THE PSYCHOLOGICAL IMPACT OF RETIREMENT

CUNA MUTUAL GROUP
The complicated feelings of the transition from pre-retirement to actual retirement are real and represent more than just financial uncertainties. What happens psychologically when the regular paychecks stop, time is in abundance and a new phase of life begins? For individuals who have worked their whole lives, their sense of self or value may be tied to their jobs or their businesses. Likewise, their interpersonal relationships or social networks may be depleted. For others, retirement is a stark reminder of mortality: the closing of a milestone chapter of life.

These concerns may have a serious negative effect: decision paralysis. When wrestling with anxiety or intense feelings about big issues like retirement, people often retreat from decisions. The default action may then become inaction, thereby exacerbating problems even further. For financial advisors, this means it’s time to identify and better understand some of the vital (and easily overlooked) financial and psychological impacts of retirement. With an understanding of these realities, advisors can share insights and expertise that ease clients’ fears, help them cope with complex feelings and, ultimately, guide them to and through appropriate actions.

The traditional pension plan that supported many individuals in retirement has, for most Americans, disappeared. A prolonged period of very low interest rates makes income generation on a fixed retirement portfolio extremely difficult.

Understanding the Emotional Effect

If you picture a carefree retiree walking on a beach or enjoying recreational activities happy and in good health, you might think life couldn’t get much better.

Yet, carefree and confident seniors represent an ideal of retirement far from reality for most. Instead of golden beaches and optimism, the reality is that many people have mixed emotions and anxiety about retirement. Others are less confident and more financially vulnerable than these idealized images suggest.

Advisors must recognize and understand the complex emotions and anxiety often felt by individuals approaching retirement.
Where Do Consumers’ Feelings About Retirement Come From?

Popular culture often portrays retirement as the highly anticipated capstone event of people’s lives—a time after a long career where they finally have the freedom to pursue hobbies, spend time with family or travel. But all too often, as the reality of the event draws near, a mix of personal and financial factors causes some to have a foreboding feeling about retirement.

**FINANCIAL CONFIDENCE**

Data obtained from the 2020 Employee Benefit Research Institute (EBRI): Retirement Confidence Survey shows many working individuals feel financially uncertain about their retirements:

- **33%** are not confident in their ability to live comfortably in retirement
- **37%** are not confident they will have enough money to take care of medical expenses during retirement
- **48%** have actually tried to calculate how much money they will need in retirement
- **69%** say their non-mortgage debt has negatively impacted their ability to save for retirement

**68% of workplace plan participants prefer some guidance from a professional.**

Not surprisingly, those who have a workplace retirement plan experience higher levels of confidence, with 8 in 10 saying they’ll rely on their defined contribution plan as a source of income in retirement.
CUNA Mutual Group’s Chief Market Strategist, Scott Knapp, points out the changes to the way we fund retirement as having a significant impact on the insecurity many Americans feel about it. With the passage of the Employee Retirement Income and Security Act of 1974 (ERISA) and the widespread adoption of 401(k) and 403(b) retirement plans, there has been a massive shift from defined benefit pension plans, or traditional pensions, to defined contribution retirement plans. Indeed, the traditional pension is rare.

“Today, the risk and responsibility are borne by the individual,” said Knapp. “This used to be borne by the employer.”

Throughout this shift toward individual responsibility for retirement, employers and the financial industry have invested heavily in financial education. In general, workers say they’re satisfied with the educational materials they receive. When digging deeper, however, 8 in 10 workers indicated that they want education about how to manage competing financial priorities or how to convert savings into income in retirement.

This disconnect might stem from a tendency by those in the financial industry to use complex concepts, insider jargon and an overabundance of information that may leave investors more confused rather than more informed.

Planning for retirement can be relatively simple, yet the industry tends to shroud it in nuance and complexity. As a result, people may put off investing decisions because they’re too complicated or unnerving.

Retirement savings plans that include auto-enrollment through an employer and qualified default investments for those unable or unwilling to choose investment instruments may be a key to starting—and building—workable retirement savings balances.
FINANCIAL TRANSITIONS

Switching from accumulating to drawing down savings can be unnerving. For most people, having a steady paycheck and regularly saving feels very different from living off a nest egg and tapping retirement savings to cover day-to-day expenses.

Advisors can help clients take the first step of revising their investment strategies to reflect this transition. For past generations, this has meant transitioning investments into less risky, income-generating holdings like bonds or CDs. But today, staying the market is now a commonplace investment strategy. But without any guarantees, even conservative strategies bring a new level of client concern and stress, especially during volatile markets.

It wasn’t always this way. CUNA Mutual Group Chief Economist Steven Rick refers to the stock market in the 1980s and 1990s as the “Great Moderation,” a time when markets seemed to move steadily up. But after 2008-09, many investors were jaded by the rapid market downturn and significant losses. A decade later, feelings of skepticism and anxiety over significant market drops may have opened those old wounds.

Without help from an advisor, many less-sophisticated investors are searching for information online. “Retirees read a lot of misinformation in the media that undermines their confidence in traditional investments. This can really ramp up fear and uncertainty,” says Rick.

