

Managing Your Retirement Assets In The Age of Medical Miracles

RetirementDNA

mapping retirement & executive benefits for biotech & life sciences leaders

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Our country and the entire world have been blessed with tremendous inventions throughout history that have brought lifestyle improvements. From the Industrial Revolution to the still progressing Technology Revolution, the end results have improved life and increased productivity.

Now well into the new century, we have already entered a revolution that will bring about many societal changes, some good and some bad. A revolution that will potentially eradicate many diseases; a revolution that will pave the path for genetic augmentation and disease prevention; a revolution that may challenge the very meaning of what it means to be human. The revolution we are referring to is The Biology Revolution.

This article has been written to help investors better understand The Biology Revolution and its impact on retirement planning. It will not consider the social and political aspects of The Biology Revolution as this is best left for personal reflection. Rather, the focus of RetirementDNA is to help investors build and protect their retirement capital. Therefore we will only address The Biology Revolution as it impacts the accumulation, protection, and income distribution of retirement assets.

The 6Ls of Retirement Risk

Before we consider the specific impact of The Biology Revolution on retirement planning, let's first review the six key risks that every investor faces in building and managing a retirement nest egg.

- Lack of capital
- Losses on investments
- Loss of income
- Long-term care
- Longevity
- Litigation

These are the six risks that every investor faces, as we've discussed in our prior articles. The Biology Revolution has a significant and direct impact on two of these risks – longevity risk and long-term care risk. These two risks combined dramatically impact investors' savings strategy. To learn how, let's now consider the connection between biology and retirement.

The Biology Revolution and Retirement Risk

During the twentieth century, average life expectancy in America increased by about 50%; the average person could expect to live to 76 years old. What is particularly amazing about this fact is that the increase came without a major medical breakthrough! In fact, most of

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the increase in life expectancy is attributable to a dramatic improvement in infant mortality rates. The twenty-first century will be different. This century will truly become the age of medical miracles and biological improvement. Many leading scientists and biologists believe that we may experience life expectancy improvements in the next twenty years alone that match those of the last hundred years!

Most Americans are not aware that in the last 5 years...

- The mapping of the human genome has led to incredible discoveries in the genetic manifestation of disease and potential gene therapies.
- Many believe the “biological clock” can potentially be reset at the cellular level using telomerase, stopping cell senescence (aging.) This would allow cells to continue dividing without becoming cancerous; clinical trials have already begun.
- An anti-aging pill, which acts as an anti-oxidant against free radicals and proven to be effective in some organisms, may be on the market by 2006.
- Tissue engineering has already been used to treat damaged hearts by injecting thigh muscle cells into damaged heart tissue to regenerate healthy heart muscle.
- A tissue engineered heart valve is now on the market in Europe. This new valve will replace pig valves and minimize tissue rejection.
- A pill that mimics the benefits of low calorie diets is being developed, as the potentially controlling “sir2” gene and the cellular pathway are better understood.
- Bioengineered corneas have been successfully implanted at the University of California Davis, restoring complete sight in 10 of 14 blind patients.

- A longevity gene, possibly identified on Chromosome #4, is leading to discussions of a longevity pill. Consider the incredible story of the Kahn siblings and their amazing 136 billion to one longevity story.

- Replacement body parts for every body part by 2035.

You don't have to be a scientist to comprehend the incredible impact of these biology-based discoveries now taking place. Even when it comes to retirement planning, the impact of a 5-10 year increase in life expectancy is potentially devastating.

What should investors do to effectively manage their assets during this new age of medical miracles?

When it comes to retirement income and asset management, there are three uncertain yet key determinants that drive the management process. These three determinants are now outlined along with our specific recommendations for investors.

1) Life Expectancy: If you knew exactly when you would need your last income check from your nest egg, retirement income management would be pretty easy. The new reality is that assuming life expectancy to age 90 or greater is the conservative and prudent way to plan. Our

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recommendation is that a life expectancy of 90 be used if single and 95 if married.

2) Rate of Return Assumptions: The era of 12%-15% assumed rates of return are gone. Markets move in cycles. So although we had a great run from 1982-2000, the next 15 years may deliver returns of only 5%-7% assuming a “balanced” and diversified portfolio.

Assuming too great a return on your investment will leave you far short of what you need for retirement. We recommend that retirees assume a rate of return of no more than 7% on their portfolio.

3) Withdrawal Rate Assumptions: This is an area where both investors and their advisors make many mistakes. It is not uncommon to see retirees withdraw far too much from their retirement plans than is sustainable given longer life expectancy and lower returns. Our research indicates that a withdrawal rate of 4.5%, with annual inflation or five year adjustments, should be utilized.

Longevity Insurance: Hedging Your Bet During The Biology Revolution

Even when using these conservative assumptions, there still remains the possibility that an investor could run out of money during retirement. In fact, our research shows (based on historical rates of returns from 1946-1999) that an investor with a balanced portfolio (40% stocks, 40% bonds, and 20% cash) withdrawing 4.5% per year with an annual inflation adjustment would have run out of money nearly 25% of the time after only thirty years! A conservative investor (20% stocks, 40% bonds, and 40% cash) would have run out of money 67% of the time! (We should point out that a conservative portfolio with 4.5% inflation-adjusted withdrawals performs so poorly under historical return simulations that we strongly rec-

ommend against such an approach.)

Since there is a strong possibility of running out of money in retirement, how do you hedge your bets? The solution is “longevity insurance.”

As with all types of insurance, longevity insurance will shift risk away from you and to an insurer that can afford to assume risk. Specifically, longevity insurance takes a portion of your retirement assets and purchases an immediate annuity. When you buy an immediate annuity, the insurance company guarantees an income for the rest of your life – even if you live to 120 years old!

Our research indicates that buying an immediate annuity as longevity insurance with 25% of the retirement assets can reduce the risk of running out of money in retirement by 50% for a balanced investor. The same research shows that a forty year retirement assumption would require about a 50% allocation of retirement assets to longevity insurance in order to minimize the risk of running out of money to an acceptably low level.

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A Summary of Recommendations

Increasing life expectancies – longevity risk – is a new reality for investors. Longevity risk is high enough that many investors will run out of money during their retirement. For those investors who share our concern about this risk, we provide guidance with four key retirement planning recommendations.

Recommendation #1: Assume life expectancy through 90 for individuals and 95 for married couples.

Recommendation #2: Assume no greater than a 7% rate of return on your retirement assets.

Recommendation #3: Withdraw no more than 4.5% with annual inflation adjustments from your portfolio.

Recommendation #4: Consider longevity insurance for your portfolio by placing a portion of your assets into immediate annuities.

For more information on longevity insurance, and retirement income and asset management during the age of medical miracles, contact RetirementDNA.

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