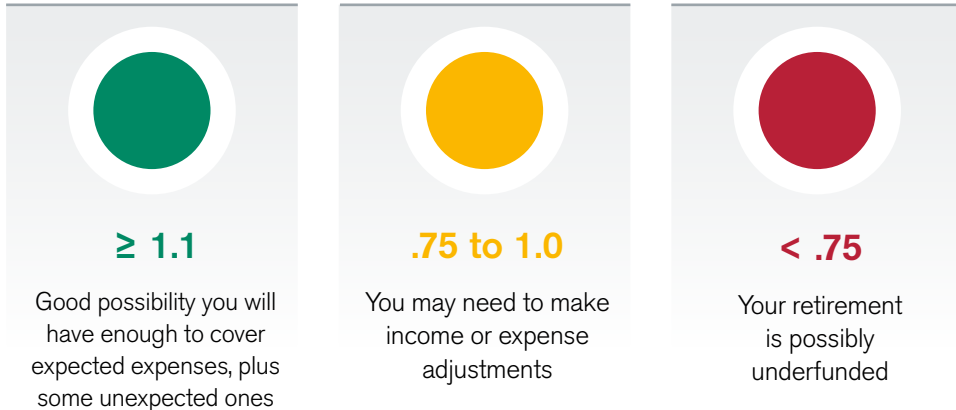
Be sure to include all potential sources such as:

- **Lifetime income** - Social security benefits, pensions and annuities
- **Savings/investments** - 401(k)s, IRAs, mutual funds, CDs, stocks/bonds, and returns from these investments
- **Earnings** - Full- or part-time job
- **Other assets** - Real estate and equity in a home or business

## 3. Check reality—are you on track to retire?

With your estimated annual income and expenses in hand, use this formula to get a preliminary, ballpark assessment of your retirement fitness.\*

$$\frac{\text{Expected Annual Income}}{\text{Expected Annual Expenses}} = \text{Retirement Funding Fitness Ratio}$$



Source: American Century Investments, 2019.

*\*This is intended as directional only and not to represent a true retirement readiness assessment. A full assessment requires a complete analysis of your financial situation.*

### If you didn't get a green light, there are ways to improve your readiness:

- Delay retirement and save more
- Reduce future expenses
- Defer Social Security payments to maximize your benefits
- Evaluate how much risk you can take with your investments. More aggressive investments may help you grow your savings, but also come with more risk.

## Total Income Example

### Savings/Investments

401(k)	\$450,000
IRA	\$60,000
Mutual Funds	\$103,000
Stocks	\$23,000
Bonds	\$46,000
<b>Total</b>	<b>\$682,000</b>

### Annual Income From Investments

\$682,000 x 4%	<b>\$27,280</b>
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### Annual Income

Social Security	<b>\$35,000</b>
Pension	<b>\$10,000</b>

### Annual Earnings

Part-time job	<b>\$12,000</b>
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**Total Annual Income**    **\$84,280**

## Health care expenses may require a budget bandage

# 53%

of pre-retirees express anxiety about their upcoming retirement. Worries about paying for healthcare contribute to this sentiment.

Taking steps to improve your health and planning ahead to cover these costs are vital considerations.

Source: Healthview Services 2018. Retirement Healthcare Costs Data Report, 2018

The biggest inflation risk for retirees is health care. Historically, this inflation rate has been much higher than overall inflation and it can become acute if a long-term illness occurs.

Source: Annual rate of inflation for healthcare versus overall from 2000 to 2019. Bureau of Labor Statistics, 2019.

## Plan it

Once you have a target budget, it's important to know the key risks you will likely face and how to incorporate protection strategies in your plan.

### 1. Outliving your money

The biggest risk that retirees can face is running out of money. This is known as longevity risk.

#### Plan to Live Longer Than You Think

Probability of Today's 65-Year-Old Living to Various Ages

65 Year-Old Male		65 Year-Old Female	
Age	Probability	Age	Probability
80	71%	80	79%
85	54%	85	65%
90	34%	90	46%
95	16%	95	25%

Source: Social Security 2010 Mortality Table, with future mortality improvement projected using the Society of Actuaries MP-2015 scale.

