What happens when a bear market coincides with a care market for a couple without a pension?

For many retirees who have accumulated substantial sums for retirement, the prospect of a severe bear market may seem like the biggest risk to the sustainability of their retirement assets. But another and perhaps more insidious risk lurks: a health crisis requiring long-term care services. What happens if both of those events happen at the same time?

A growing cadre of retirees are embarking on their golden years without the support of a pension, with Social Security likely to be their only source of dependable, rock-solid cashflow. The remainder of their retirement income will have to come from the often-considerable sums – commonly exceeding seven figures - that many have accumulated over a long career.

But when faced with both a declining market and a long-term care event, even seven figure portfolios may face early depletion. And with 50% of 55+ folks facing a future LTC event and only 7% of those with current LTC coverage, a huge planning gap… and opportunity…. is there for those in the know.

> **"A comfortable retirement all starts with planning, including planning for the unknown."**

Typical Retirement:
Withdrawal from Accumulated Assets + Social Security

Many of these retirees will need more cashflow to support their retirements than Social Security alone will provide, so the remainder will need to come from their portfolios via regular withdrawals. A common method for producing cashflow from a typical balanced portfolio of stocks and bonds is to withdraw 4% of the initial value of the portfolio at retirement, and then increase the dollar value of those annualized withdrawal by the rate of inflation, or about 2.5-3%.

This method has been analyzed extensively and is believed to provide a high likelihood (not guaranteed) of that 4% inflation adjusted cashflow lasting for a 30-year retirement. For example, a $1 million portfolio would be sufficient to generate about a $40,000 annualized real income over a 30-year period.

Care Market:
A Long-Term Care Event During Retirement Will Push Withdrawals Well Over 4%

Any withdrawals higher than 4% of the initial portfolio value will reduce the probability of that cashflow being sustained for a 30-year period. Given the median annualized cost of long-term care services in the USA is between $68,000-$116,000 (Genworth), one can see the withdrawals needed in retirement will change drastically for those facing a need for LTC services.

Consider a recently retired couple with $3 million in a balanced portfolio at age 67. They are targeting a $180,000 income in retirement, of which $60,000 will come from Social Security. The other $120,000 will come from their portfolio, which will be covered using the 4% withdrawal method ($3,000,000 x 0.04 = $120,000). That 4% withdrawal could overnight become a 7% withdrawal if one member of that couple suddenly fell ill and required long term care services at $100,000 a year. That $100,000 cost of care would immediately become the equivalent of a 3.3% withdrawal ($100,000/$3,000,000), on top of the 4% withdrawal already being taken.

Now throw in a bear market just as the care event is unfolding, and you've got a real problem that can rapidly deplete a seven-figure portfolio earlier than planned. For example, a 60/40 portfolio (source: lazyportfolioetf.com) lost 30% of its value in the 16 months from November of 2007 until February of 2009, and didn't recover until October of 2010. That's a total of 36 months for a portfolio of 60% stocks and 40% bonds to finally return to its value from three years earlier.

If this same couple found themselves needing to withdraw about 7% of their initial portfolio value during that period, the results could be devastating to the remainder of their retirement.

Summary

A comfortable retirement all starts with planning, including planning for the unknown. The classic "Big M" unknowns of Mortality (when will you die?) and Market performance (how will the market perform when I need the money?) have been well addressed by the annuity industry's current crop of products. But the third big M – Morbidity – remains a highly exposed and unaddressed risk for most.