Why Retirement Planning Fails

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Retirement Rehab

We've all heard the traditional wisdom out there about retirement planning. The 4% rule. Basically, it means you need to have enough money to be able to withdraw 4% of the balance every year during retirement.

This traditional wisdom is off for a lot of reasons — for one, it assumes you're going to run out of money and pass away at exactly the same time.

But there are other reasons why it's not relevant today.

Nest Eggs Aren't What They Used to Be

The 4% rule was first conceived in the 1990's based on interest rates. Back then, interest rates were so high that you could invest in a CD and grow a nest egg even after withdrawing on 4%. When you die didn't even matter.

It was easy to dip into your principal retirement fund when needed, risking the possibility of leaving less for your surviving spouse or heirs, because people had so much confidence they'd make it back.

Many smart financial advisors saw the writing on the wall — healthcare costs were rising above inflation and life expectancy was growing. But nobody listened to their objections thanks to high interest rates.

But conversations like that don't happen today. It's just not a reality. CD and other rates are so low that even a decent sized nest egg won't generate much income.

We’re Destroying the Math

Americans today need to accumulate a massive nest egg if they ever want to fund a decent retirement living with a 4% withdrawal rate.

According to Transamerica, American workers age 50 and older have a median $135,000 only in total household retirement savings. That’s a lot less than previous generations managed to save, despite the fact that we need much more in order to make up for poor interest rates.

You can thank the last financial crisis and a culture of consumerism for that. We have a spending problem, which doesn’t go away later in life. Despite all that retirement planning, many end up spending much more than 4% during the first years of retirement anyway.

You’ll Probably Live a Long Time

The 4% rule was originally based on research of historical interest rates. But new research (circa 2013) is telling a different story. Retirees are 50% more likely to run out of money using the 4% rule today.

And that data is just based on market changes. It doesn’t even take into consideration the fact that you’re probably going to live a very, very long time.

Considered by many to be the greatest achievement of the 20th century, life expectancy has skyrocketed. Most babies born in 1900 didn’t live past age 50; today in Japan, life expectancy at birth is more than 83 years. As more diseases are cured and anti-aging treatments advance, it’s only bound to get higher during your lifetime (in the US and elsewhere).

So how can you plan for the 4% rule if you could live till 70 or till 100? That’s a huge gap. The 4% Rule is a bet against increasing life expectancy. You also have an implicit risk of rising healthcare costs.

The Bottom Line

Whatever wisdom you’ve heard, traditional retirement planning rules of thumb developed 20 years ago don’t make any sense today. The 4% rule used to be an easy solution, but the rules of the game have changed.

Today’s investing landscape tells us that reliable cash flow is at a premium. Even a reasonably sized nest egg won’t cut it. To get the Nest Egg which the 4% Rule draws from is an archaic assumption of steady employment in an era of massive technological change and job instability. Many of us will never even be able to test the 4% rule.

Luckily, you can fix the problem if you just ignore traditional advice and start thinking outside the box. If you’re a seasoned corporate executive with a less-than-stellar nest egg, you can still make retirement planning a reality.

The paradigm has changed from a pile of cash to durable and reliable cash flow. Smart real estate investment and establishing secondary businesses are just two of many options out there. Join our community to learn more and succeed with retirement planning.