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DREAM BIG, ACT NOW: SIX SECRETS OF RETIREMENT

RETIRE THE WAY

YOU WANT

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HOW TO SEE IT

Fold the page over to reveal a bright future.

Money → COVER STORY

RETIRING THE WAY YOU WANT, WHEN YOU WANT, TAKES MORE THAN JUST SAVING EVERY MONTH. A GUIDE TO THE KEY DRIVERS OF POST-WORK HAPPINESS YOU MAY NOT HAVE CONSIDERED—AND WHAT YOU CAN DO ABOUT THEM.

BY BETH BRAVERMAN, DONNA ROSATO, AND PENELOPE WANG
PHOTOGRAPHS BY TRAVIS RATHBONE

TO GET THE DREAM RETIREMENT,



you need to save money and the markets need to give you a decent payback for your effort. No secrets there.

Hiding in plain view, however, are other keys to post-work bliss that are at least as important as savings rates and stock returns. Especially from your mid-forties, say, to your early sixties, you'll make money-related decisions that have clear implications for the near term but that require some imagination for you to see their critical impact on how you'll live 10, 20, or 30 years down the road. After consulting retirement experts and poring over the latest academic research, MONEY has identified five of these secrets and, as a sixth, found a new twist on that admonition to save, save, save. This story will lay out these hidden retirement drivers and help you make use of them in your planning. You'll also see how they could affect your finances in the years after you call it a career, based on numbers crunched by Jack VanDerhei at the Employee Benefit Research Institute, whose computer model simulates 100,000 possible market paths.

This special retirement issue continues with a quiz to help you see just how prepared you'll be for post-work life (open the foldout after page 72), and it also features an interview with an innovative researcher who has studied investors' blind spots when it comes to thinking about the future. Finally, you'll meet three couples who don't have to imagine what the transition to retirement will be like—it's upon them, and they have big decisions to make.



INVESTMENTS

THE SECRET: 16.6% IS THE MAGIC NUMBER.

HOW MUCH DO YOU NEED to save to retire?

It's a vexing question because different generations of savers have different luck. Some feel the market winds at their back during their careers, while others trudge through with low returns. Wade Pfau, professor of retirement income at the American College, which trains financial planners, has crunched the numbers to find a safe level of saving that would have worked in every historical market stretch going back to periods beginning in the



PROP STYLING BY LAURIE RAAB; GROOMING BY GREG CLARK

19th century. He found that setting aside 16.6% of income and putting it in a diversified portfolio of stocks and bonds did the trick every time. (Good news: Employer matches count toward that savings rate.) That's if you're consistent about saving over 30 years. A slow starter must ramp up higher—a 45-year-old with two times salary saved would have to go for 20%. “During some boom times, workers could get away with saving less, but you can't count on above-average returns,” says Pfau.

That's a useful warning right now because investors face some real challenges in the coming decade. Part of the problem is basic math: The 10-year Treasury bond yields less than 2%, and the Federal Reserve gives every indication that rates will stay low for years. “Current yields are a good predictor of bond returns,” says David Blanchett, head of retirement income at Morningstar Investment Management.

Stocks are less predictable—see the story on page 43 for reasons for optimism—but risks today include a wobbly global economy and an aging population who may prefer holding bonds to

stocks. The more you can save, the less you have to worry about this stuff.

TAKE ACTION

Do more than the max. For higher earners, “maxing out” your 401(k), as satisfying as it feels, might be a trap. Within your 401(k) you can save \$17,500 in 2013. Those 50 and older can save an additional \$5,500.

Because of IRS rules that prevent plans from benefiting mainly higher-income workers, some plans limit the contributions you can make even more, says Rick Meigs, president of 401khelpcenter.com. Step up savings by adding to a Roth IRA, where after-tax money can grow tax-free. You may not be able to invest directly in a Roth if your salary is above income limits. (Starting at

\$178,000 for married couples filing jointly in 2013, the amount you can contribute begins to phase out.) Fortunately there's a backdoor: Save in a nondeductible IRA, which you can then convert to a Roth.

Buy cheap funds—it's like saving more, but easier. One wrinkle of Pfau's study: He didn't include investing expenses in his returns. If you pay a management fee of 1% a year on your funds, says Pfau, the safe savings rate jumps to over 22%. You have one advantage over past investors who enjoyed more bullish times, though. You can buy index funds and ETFs that cost 0.10% or less.

Get in touch with the future you. Behavioral finance research suggests

that saving is easier if you spend a moment thinking about your future self. Look at an age-morphed photo of your face, and you are likely to put away more, says NYU researcher Hal Hershfield. You can get a glimpse of your older self via a mobile app, such as Aging Booth (IOS, 99¢; Android, free).

