HM Payson PLANNING NOTES

July 27, 2016

MOLLY C. REINFRIED, CFP®

MICHELLE R. SANTIAGO, ESQ.,CFP®

Toni M. Mead, Contributor & Editor

RETIREMENT CONSIDERATIONS FOR WOMEN

It is well known that there is a gap in pay between men and women – women working full time earn roughly 77 cents for every dollar earned by men[1] – however, it is far less commonly discussed that there is also a retirement gender gap. The poverty rate of women over 65 is 64% higher than that of men[2], and retired women are half as likely to have pensions or other income[1], with 25% of retired women living on Social Security alone[1]. It comes as no surprise that, in a recent survey, 57% of women reported a fear of running out of money – second only to fear of losing their spouse[2]. The retirement gap is primarily due to longer life expectancy and lower lifetime earnings but is exacerbated by a lack of confidence and knowledge in the areas of saving and investing.

Given the gap, it is especially important for women to be informed and to have a plan. Financial education can increase confidence in women's abilities to formulate and execute investment and money management decisions, while an awareness of the challenges facing women can better inform the decisions they make while creating a retirement plan.

Understanding the gap

Higher lifetime spending:

The average woman's life expectancy is 80.1 compared to 74.8 for men[1]. This translates to more years in retirement, higher costs for long term care, disability insurance and medical insurance, and a higher likelihood of living alone during retirement – according to a 2004 study, 57% of women 65 or older were single, compared to 24% of men[1].

On top of the higher costs associated with longer life expectancy, there are a number of other things that cost more for women. These include mortgages, cars, personal care services such as dry cleaning and haircuts, personal care products, and clothing[3].

Lower lifetime earnings:

As mentioned above, there is a pay gap of 77 cents on the dollar for all women employed full time, but there is also an employment gap. Due to the fact that women are more likely to take on the responsibility of caring for children and disabled or elderly relatives, they are also more likely to work part time or leave work temporarily or altogether – 25% of all working women work part time as opposed to 11% of all working men[1].

Working part time and moving in and out of the work force are correlated with fewer pay increases, fewer advancements and training opportunities, and reduced access to employee benefits including employer sponsored retirement plans; this means missing out on employer matching contributions and a reduction in saving and investment potential[1].

The pay gap and the employment gap work together to create an average lifetime earnings gap; a woman in Maine with a 40 year career will earn on average $385,880 less than a man over her lifetime[4]. This leads to less opportunity to save as well as a smaller earnings record and, therefore, a smaller Social Security benefit in retirement.

Behavioral differences:

While women have fewer resources to save, they are also less likely to do so. Women who are eligible for employer sponsored retirement accounts are less likely to save than men, and those that do participate commonly save a smaller percentage of their income[5]. Furthermore, women are less confident investors with lower risk tolerance and less likelihood to invest at all[5].

Create a plan

Taking a hard look at the differences can be discouraging, but it's important to know what you're up against when making choices about your lifestyle and retirement goals. Additionally, an awareness of the differences highlights the importance of creating a plan and starting early.

The first step: Budgeting

For many, the greatest risk to their financial plan is one they can control – their spending – and for women this is an even greater risk given their longer life expectancy and higher costs. The first step in gaining control of your spending is to create a budget. This exercise will inform you of your earning and spending habits and help you determine and achieve savings goals.

To get started with a budget, it is important to identify your sources and uses of cash. Your sources might include salary, Social Security or portfolio withdrawals. Your uses of cash include your fixed expenses (mortgage payments, utilities, insurance, property taxes, healthcare, etc.) plus your discretionary and lifestyle expenses.

