

The Financial Nightmares Facing Boomers

The Not-So-Golden Years

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This month, the first baby boomers officially reached retirement age, and they're in a gloomy mood. A Pew Research Center survey last month found that 80 percent of the nation's 79 million boomers are dissatisfied with the way things are going today—more than members of any other age group. This may reflect that 60 percent of Americans aged 50 to 61 think they might need to delay retirement because of the recession, according to a May 2010 Pew survey. Fully 57 percent of boomers said their household finances have deteriorated in the past few years, more than any other generation surveyed.

Sinking home equity, rising health-care costs, and low returns on most investments have left boomers near retirement confronting a pile of financial worries instead of happy visions of golf, grandchildren, and travel. Here are some potential financial disasters facing this generation—and tips on how to avoid them.

Inflation

The U.S. cost of living rose just 0.1 percent in November 2010, according to a Dec. 15 Labor Dept. report, but inflation could be a serious concern in the future. Recent efforts by the U.S. Federal Reserve to stimulate the economy have drawn criticism from GOP leaders. Four of them, including new Speaker of the House John Boehner (R-Ohio), sent a letter to the Fed on Nov. 17 warning that so-called quantitative easing could lead to "hard-to-control, long-term inflation." An annual inflation rate of 7 percent running for a decade is enough to cut a dollar's purchasing power in half.

How to Avoid: The usual recommended hedges against inflation are investments in commodities, real estate, and Treasury Inflation Protected Securities, or TIPS. Princeton University economics Professor Burton G. Malkiel advises buying securities in countries rich in natural resources, such as Brazil and Australia.

Parent-Child Sandwich

Boomers can feel quite a financial squeeze when their aging parents and their children need help. With the younger generation disproportionately hurt by the recession, many twentysomethings have moved back in with parents. According to 2010 Census Bureau data, 5.5 million Americans aged 25 to 34 live with their parents, up 38 percent from 2000. In November, the unemployment rate for people aged 20 to 24 was 14.8 percent.

Meanwhile many elderly Americans have had to move in with their children. In a 2009 survey by the National Alliance for Caregiving, 21 percent of caregivers for older adults said the economy had forced them to live together in the previous 12 months. An earlier study by the group found, on average, that families caring for older adults spend 10 percent of their income to do so.

How to Avoid: Ask children to pay rent—at least enough to cover extra expenses. When caring for aging relatives, don't try to do it all yourself. Experts advise finding ways to spread responsibilities among other friends and family members.

Scams

A fifth of Americans over age 65 have been victims of a financial scam, according to the nonprofit Investor Protection Trust. The defrauding of seniors costs more than \$2.6 billion per year, according to MetLife. The largest investment fraud in history was uncovered when Bernard Madoff's money management business turned out to be a Ponzi scheme, revealing \$65 billion in nonexistent investments. Investors lost about \$20 billion in principal.

How to Avoid: Look for common safeguards such as independent audits and custodial accounts held independently of managers. Spread your money around so you're not relying on just one manager for your retirement. Think twice before buying complex financial products such as annuities or reverse mortgages—and consult an impartial adviser. In July, *Bloomberg Businessweek* reported that improper selling of reverse mortgages plays a big role in many scams.

Gold Bubble Bursts

The price of gold is up more than 170 percent since the beginning of 2006 and hit a record of \$1,431.25 an ounce on Dec. 7. Billionaire George Soros has predicted that the gold rush can't last, calling the precious metal "the ultimate asset bubble" at the World Economic Forum last January. According to money manager BlackRock, individual investors may hold as much as half the gold in exchange traded funds. "Your little guy is going to get hit by the doorknob on the way out," Boston University master lecturer Mark Williams told Bloomberg News last month.

How to Avoid: Many investment professionals advise limiting gold and other commodity investments to a small portion of your portfolio—around 5 percent or less.

Not Saving Enough

According to an 2010 Employee Benefit Research Institute survey, 13 percent of workers aged 55 or older are "very confident" that they have enough money to live comfortably through retirement, down from 27 percent in 2000. Only 53 percent of older workers have actually tried to calculate how much money they will need in retirement, the survey said.

How to Avoid: Those who have fallen behind on retirement savings don't have a lot of options: They can save more, work longer, or cut back on their spending. The EBRI survey found that 42 percent of older workers don't plan to retire until age 66 or later, up from 20 percent in a 2000 survey.