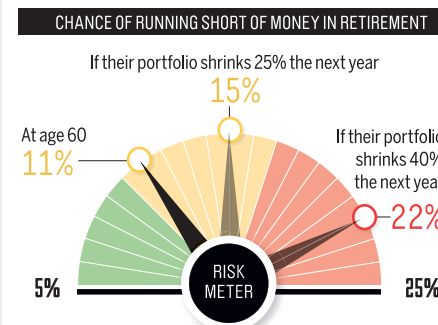
Know when to dial down risk. Five years before retirement, zero in on how much you'll need to pay essential expenses, says financial adviser Harold Evensky of Coral Gables, Fla. Shift the equivalent of one year of expenses to cash or short-term bonds so that if stocks plunge when your quitting date is in sight, you'll know you'll have some extra time for markets to recover. This cushion will help keep you from selling in a panic.

THE MARKET FACTOR: A BIG DROP NEAR THE END CAN REALLY HURT

Couple earning \$130,000 a year with \$500,000 saved at 60.

This married couple held on to a stock-heavy portfolio to age 60. EBRI says that this gives them a reasonable shot of not running out of money in retirement. But if they hit a 2008-like bear market at that age, they'll be faced with a choice of putting off retirement or living with an increased risk of running out of money. **For a less anxious ride, it's a good idea to start building a safer portfolio by 60.**

NOTES: Couple contributes 10% of income a year and works to 65. Home value \$250,000. Assumes random returns with an average of 8.9% for stocks and 6.3% for bonds. SOURCE: Employee Benefit Research Institute's Retirement Security Projection Model



HEALTH

THE SECRET: A GREASY BURGER IS WORSE THAN A BEAR MARKET.

WHEN IT COMES to retirement, good health cuts both ways. As any financial calculator will tell you, living longer actually means you'll need a bigger nest egg (see the graphic). But the healthier you are leading up to retirement, the easier it is to build up the savings you'll need. A recent National Bureau of Economic Research study by James Poterba, Steven Venti, and David Wise found that people who

were among the healthiest 20% in their fifties retired with three times the assets of the least healthy. And the healthy also spent down their wealth more slowly. Poterba says that's because the impact of health on your finances begins well before you quit working. "People in good health have lower health care costs, so they have less of a drain on their resources," he says. Also, other research shows that

about half of people who retire earlier than they planned cite health as the reason. Staying healthy gives you more power to save for longer.

TAKE ACTION

Know your numbers.

According to the U.S. Agency for Healthcare Research and Quality, one-third of adults with diabetes don't know it, and 20% of adults with high blood pressure are unaware. If you haven't been checked for a few years, do so now. Make sure your spouse does too.

Focus on what you can control.

Just because you have a family history of a health condition doesn't mean you'll get it as well. "DNA isn't your destiny," says Laura Carstensen of the Stanford Center on Longevity. "Research shows a very small number of factors make a big difference." Those probably won't come as a surprise: whether you smoke, how much you drink, your weight, and your exercise routine (you've got one, right?). Any smoking is bad, but how much alcohol or weight is too much? Here's the scoop: No more than seven drinks a week for women or 14 for men, according to the National

Institute of Alcohol Abuse and Alcoholism. For weight, check your body mass index at cdc.gov to see if you are in the healthy range.

You don't have to become a triathlete.

Just 2½ hours of moderate exercise a week can make the difference, according to the Centers for Disease Control. Need some extra motivation to hit the treadmill? People who are fit in middle age battle fewer chronic ailments in the last five years of life, so they get to enjoy more of their retirement being active and feeling good.



CAREER

THE SECRET: SUCCESS AT 50 MEANS A WHOLE A NEW SKILL SET.

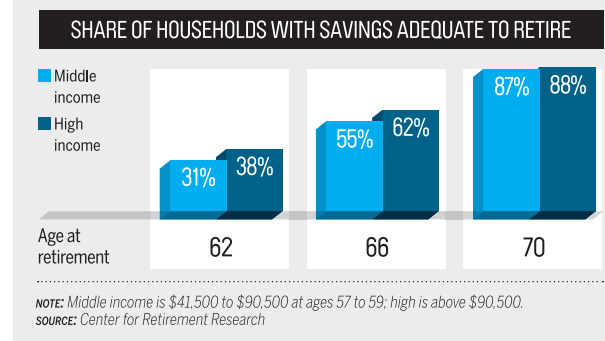
NEARLY HALF OF workers in their fifties expect to retire after 65, according to a survey by TransAmerica. Smart plan (see the graphic above). "You can't finance a

30-year retirement with a 40-year career," says Martha Deevy of the Stanford Center's financial security division.