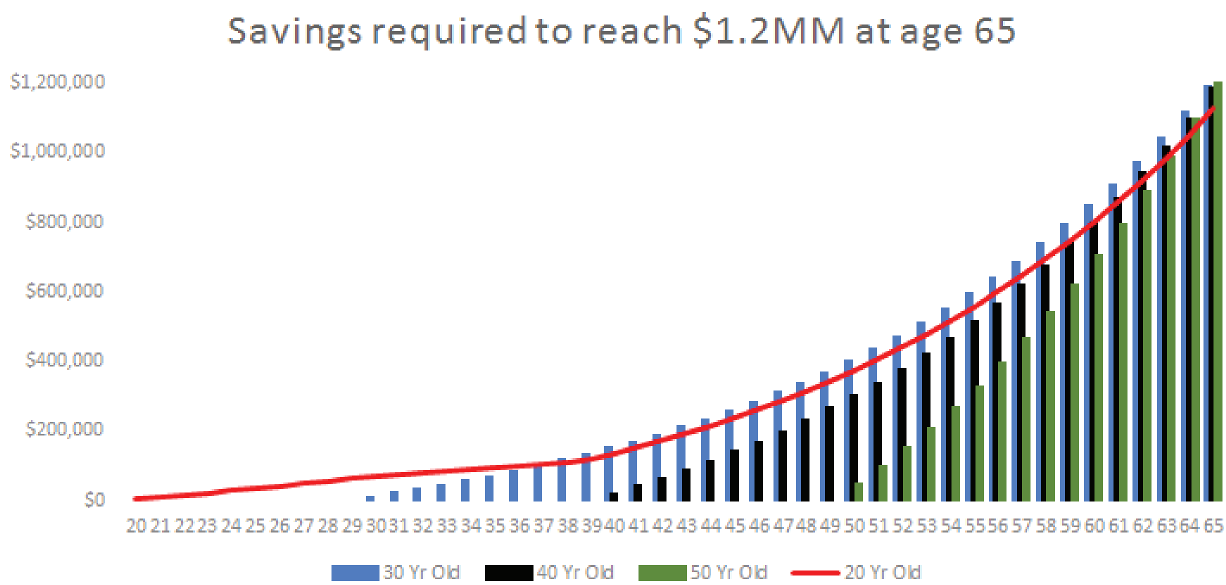
In order to keep uses of cash in line with your sources of cash, you need to consider your financial priorities. It is important to find a financial balance among your priorities and reflect that in your spending. The standard budget guideline is to take the 50/20/30 approach, allocating 50% of your income to your essential living expenses, 20% to savings (15% to long term goals and 5% to short term goals) and the remaining 30% to discretionary spending. However, this standard might need to be customized depending on your lifetime goals, earnings and other circumstances.

Once a basic budget is in place, you can use it to help create a plan to achieve your goals, including determining how much you will need to save for retirement given projected income and spending habits, estimated Social Security or pension benefits, and the age at which you can comfortably retire.

July 27, 2016

The most important step: Saving

Saving is the best way to prepare for your lifetime financial goals. Retirement, buying a home, sending children to college and caring for parents are among some of the financial challenges that people save for. This can be difficult for women when trying to balance multiple roles including working, parenting and caregiving, but the most important step to take is to get started. Although retirement may be years away, time is a valuable asset allowing investment returns to compound. Starting early is especially important given women's lower lifetime earnings. Saving early can help offset lower wages and potential years spent working part time or not at all.



For example, a 30 year old who begins saving $10,000/year, generating a 6% annual return, with plans to retire at age 65, will accumulate approximately $1.2MM at retirement. Comparatively if she does not begin saving until age 40, she must double the savings rate to $20,000/year to attain $1.2MM at age 65. A 50 year old must save $47,000/year to achieve the same results! Alternatively, if she had started saving $5,000/year at age 20 until age 30 when she was out of the workforce for 10 years but her funds remained invested generating a 6% return and she then saves again at $10,000/year from age 40 to age 65, she would accumulate $1.1MM at retirement.

Here are a few savings goals to work toward:

- Contribute to a retirement plan at work if you can, at least to benefit from the employer match; don't leave this money on the table.

