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Kevin M. Lynch
The American College of Financial Services

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Living Too Long
Where will you live, and how will you finance it?
by Kevin M. Lynch, CFP®, ChFC®,CLU®, RHU®, REBC®, CASL®, CLF®, CAP®, LUTCF, FSS

Help ensure your clients enjoy retirement where they want.

WHEN A PERSON RETIRES, a shift in spending patterns tends to manifest itself throughout the different stages of a person’s retirement. Initially, as you leave the work force, there is, of course, a reduction in the taxes you pay. In the preretirement period, you were paying FICA taxes and spending money on work-related needs, such as commuting expenses and meals away from home. After retirement, many of these expenses decrease while others increase. Household expenses decline steadily with age. Using age 65 as a benchmark, household expenses decline by 19 percent in the first decade of retirement, 34 percent by the end of the second decade of retirement and 52 percent by the end of the third decade in retirement. “Home and home-related expenses remain the single largest spending category for older Americans,” according to Sudipto Banerjee of the Employee Benefit Research Institute. Banerjee further reports, “Health-related expenses are the second largest component in the budget of older Americans. It is the only component which steadily increases with age. Health care captures around 10 percent of the budget for those 50-64, but increases to about 20 percent for those ages 85 and over.”

As financial service professionals, what does this mean to you? How can you use this data to better advise your clients on retirement issues?

Because home and home-related expenses play such a major role in a person’s post retirement budget, it is important that you understand your client’s needs and desires for where they want to live and how they can afford to pay for it.

To begin with, we will look at the age-old assumption that when people retire, they will downsize. I am, of course, referring to the practice of selling the larger family home, usually paid for, and using the proceeds to purchase a smaller, more suitable home in an area where the client wants to live during retirement. It is assumed that the proceeds from the sale of the older, paid-for home will be sufficient to pay for the new home in cash, and perhaps even have a surplus to be added to the client’s retirement income-generating assets. According to a Rand Labor and Population Working Paper (Banks, Blundell, Oldfield, & Smith, 2010), since the first studies of downsizing in the U.S. (Merrill, 1984, and Venti and Wise, 1989, 1990), there has been a reduction in the number of rooms in household residences as age increases. This research would tend to verify the commonly held belief that older Americans do downsize in retirement. In addition, when researchers study mobility in Americans age 60 to 70, there is evidence that, among the considerations primarily
influencing the older American’s decision to relocate, is pursuit of a warmer climate, lower taxes and lower cost of living. For the oldest Americans, however (especially those over 80), being closer to family ranks higher in importance than do those considerations previously mentioned. For these oldest Americans, the need for care due primarily to the frailties of older age takes precedence over lifestyle and amenities available elsewhere. Because of the limitation of sample sizes of these oldest American’s, though, statistics do not tell the complete story. As your clients’ trusted advisor, you must explore their specific feelings and desires in this area.

Another issue with which your client may have to contend where downsizing is concerned is the major disruption to the housing market since 2008. In addition to major turmoil in the financial markets, which caused many to delay retirement between 2008 and 2010 due to decimation, or at least partial depletion, of their retirement nest egg, real estate values plummeted during the same period. The housing market, as we knew it, may be changed forever, according to research by The Demand Institute (Keely, van Ark, Levanon, & Burbank, 2012). The Institute’s findings indicate that although the worst is over for the U.S. housing market and a recovery is beginning, the recovery will occur in two stages and be led by a demand for rental properties. It is estimated that rental demand will help clear out the huge supply of existing homes on the market, which were a result of large numbers of foreclosures. Using 2005 as a baseline, during the recent disruption in the housing market, there was a 129 percent increase in foreclosures from 2005 to 2011. The Demand Institute estimates that it will take two to three years to clear out the oversupply of existing properties.

What does that mean to you and your clients? These factors in the real estate market may have a negative impact on older Americans wanting to sell large, expensive homes during the initial recovery stages, because rental demands will come primarily from younger people and immigrants, and younger people were hit particularly hard during the recession that is currently ending. In addition, the recovery will not be uniform across the states and will even be vastly different within states. This could affect your clients, as well, by making it hard to sell their current property and being in competition with others seeking to purchase smaller homes in which to spend their retirement.

“Where do I want to live in retirement?” and “How will I finance my retirement housing and household expenses?” are both important questions for you to help your clients resolve. The challenges in doing so will require your best efforts and perhaps the assistance of a real-estate professional to help your clients through the various stages of the market’s recovery.