### Help make your money last

You can manage longevity risk through careful planning.

- Choose a realistic time frame for how long your retirement money needs to last. If you retire at age 65, plan for 30 to 35 years.
- Maintain an adequate amount of stock investments. This can potentially help your savings continue to grow; however, it does come with additional risk.
- Pick a sustainable withdrawal rate, between 3-5%.

### 2. Losing purchasing power

The dollar losing value over time, known as inflation risk, can have a devastating impact on your retirement security. This can be true even when inflation is relatively low.

#### Help maintain your buying power

- Add inflation-hedging investments to your portfolio.
- Maintain enough stock investments so your savings potentially can keep growing.
- Maximize Social Security payments, which automatically adjust for inflation.

*As with all investments, there are risks of fluctuating prices, uncertainty of dividends, rates of return and yields. Current and future holdings are subject to market risk and will fluctuate in value.*

### 3. Declining market

Market declines, especially early in retirement, can undermine your portfolio.

#### Diminish volatility impact

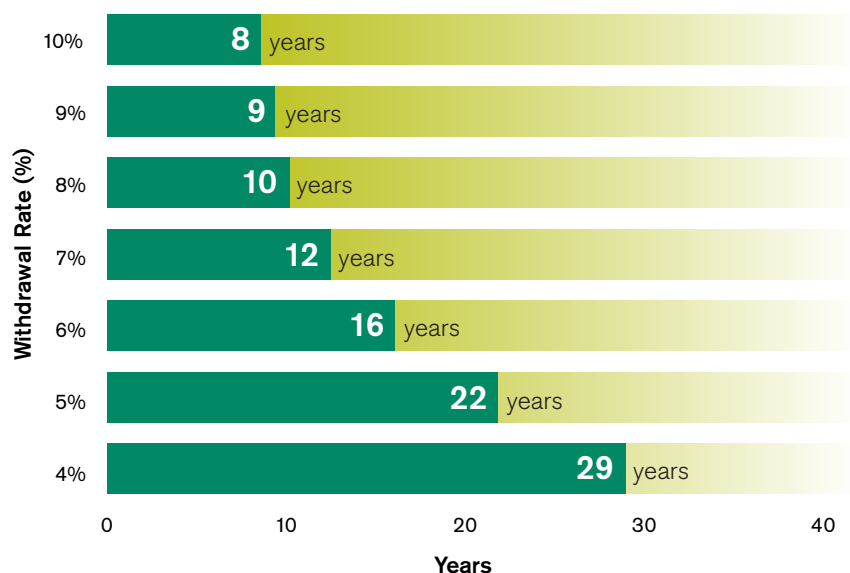
- Balance market highs and lows by having a mix of investment types. You want investments that react differently when market conditions change.
- Align how much of each kind of investment, known as asset allocation, with how much risk you're willing to take. It may help you be less likely to panic in a downturn.
- Maintain lower-risk investments to cover your first three to five years of retirement.

### 4. Overspending

Spending in retirement refers to the withdrawal rate you choose from your savings. Taking too much can deplete your savings too fast.

#### Lower Withdrawal Rates Could Make Your Money Last Longer

(Hypothetical Examples)



*These hypothetical situations contain assumptions that are intended for illustrative purposes only and are not representative of the performance of any security. There is no assurance similar results can be achieved, and this information should not be relied upon as a specific recommendation to buy or sell securities. Assumes a portfolio with 50% equity, 45% bond, 5% cash allocation over 30 years at a 90% confidence level, with the following average monthly capital market returns: Stocks: 7.90%, 18.90% standard deviation; Bonds: 5.00%, 4.95% standard deviation; Cash: 2.25%, 1.00% standard deviation. The correlation between Stock and Bond returns is 0.2. Inflation rate is assumed to be 2% annually and is included in each of the withdrawal rates depicted above.*

*Standard deviation defines how widely returns vary from the average over a period of time.*

Source: American Century Investments, 2019.