The reality, though, is that many careers

A LONGER WORKING LIFE GETS YOU A LONG WAY

If you can wait to retire, your outlook is better, even if you're a high earner. You need to build a career that lasts, though.



don't make it to 65. (The median retirement age is 62.) Being pushed out early isn't the only risk; losing a job in middle age can leave a hole in your savings even after you get back to work.

You may not always be able to avoid a layoff, but "you can't afford to become complacent," says Geoff Hoffmann of recruiting firm DHR International. The rules of managing your career in its second half are different from those that worked when you were younger. You need a fresh strategy to get you up the ladder when there are fewer rungs to climb, with stiffer competition for jobs at your level.

TAKE ACTION

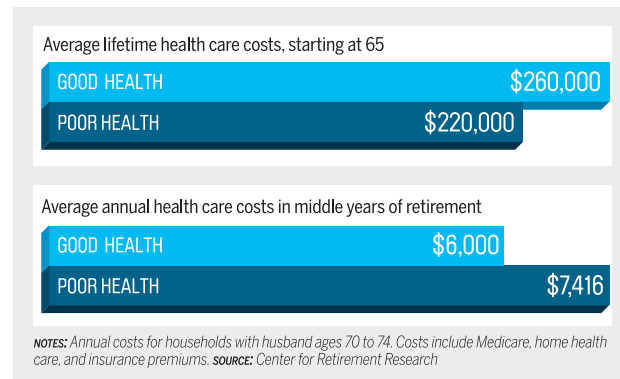
Go beyond mentors. Find champions. Early in

your career you may have had a mentor who showed you the ropes of your job. Later on, though, you'll need higher-level contacts who can sing your praises when it comes time for raises, promotions, or job cuts, and who can connect you to decision-makers in other departments or firms. "You want credible people who can advocate for you," says Hoffmann.

They may not be in the next cubicle over or people you're likely to see every day. Put yourself in positions to interact with senior-level people in a meaningful way: Seek out cross-departmental assignments or get actively involved in industry associations. People are more likely to champion you if they feel that you've been a champion for them too.

LONGEVITY COSTS, BUT IT'S A BARGAIN

Good health actually means you have to save a bit more—but that's just because you're living longer. Every year retired people devote a lot less of their budget to health care.



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In your networking, give at least as much as you hope to get.

■ **Show knowledge, not credentials.** After 45, pricey degrees may not be worth the investment. You simply have less career time to make the cost pay off. Employers do like to see, though, that you're still learning, says Scott Kane, founder of the job-placement service Gray Hair Management. Sign up for short courses that teach skills that apply to your industry. (Online providers Coursera and Udacity now offer many for free.) Or take on projects at work that force you to master a new technology.

■ **Focus on transferable skills.** Think about the things you've done that could be valuable to a wide variety of employers—for example, the time you overhauled a training program or spearheaded a cost-cutting team. Keep track of these accomplishments by regularly updating your résumé and LinkedIn profile.

FAMILY

THE SECRET: KNOW WHEN TO SAY NO TO THE KIDS.

THE PLAN WAS TO speed up on retirement saving once your kids were out of school. Then your son lost his job and moved back home—and Nana is becoming frail and needs help too. A new survey by Pew Research found that 48% of middle-aged adults with grown children gave them financial support in 2012. Some 21% with a

parent age 65 or older gave financially. Others gave time, which has its own costs; over 60% of those providing care are saving less for retirement as a result, says a survey by the National Alliance for Caregiving. And 15% in the Pew survey helped both adult kids and parents. "When it's both, it gets overwhelming," says

Milwaukee financial planner Alan Moore. By identifying early on what you can pay—and what you don't have to—you can save yourself both money and angst.

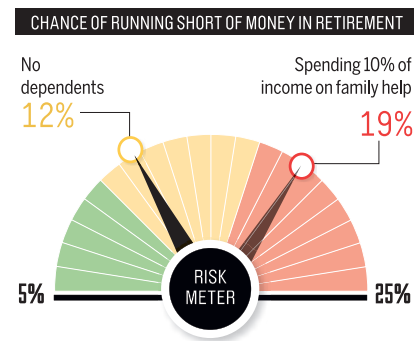
TAKE ACTION

■ **With your kid, draw the lines upfront.** One of Moore's clients ended up buying his son, who hadn't moved out, a house. "He told me, 'I just wanted my house back,'" says Moore. "I'm not sure he could really afford it." Even if things haven't gone that far and your kids are on their own, you may still be chipping in for health care insurance or cellphone bills. However you pitch in, "set clear expectations upfront—

THE FAMILY FACTOR: WHEN EXTRA NEEDS SLOW DOWN SAVING

Couple earning \$130,000 a year, saving 12% of income; \$300,000 saved at age 55.

