Eight core ideas for retirement planning: Wade Pfau

By Editorial Staff *Thu, Feb 18, 2016*

Here are eight useful principles from the award-winning economist and professor of Retirement Income at The American College of Financial Services.

In an article published this week in **Advisor Perspectives**, Wade Pfau, Ph.D., the director of the doctoral program in Financial and Retirement Planning at The American College in Bryn Mawr, Pa., describes what he calls “eight core ideas” to guide retirement income planning.

Here are those eight ideas, along with summaries of the explanations Pfau gave in his article:

Play the long game. Strategies that emphasize long-term planning over short-term expediencies include delaying the start of Social Security benefits, purchasing a single-premium immediate annuity (SPIA), paying a bit more taxes today to enjoy lower taxes in the future, making home renovations that support aging in place, setting up a plan that accounts for the risk of cognitive decline and opening a line of credit on a reverse mortgage.

Don’t leave money on the table. The holy grail of retirement income planning includes strategies that enhance retirement efficiency. If one strategy allows for more lifetime spending and/or a greater legacy than another strategy, then it is more efficient.

Use reasonable expectations for portfolio returns. You should not expect to earn the average historical market returns for your portfolio. Half the time returns will be more than average and half the time they’ll be less.

Avoid plans that assume high market returns. Stocks potentially offer a higher return than bonds as a reward for their additional risk. But this ”risk premium” is not guaranteed and may not materialize.

Build an integrated strategy to manage various retirement risks. Retirement risks include unpredictable longevity and an unknown planning horizon, market volatility and macroeconomic risks, inflation and spending shocks. Each of these risks must be managed by combining different income tools with different relative strengths and weaknesses.

Approach retirement income tools with an agnostic view. The most efficient retirement strategies require an integration of both investments and insurance.

Start with the household balance sheet. A retirement plan involves more than just financial assets. This has been a fundamental lesson from various retirement frameworks, such as Jason Branning and M. Ray Grubbs' Modern Retirement Theory, Russell Investments' Funded Ratio approach and the Household Balance Sheet view of the Retirement Income Industry Association.

Distinguish between "technical" and true liquidity. In a sense, an investment portfolio is a liquid asset, but some of its liquidity may be only an illusion. Assets must be matched to liabilities. Some, or even all, of the investment portfolio may be earmarked to meet future lifestyle spending goals, and is therefore less than fully liquid.