#### Market volatility is a significant risk for retirees:

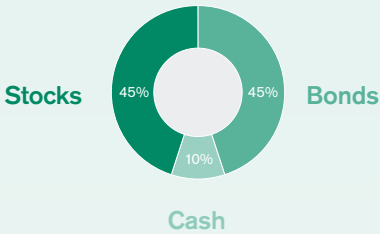

- Generally your savings will be the largest at retirement, before any withdrawals have begun. A market decline early on could have a greater dollar impact.
- Withdrawals intensify the impact of market declines because they represent funds that can no longer grow when the market does rebound.

#### Tips to minimize its effects:

- Temporarily reduce your withdrawal rate so more of your investments have a chance to rebound.
- Avoid selling stocks. Take your withdrawals from cash, then bonds, and lastly stocks, and only if you have to.

## Select the right income strategy

There are numerous philosophies in the marketplace for building a retirement portfolio for income. Three are listed here as thought-starters. Ultimately, your strategy depends on your individual needs.

	Total Return	Buckets/Time Segmentation
Income Strategy	 <p>Stocks 45% Bonds 45% Cash 10%</p> <p>Create a broadly diversified portfolio that aligns with your risk tolerance.</p>	 <p>1-5 Yrs. 6-15 Yrs. 16-30 Yrs.</p> <p>Divide your portfolio into two to six buckets, each with its own allocation/ income goal.</p>
Portfolio Goals	<ul style="list-style-type: none"> <li>• Seeks risk-adjusted, total return that you can convert into annual income.</li> <li>• Resembles a pre-retirement portfolio.</li> </ul>	<ul style="list-style-type: none"> <li>• Each bucket has its own degree of liquidity and risk; shorter term buckets are less risky.</li> <li>• Draw monthly income from short-term buckets.</li> <li>• Long-term buckets replenish short-term ones.</li> </ul>
Benefits	<ul style="list-style-type: none"> <li>• Easy to implement and monitor.</li> <li>• May help avoid excessive yield focus.</li> <li>• Time-tested and well researched.</li> <li>• Flexible and puts you in control.</li> </ul>	<ul style="list-style-type: none"> <li>• Enables you to match income timing with risk.</li> <li>• Can help risk-adverse clients maintain stock exposure during down markets.</li> <li>• Easy to measure results and make adjustments.</li> </ul>
Cautions	<ul style="list-style-type: none"> <li>• Unless broadly diversified, your portfolio could be more susceptible to market swings.</li> <li>• Success may depend on factors you can't control—like a market swing right before, or early in, your retirement.</li> </ul>	<ul style="list-style-type: none"> <li>• Can be complex to manage multiple accounts.</li> <li>• Moving money across buckets may incur taxes.</li> </ul>
Best for Retirees Who	<ul style="list-style-type: none"> <li>• Are well funded.</li> <li>• Can tolerate more risk.</li> <li>• Want to control their assets.</li> </ul>	<ul style="list-style-type: none"> <li>• Are anxious about risk.</li> <li>• Have precise short- and long-term goals.</li> <li>• Have more constrained retirement funding.</li> </ul>

*Diversification cannot protect against loss in a down market.*



## Income Floor



Essential Expenses

Discretionary Expenses

Part of your portfolio is dedicated to essential expenses (your income floor), while the rest aims to grow your savings.

- Your income floor contains very conservative, fixed-income investments like bonds, and/or an annuity.
- Discretionary savings are managed like a diversified total return portfolio.
- Potentially improves income stability.
- Helps reduce longevity and market risks.
- Allows more aggressive investments for discretionary savings.
- Managing the income floor can be complex.
- High fixed-income allocations or insurance products can limit growth.
- Current low interest rates make annuities expensive.
- Are highly concerned about risk.
- Have more constrained funding.



### A diversified portfolio is essential in retirement

Diversification means spreading your money across different types of investments which are expected to perform a certain way under particular economic conditions. A few stocks and a few bonds won't cut it in retirement.

## Position it

Your retirement portfolio will be just as important as your pre-retirement portfolio. Your goal is to build a portfolio that gives you the best chance of success while minimizing risk.

The investments you choose are critical, but they are not a cure-all. They cannot fix insufficient savings or chronic overspending. Below are some key principles to consider.

