



RETIREMENT INCOME

—DEFINING THE ISSUES

Many investors have spent years accumulating assets for retirement through 401(k)s, IRAs and traditional investment accounts. In the retirement income phase of life, an investor typically spends savings and receives retirement payouts. The retirement income phase may include risks that many investors have not considered. Some of these risks are outlined below:

Changes in Pension Coverage: In past generations, a pension was the most common source of a sound retirement plan. Today, pension plans are almost always a lesser piece of the retirement income picture, as other programs have taken the place of defined benefit and other pension plans. These alternatives shift the risks of meeting plan obligations from employer to employee. The obligation to make assets last throughout retirement now rests almost entirely on the shoulders of the investor and, potentially, at the mercy of the markets.

Longevity and Health: One reason for the shift in risk management responsibilities has been the fact that employees are living longer. A 65-year-old man has a 25% chance of living to age 89 and a 10% chance of living to age 94. A 65-year-old woman has a 25% chance of living to age 92 and a 10% chance of living to age 97 (Source: Employee Benefits Research Institute, choosetosave.org). That means an investor needs to plan for a 25 to 30-year retirement. Pensions and Social Security may be considered sources of income that are guaranteed for life, effectively eliminating longevity risk. Yet 401(k) and IRA assets are often invested in securities with fluctuating values and income streams. Determining the amount of income an investor can safely take from investments without the risk of running out of assets isn't an easy task.

Rising Health Care Costs: Health care costs are one of the most expensive items in most retirees' budgets. Median annual out-of-pocket costs are expected to grow from about \$2,600 in 2010 to \$6,200 in 2040, as expressed in constant 2008 dollars. About 10% of older adults with the most pressing medical needs will spend more than \$14,000 per year on health care in 2040, and that's with Medicare coverage (Source: Will Health Care Costs Bankrupt Aging Boomers, 2010 Urban Institute).

Even with the recently passed health care reform legislation, estimating how much income an investor may need for future health care expenses can prove a real challenge for people entering retirement. These costs, by their nature, will continue to escalate over time.

Note: Janney Montgomery Scott has produced a white paper about the recent health care reform legislation. If you are interested, please contact your Financial Consultant to request a copy.

Market and Economic Risks: Volatility has shaken investors' confidence in the market and the overall economy. For many pre-retirees, a viable solution may be planning to delay their retirement. A recent study (2010 Retirement Confidence Survey), conducted by the Employee Benefits Research Institute and Mathew Greenwald and Associates, found that one-quarter of workers (24%) report that they have postponed their planned retirement

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age in the past year. Among the reasons cited for these decisions were the poor economy (29% of those postponing retirement), a change in their employment situation (22%), inadequate finances (16%) and the need to make up for losses in the stock market (12%).

WHAT CAN BE DONE TO HELP ADDRESS THESE RISKS?

Time the transition into retirement. Delaying retirement by just a few years can significantly extend the lifespan of an investor's assets. Other alternatives to managing a transition to retirement may include working part-time or consulting to lessen the burden on an investor's retirement portfolio.

Look at health and family history. While it is difficult to determine one's exact life expectancy, many individuals may be able to gauge the probability of being on the longer end of their life expectancy by looking at their medical history and the longevity of close family members. Having realistic expectations about how long assets may need to last will help investors make informed decisions about how and when to retire. Another part of the retirement planning process is planning for illness or premature death which can result in unexpected expenses and impact a family's ability to meet its long-term needs. Investors may want to consider adding a trust, or a long-term care or life insurance policy, to help provide for their spouse and/or heirs after they are gone.

Consider spending behavior in retirement.

Standard planning practice estimates that post-retirement income needs are generally between 80–105% of pre-retirement income; yet pre-retirees often underestimate this need. The impact of underestimating long-term needs may not be felt for many years to come, with the brunt of the impact felt only in a retiree's later years. Travel, indulging grandchildren and maintaining lifestyles can be more expensive than most think. Adjusting spending habits based on market conditions by spending more during good markets and less during poor markets can help extend the lifespan of savings—as can lowering annual spending levels in retirement.

Ensure professional guidance of retirement portfolios.

Taking time to concentrate on retirement income is an important step in an investor's overall financial plan. Creating retirement income requires coordination of several income sources, like IRAs, pensions and Social Security with income from a diversified investment portfolio. Your Janney Financial Consultant can help you determine your retirement income needs, consider future tax consequences and develop an appropriate investment strategy.

Contact your Janney Financial Consultant to discuss how they can help with your retirement income.

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