- Once you are saving at least enough to benefit from your employer match, work on building your retirement savings rate to 15% of income by raising your contribution percentage by 1% each year, keeping in mind that the maximum employee contribution for most employer sponsored plans is currently, $18,000/year, with an additional $6,000 for those age 50 and older.

- There is a current tax benefit to saving to a tax deferred retirement plan. Saving $1,000 per month may only reduce your take home pay by $600 or $700. Most people can save some dollar amount pretax with minimal impact to their paycheck.

- For those years spent out of the workforce, take advantage of contributing to a spousal IRA utilizing household income to continue saving toward retirement.

- Although you may have children or other dependents who need financial support, make a commitment to pay yourself first and always save a portion of your income for retirement.

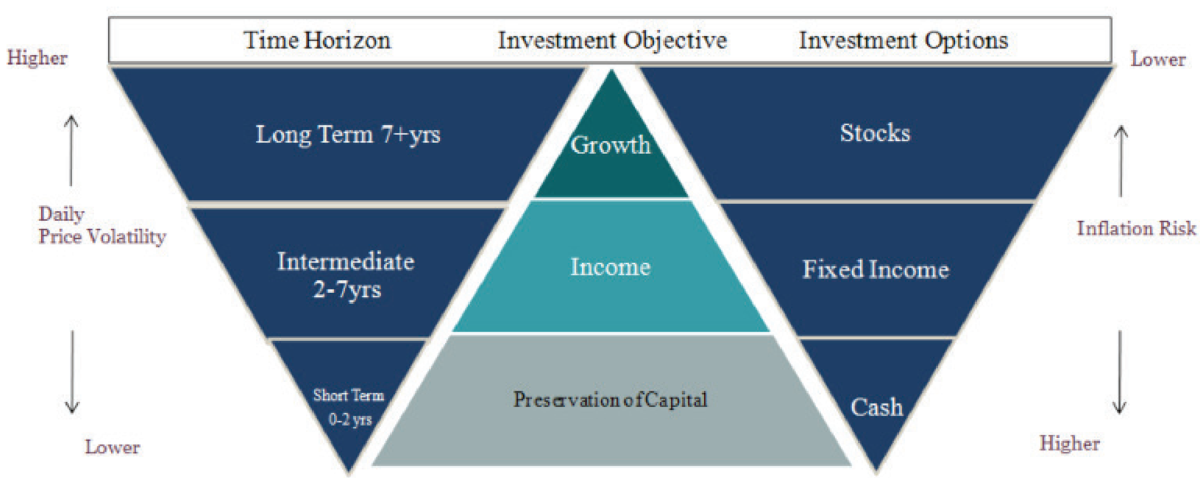
Making your money work for you: Investing

While saving is arguably the most important step toward preparing for retirement, it is unlikely that you will be able to reach your goals by saving alone. Annual inflation depletes the value of your savings and over time it can significantly erode the spending power of your money. The highest savings account interest rates today, at about 1.1%, fall well under the 2% target inflation rate (2.25% historical average)[6]. Investing your savings can help you outpace inflation and, if done wisely over a long period of time, could compound to return more than you could earn in your lifetime.

July 27, 2016

Studies have shown that women approach investing differently from men. Common traits among women include investing more conservatively, trading less frequently (a good thing), and a greater willingness to stick to a plan. Having a sound investment strategy and understanding what you own and why you own it are critical ingredients for success. Each of these go a long way toward creating investor confidence, which is important as 90% of women will end up managing their finances on their own at some point in their lives.[5]

The conventional approach to investing is to shift your assets as retirement approaches so that your cash and bond allocations account for the majority of your portfolio. With retirement often lasting 20-30 years, however, inflation will likely have a significant impact on your cost of living. While conservative investments such as cash and bonds provide short-term stability, they do little to protect you from the long-term effects of inflation. Stocks, on the other hand, while offering little stability in the short-term, are well suited to hedge against the longer term inflation risk given their greater potential for growth of principal and growth of dividend income.