Retiring Too Luxuriously

For decades, a typical rule of thumb for retirees was that they could spend their savings at the rate of about 4 percent per year without running out of money. The poor performance of markets in the past decade, however, has challenged that rule. New research suggests that boomers might better spend just 2 percent of their nest egg each year in retirement.

How to Avoid: To be safe, retirees should save more and spend less. Fortunately, spending often slows as we age. (A world tour looks less enticing after age 70.) You can also keep an eye on how the market is performing, for instance, and adjust yearly withdrawals accordingly.

Too Much Company Stock

According to the Profit Sharing/401k Council of America, 18.1 percent of retirement plan assets last year were invested in the stock of participants' employers. Such concentrated investment in one company can be dangerous, financial planners warn. If a company runs into trouble, employees can lose both their jobs and a large portion of savings.

How to Avoid: Start cutting back company stock holdings as soon as feasible—perhaps by selling some stock each quarter— and then put together a more diverse basket of investments.

Another Stock Market Crash

It's nice to think that the financial crisis from 2007 to 2009 was the last we'll see in a lifetime. Remember, though, that there were significant stock market crashes in 1929 and 1987, and weak, bearish markets in the early 2000s and through most of the 1970s.

How to Avoid: Trying to time the market isn't the answer. Most investment advisors suggest simply diversifying your portfolio, putting more into bonds and less into stocks as you age. U.S. Treasuries increased in value during the crisis and other bonds held onto their value better than stocks. (Still, if inflation roars back, it will hit long-term bonds particularly hard.)

Failure of a Family Business

Family members who work together can end up with all or most of their net worth in the business. That means their nest eggs can be highly illiquid—a dangerous position if the business falters. More than 85,000 commercial businesses filed for bankruptcy protection in 2010, according to data provider Epiq

Systems, up 182 percent from 2006.

How to Avoid: While your business is doing well, try to generate cash that can be invested in a diverse portfolio. Also, do everything possible not to touch your retirement savings when starting up or expanding a small business. Experts advise exploring other options such as loans and private investors.

Living Too Long

According to a 2005 survey by the Society of Actuaries, 42 percent of Americans approaching retirement underestimate how long they will live by five years or more. A longer life means more years of living expenses that must be funded in retirement, as well as a greater chance of high medical costs.

How to Avoid: It can be expensive to buy annuities that provide a lifetime income stream, but they can pay off if you live long enough. When planning for retirement, be aware that a 65-year-old woman has a 50 percent chance of living to age 86 and a 20 percent chance of living to 94.

Rising Health Costs

Medicare covers much of a retiree's health-care expenses, but not all. Rising costs could leave retirees on the hook for some big bills from doctors, hospitals, and nursing homes. According to a March 2010 report from the Boston College Center for Retirement Research, a typical couple aged 65 will spend \$197,000 to \$260,000 on health care not covered by insurance during their retirement, with a 5 percent chance that costs could exceed \$570,000. The report notes that less than 15 percent of households had that much in total assets in 2007.

How to Avoid: Workers need to save, not just to cover retirement living expenses, but also to fund health care. Long-term care insurance, while difficult to evaluate and potentially costly up-front, can help cover the unexpected costs of long illnesses.

Underwater Mortgages

The decline in home prices has pained baby boomers; many find themselves owing more on their mortgages than their houses are worth. These so-called underwater mortgages make it difficult to sell homes and can leave homeowners with crippling mortgage payments. According to CoreLogic, about 10.8 million U.S. homes were underwater as of Sept. 30. Nouriel Roubini, founder of Roubini Global Economics, said on Nov. 2: "If house prices are going to fall another 5 to 10 percent, another 8 million households are going to be in negative equity."

How to Avoid: There is no way easy way to make solvent a mortgage that's already under water. You can try to rent out your home or renegotiate your mortgage. Or you can wait in hopes that home prices recover over the next several years.

Washington Changes the Rules

In 1970 the total national public debt was about \$283 billion, or 28 percent of gross domestic product. Now the federal debt stands at about \$9 trillion, or 62 percent of GDP. Lawmakers and bipartisan commissions have proposed a variety of fixes for the country's debt problem: limiting tax deductions and raising tax rates, cutting Medicare, taxing Social Security benefits for upper-income groups, and raising the ages at which people become eligible for benefits.

How to Avoid: Luckily for older baby boomers, many of the reforms proposed so far wouldn't change much for those close to retirement. For example, the National Commission on Fiscal Responsibility and Reform's proposed plan wouldn't raise the Social Security retirement age to 69 until 2075. Still, some provisions —especially changes in tax laws—might affect younger boomers, so they should carefully watch developments in Washington.