A middle-aged couple find themselves in a particularly tight Sandwich Generation squeeze, helping out adult children while also providing financial support to elderly parents. Here's what EBRI says happens to their plan if they give up a tenth of their income to their family members and reduce their 401(k) contributions accordingly. **Setting limits on what you'll spend makes it less likely you'll lean on your kids later.**



NOTES: Couple contribute 12% of income a year and work to 65. Family care reduces available income. Home value \$250,000. Assumes random returns with an average of 8.9% for stocks and 6.3% for bonds. SOURCE: Employee Benefit Research Institute's Retirement Security Projection Model.

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even put it in writing," says Theresa Wan, a financial planner in Dumont, N.J.

Ask: What specific help does she need? If she's living with you, what rent will she pay, and for how long? (You could deposit "rent" into a fund she can use for future costs after she moves out.) Distinguish between investments in her future, such as a career counselor or job-related courses, and extras that should be her responsibility, like concert tickets.

■ **Get a clear view of your parents' finances.** That's often a tough conversation, but you can ease tension by enlisting a third party, such as a financial planner. If you know what Mom or Dad can afford when a problem arises, you can take steps together with them to avoid unnecessarily damaging your own finances. For example, it might become clear that if your parents downsize to a smaller condo, it would free up some money for paying a home health aide, perhaps forestall-

ing a costlier nursing home stay.

■ **Tap senior services.** Government and nonprofit agencies offer a range of help for the elderly, says Louise Schroeder, a financial planner in Stillwater, Okla. Services include adult day care and in-home aid, and may be low cost or free. To find help in your area, go to eldercare.gov.

■ **You'll face a time drain, but you can get a hand.** Having to provide aid to a parent gets in the way of your career and leaves little time left over for getting on top of your own financial planning. A geriatric-care manager can help oversee your parents' home and health services, says Schroeder. Search for one at caremanager.org; expect to pay \$150 to \$200 an hour.

■ **Don't miss tax breaks.** You may be able to claim adult relatives you help as dependents. For them to qualify you must provide more than half their financial support, says CCH tax analyst Mark Luscombe. Their gross income for the year, excluding Social Security, must also be less than \$3,900, as of 2013.

MIDLIFE CHANGES

THE SECRET: FORGET THE HOUSE. GO FOR THE PENSION.

RETIREMENT PLANS OFTEN go by the wayside when your marital status changes. "As a married couple, you have this vision of riding off into the sunset together when you retire. When the marriage ends, you have to create a new vision of your retirement," says Raleigh, N.C., financial planner Steve Gaito.

Divorce or having a spouse die young saps income and assets, making it much harder to continue saving the same way you did as a married couple. A recent survey by ING found that the average divorced person had \$10,000 less in retirement savings than the average married person, even though the divorced respondents were typically five years older. Women often find themselves especially pressed: Household income drops 41% for women after a divorce and 37% in widowhood, compared with under 25% in both cases for men, according to a report by the Government Accountability Office. Although family changes put a lot of immediate worries on your plate, it's crucial to keep one eye on your long-term plan.

→ RETIRE THE WAY YOU WANT



TAKE ACTION

❑ **Don't make 401(k) and pension plans an afterthought as you split up assets.** While your first impulse might be to go for the family house, weigh the benefits of doing so if it means getting less of the retirement accounts you and your spouse built up together. "The spouse who gets the retirement plan assets may be in much better shape for retirement than the one who got the house," says RegentAtlantic investment adviser Chris Cordaro. Houses are illiquid and have

carrying costs that may be difficult to maintain on a single person's income. Sometimes the best strategy for both parties is to sell the house, split the equity, and downsize.

❑ **Next, take control of your portfolio choices.** If you get a portion of your spouse's workplace retirement accounts, the court will sign off on a qualified domestic relations order. With a traditional pension, this allows your spouse's plan to create a separate account in your name. If it's a 401(k), the money could either go into an IRA or be kept in your name with your spouse's plan administrator, with a choice to roll over

later. Converting to the IRA is usually best, as this will give you a wider choice of investment options and more control over the fees you pay.

❑ **Keep the investing part simple.** Since in many couples just one spouse handles the chore of managing investments, you might feel like you suddenly have to climb a steep learning curve to run your retirement funds. An easy start: Put the money in a target-date fund, which gives you a premixed, diversified portfolio appropriate for your age, at least until you've had a chance to consider other investments. The target funds from T. Rowe Price and Vanguard are on the MONEY 70 list on page 110.