Therefore, in retirement, it is important to ignore convention and to adjust your asset allocation according to your financial needs rather than your age. We suggest having sufficient cash and short-term bonds to fund short-term needs (0-2 years) and intermediate-term bonds to cover intermediate-term needs (3-7 years). Long-term assets, such as stocks and real estate, are better suited to fund longer term cash needs (beyond 7 years). While there are no guarantees with owning stocks, seven years should be sufficient time to allow the stock market to go through its short-term cycles and provide a better rate of return than bonds. Allocating your portfolio investments in this manner creates a portfolio more specific to meeting your retirement needs than subscribing to general rules of thumb.

Other considerations: Risk management

While saving and investing are the most important steps to take toward achieving your retirement goals, there are other things to consider:

- When making a decision to leave the workforce or work part time to provide family care, it is important to consider all angles. While care costs can be high, often consuming most of a woman's take home pay, if you choose to leave the work force or work part time, it could affect more than just your household income. The impact to future earnings potential and reduced savings potential, including employer contributions to your retirement account, should also be considered.

- When taking on the responsibility of caring for an elderly relative, be sure to consult local agencies on aging to be sure that you are taking full advantage of any services that might allay costs or provide support to you as a caregiver.

- Life insurance should allow for a similar lifestyle to be maintained in the event that one spouse predeceases the other. Consider insurance to replace the potential loss of household income and cost of family care.

- Disability insurance can protect the household against a loss of income in the event of a disability. It is important to note that disability insurance tends to be more expensive for women; they are more likely to file a disability claim due to maternity leave and the fact that they are more prone to conditions such as auto immune disorders, depression, and mental health[7].

- Long term care insurance should be considered to reduce the risk of drawing down household assets for the health costs of one partner thus leaving no financial support for the survivor. Because women have longer life expectancies, it is often more important to insure a male partner. Additionally, given their longer life expectancy and the conditions discussed above with disability insurance, long term care insurance is more expensive for women. Consider obtaining a shared long term care policy; this decreases the cost and allows for both partners to share the coverage depending on who needs it first.

Moving forward:

Planning for retirement is a challenging goal for everyone, and it is not uncommon for soon-to-be retirees, regardless of gender, to find that there is a sizable gap between their spending needs and their income sources. Above, we have highlighted the retirement challenges specific to women (life expectancy, lower earnings, etc.) and introduced the basics involved in creating a plan. While an awareness of the challenges and knowledge of basic planning tools can help women narrow the gender gap, it is important to note that the information presented here is merely a starting point.

For a more in-depth discussion of the tools introduced here and other topics relevant to creating a plan, please visit our 10 Planning Issues When Considering Retirement newsletter.

Sources:

1. *"Women Face Unique Challenges When Planning For Retirement." WISER. WISER, 15 March 2006. Web. 5 July 2016.*
2. *Holland, Kelley "You thought the wage gap was bad? The retirement gap's even worse." CNBC LLC. CNBC, 19 October 2015. Web. 5 July 2016.*
3. *Hill, Casey "6 times it's more expensive to be a woman." Market Watch Inc. Market Watch, 12 April 2016. Web. 5 July 2016.*
4. *"The Lifetime Wage Gap, State by State" NWLC. NWLC, 4 April 2016. Web. 5 July 2016.*
5. *Spann, Scott, PhD, CFP, Gregory A Ward CFP, Cynthia Meyer, CFA, CFP, ChFC, and Liz Davidson, CEO, Financial Finesse, Inc. "Study Finds 26% Gender Gap in Retirement Shortfall for Median 45-Year-Old Employees." Press Release Distribution, EDGAR Filing, XBRL, Regulatory Filings. BusinessWire, 2015. Web. 5 July 2016.*
6. *"The Importance Of Investing Your Savings" Value Walk. Value Walk,14 November 2015. Web. 5 July 2016.*
7. *"Widening the Disability Insurance Gender Gap" Physician Advisors LLC. Physician Advisors, 2015. Web. 5 July 2016.*