Our research indicates that

**35%** to **55%**

may be an appropriate amount of equities for a 30-plus year retirement span.\*

Since 2008, people generally are underexposed to equities. This can exacerbate longevity and inflation risks and actually hurt, not help, in retirement.

\*Assumes a 4-5% withdrawal rate over 30 years of retirement. Source: American Century Investments, 2019.

### Avoid the yield trap

With interest rates at historic lows, it may be tempting to invest in stocks and bonds with the highest yields in their categories. The problem is that often those yields are unsustainable and come at the expense of significant capital risk.

### Match spending to risk

Align investment risk to cover the types of expenses you have.

Use low-risk/low-volatility investments for essential expenses, especially in the first three to five years.

Use stocks for discretionary expenses, to address longevity and inflation risks, and fund legacy wishes.

#### Low-Risk Investments

- Short-term government
- Intermediate-term government
- Corporate bonds

#### Stock Investments

- Growth
- Value
- International

### Choose the right asset allocation

Having the appropriate mix of stocks, bonds and cash may improve your odds of retirement success.

#### You may want more stock exposure when:

- Your retirement time frame is longer
- Inflation is higher
- Your withdrawal rate is higher
- You have a higher risk tolerance

#### You can have lower stock exposure when:

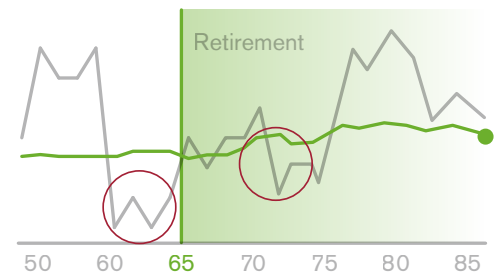
- Market risk is high
- Your retirement is well funded and conservative investments will sustain your retirement income

### Enhance diversification

Spreading your money across different asset types has historically been successful for managing volatility.

Diversification may also help increase the probability that your money will last.

#### Diversification may help lower risk if volatility occurs right before or after you retire



*For illustrative purposes only. Does not represent an actual portfolio or returns.*

*Diversification cannot protect against loss in a down market.*

*This information is for educational purposes only and is not intended as investment advice.*

## Portfolio Review – Don't leave your retirement to chance.

Preparing your portfolio for retirement takes careful planning.

### Revisit

While a long-term view of your investments for retirement is recommended, once your plan is in place, it a good idea to review it from time to time.

In addition to market volatility, your time horizons change and your tolerance for risk too. Changes in the market and life events are unavoidable. Our investment professionals recommend revisiting at least annually.

We believe having a plan gives you a better chance of success and an opportunity to shape your own retirement reality.

### Start planning now

Contact us or your financial professional to get started.

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## American Century Investments®

### Focused on your retirement

Put our commitment to quality and consistency to work for your retirement portfolio. The very nature of our investment management processes make us uniquely qualified to help you build a retirement portfolio to potentially last a lifetime.



### Retirement Income Checklist

- ✓ Visualize your retirement and goals
- ✓ Estimate expenses, health care costs and income
- ✓ Make a plan - take into account:
  - living longer than you think
  - losing purchasing power
  - market volatility
  - how much you should withdraw
- ✓ Build a portfolio - determine how much risk you can handle and diversification strategies
- ✓ Revisit - at least annually, make sure your time horizon and risk tolerance haven't changed



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### Managing Money, Making An Impact

American Century Investments® is a leading asset manager focused on delivering investment results and building long-term client relationships while supporting research that can improve human health and save lives. It's how we and our clients together **Prosper With Purpose®**.

Every day people are increasingly focused on investing to make the world a better place for themselves, their families, their organizations and the world at large. It is possible to live a more meaningful and impactful life and give back something that's more valuable than money.

When you invest with us, you can also invest in the future of others and have the potential to impact the lives of millions. That's possible because of the distinct relationship with the Stowers Institute for Medical Research, which owns more than 40% of American Century. Our dividend payments provide ongoing financial support for the Institute's work of uncovering the causes, treatments and prevention of life-threatening diseases, like cancer.

Together we can become a powerful force for good.

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