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Is Getting to the Top of the Mountain Good Enough?

For many, retirement planning involves accumulating an amount of retirement savings sufficient to allow you to retire in the lifestyle you are used to living. This traditional planning focuses on the accumulation of assets. It defines the goal of retirement planning as achieving a certain dollar amount believed to be enough to retire on. There are even some financial firms that advertise that they will help you calculate "your number."

We believe that planning for retirement needs to be redefined. We do not believe it is only about accumulating assets, but rather about planning for how those assets will provide a cash flow to you throughout your retirement. We believe there needs to be a shift in thinking in order to properly prepare for retirement.

For example, if we ask, "what is the goal of climbing a mountain," many of you would likely reply "to get to the top." We would say the goal of climbing a mountain is not just to get to the top, but rather to get back down safely. This is the difference between planning for accumulation and planning for distributions. Planning for accumulation may get you to the "top of the mountain." But if your goal is to get back down safely, as we believe it should be, then your planning may require a shift in thinking to plan for distributions. This is especially important when you consider that 80% of mountain climbing accidents happen on the way down.

When planning only for accumulation, it is simple to run computer modeling utilizing an assumed rate of return and the number of years to retirement. Stock market volatility may not be terribly relevant if you assume a reasonable "average" rate of return over the period to retirement. However, when planning for distributions, it is the sequence of returns that is far more relevant than the average expected return. Volatility can have a much greater impact when you are taking distributions and can add a complexity to the planning. This is one of the reasons why distribution planning is different than accumulation planning.

Another risk that can add complexity to the planning process is inflation risk. While it may be relatively simple to plan for a steady and constant income over your retirement, it is much more complex, and more important in our opinion, to plan for a steady and constant lifestyle over your retirement. This may require an increasing income to keep pace with inflation.

Longevity risk is another risk that must be addressed in a proper financial plan and makes distribution planning different from accumulation planning. While typical computer modeling may help create a strategy until your life expectancy, it may not address what happens if you live longer than your life expectancy. It is important to remember that average life expectancy is just that – the average. It does not necessarily reflect how long YOU will live. We believe it is important to create a strategy that provides you an opportunity to maintain your lifestyle no matter how long you live.

If your true goal is not just getting to the top of the mountain, but rather is getting back down the other side safely, then we believe it may be time to redefine what retirement planning is all about and create a strategy based on your real goals.