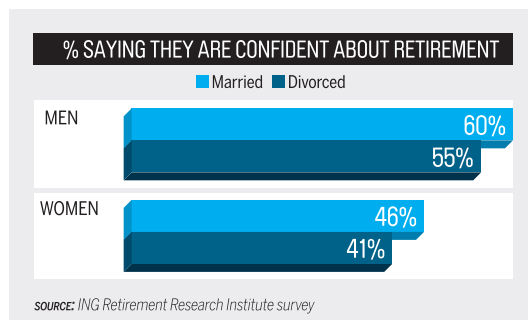
❑ **If you remarry, you can keep the money separate, but don't let it be a secret.** Prenuptial agreements are more common in second marriages, particularly if spouses want to preserve their assets for their own children. That doesn't mean you shouldn't be

working together toward your goals. "Individuals can keep things legally separate, but mentally they need to manage everything as if it's one," says financial planner Jacob Gold of Scottsdale. That means coordinating your investment strategies so that you're well diversified and discussing outstanding debt or other obligations that you may have to deal with in retirement.

❑ **When facing a spouse's early death, give yourself a financial cooling-off period.** You may suddenly have a lot of money—from life insurance or retirement accounts—to deal with at all once. And that means you'll soon hear from people, whether it's a well-meaning family member or an agent or broker, with ideas for how to invest it. Park the money somewhere safe for the short-term. If you let six months or a year pass while you deal with the emotional impact of the loss, you can make financial decisions with a clearer head.

THE RETIREMENT GENDER GAP

Women especially worry they won't have enough, and divorced women have the most concern.



RETIRE THE WAY YOU WANT

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DEBT

THE SECRET: BURN THE CREDIT CARDS, NOT THE MORTGAGE.

EVEN LONGTIME savers sometimes retire in the red, perhaps after getting pinched by a job loss or a health problem. An Ameri-prise survey of older workers with at least \$100,000 in assets found that 22% weren't on track to

pay off their credit cards by retirement. High-cost debt is especially dangerous in retirement because you are likely to see your income go down, and if you draw heavily on your nest egg to keep up with payments, you're

more vulnerable to outliving your money. Well before 65, have a plan to wind down those obligations.

TAKE ACTION

➤ **Paying off pricey debt is the only good reason to save less.** Just make sure to put away enough to get any employer match.

➤ **Use these rules of thumb for college debt.** It's tempting to take big loans to pay for a kid's dream school. Have your child look into Stafford loans first (borrowing over four years no more than his projected first-year salary), and then consider Parent Plus

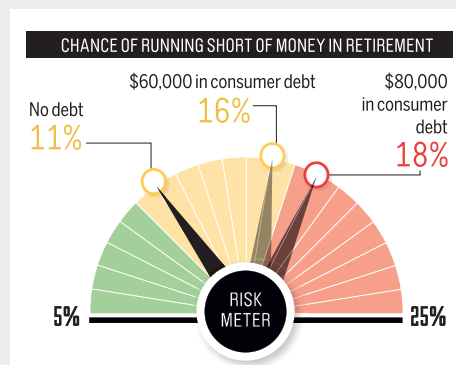
loans or co-signing on a private loan. The rules: Don't borrow more for all of your children than your annual salary. And be sure you can pay it off in 10 years or by the time you retire, whichever is first, says Mark Kantrowitz of FinAid.org.

➤ **There's less rush to pay off a mortgage.** With today's rates and favorable tax treatment of mortgage interest, you may be paying less than 4%. Eliminating the mortgage can make sense, since it lowers your expenses. If you can afford the payments, however, you can hang on to the loan to leave more of your money in a diversified portfolio, says Kimberly Foss of Empyrion Wealth Management. If most of your assets are in a tax-deferred account, then by not cashing out, you're also deferring taxes as your investments continue to grow. **M**

THE DEBT FACTOR: BEWARE THE OVERHANG

Couple earning \$130,000 a year, saving 10%; \$500,000 saved at age 60.

Going into retirement with a lot of nonmortgage debt means having to devote a substantial chunk of what you've saved to paying off past spending. EBRI compared the outlook for three couples with the same savings; the only difference is in their monthly bills. **It can make sense to lower your savings rate if it lets you pay down expensive loans.**



NOTES: Couple contribute 10% of income a year and work to 65. Home value \$250,000. Assumes random returns with an average of 8.9% for stocks and 6.3% for bonds. SOURCE: Employee Benefit Research Institute's Retirement Security Projection Model