ARE LOW INTEREST RATES HERE TO STAY?

After reaching a peak in 1982, interest rates have declined steadily, and only recently began to slowly inch up. When the COVID-19 pandemic hit, however, the Federal Reserve cut its benchmark federal funds rate to nearly 0%. CUNA Mutual Group Chief Economist Steven Rick suggests that residual effects of the pandemic combined with structural changes to the economy that impact corporate earnings and interest rates may mean rates will stay lower for much longer than expected.

Aside from the immediate impact of the pandemic, several factors contribute to this decline, notes Rick. While technology initially led to big worker productivity gains, today’s economy isn’t seeing the same advancements. In addition, the Baby Boomers are beginning to exit the workforce faster than other workers are entering. So, with lower productivity per worker and the number of workers growing at a slower rate, the economy cannot grow as quickly. These structural changes in the global economy set the stage for lower-than historical-average returns on financial instruments. Low interest rates are likely here for a while.
EMOTIONAL AND LIFESTYLE TRANSITIONS

Retirement can generate a complex web of emotions. A failure or lack of desire to plan for what comes after retirement may backfire.

For many, personal identity or sense of self-worth was tied to work, and there can be a need to create a new identity and redefine relationships.

An immediate issue is defining one’s new retirement lifestyle. That lifestyle can be impacted by many things—assets, income/expenses, general health and fitness, changing spousal relationships, family relationships, locations and other factors. Regardless, many of today’s retirees no longer view the transition to retirement as simply “quitting work.” Instead, it’s stepping into a new phase, redefining oneself and determining what to do with newfound time.

Relationships that were important throughout a career may be hard to maintain when coworkers no longer see each other on a consistent basis. On the flip side, relationships at home may change as spouses identify new roles or one may enter retirement while the other continues to work.

Further, the mere act of moving from work into retirement may lead to sadness, anxiety or even depression. What might create significant anxiety for seniors? Rising healthcare costs, financial stress, estate planning, isolation, health issues, or even the responsibilities of caregiving to others can have an impact on depression. But, like many other mental illnesses, depression can be diagnosed and treated.
New Retirement Risks

Many retirees face the harsh reality of simply not having saved enough. More and more may find it necessary to extend work beyond retirement age.

One contributing factor is that some individuals approaching retirement are the “sandwich generation,” meaning they simultaneously care for aging parents while supporting their own children. These added pressures may result in spending less time and having fewer resources put toward their own retirement preparation.

Another factor is longevity. While we all look to live for as long as we can in good health, longevity poses a significant financial risk for many. According to the Centers for Disease Control (CDC), the average life expectancy of today’s 65-year-olds is 83.1 years for men and 85.7 for women. As those numbers continue to grow, so do the risks of running out of money and needing costly long term care.

10 RISKS TO RETIREMENT INCOME

- **Market Risks**: The markets can be volatile; relying on them for retirement income is risky.
- **Interest Rate Risk**: Locking in low rates on retirement savings prohibits growth; bond values are at risk if rates rise.
- **Sequence of Returns Risk**: A few years of bad returns early in retirement can have a significant negative impact.
- **Withdrawal Rate Risk**: Taking regular withdrawals at too high an amount can be unsustainable.
- **Allocation Risk**: Seeking safety by avoiding more aggressive investments can lead to missing potential growth opportunities.
- **Inflation Risk**: Inflation reduces the purchasing power of savings.
- **Longevity Risk**: The risk of outliving one’s assets.
- **Health Care Risk**: Living longer may mean more medical bills or long-term care expenses.
- **Taxation Risk**: Withdrawing funds can have tax implications, so strategies need to be employed to make the most of tax advantages and avoid penalties.
- **Legacy Risk**: Make sure intentions are met by understanding the rules of inheritance.
Additionally, through no fault of their own, some retirees may also simply retire at the wrong time in terms of market performance. Markets tend to fluctuate, and those who retire just as the market goes into a downturn may find their losses magnified. In other cases, bad timing may also involve a spike in inflation during the early years of retirement, as this scenario reduces the purchasing power of those on a fixed income. Unforeseen expenses can also impact retirement success. The expense many retirees worry about most is health care. While inflation across the broader economy is low, medical costs are one area where inflation is substantially higher.

### BAD TIMING RISK: 3 COMMON SITUATIONS

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*Hypothetical illustration based on $500,000 initial portfolio balance with annual 7% withdrawals increasing 3% annually. Investment return and principal value will fluctuate with market conditions so that upon redemption, the investment, including the principal value, may be more or less than originally invested. Illustration does not account for any fees, charges, or taxes.

It is estimated that the average 65-year-old couple will need $12,052 saved annually just for medical expenses. That annual amount will more than triple to an estimated $37,839 over the next twenty years. 

This is over and above medical expenses that are covered by insurance. This issue is complex: Medicare doesn’t kick in until age 65, premiums and copays can be considerable, and some treatments and supportive care options may not be covered. For some, taxes can represent another intangible risk because they’re hard to predict and tax policies regularly change.
The science of behavioral economics has identified many factors underlying the uncertainties and challenges individuals face in planning for retirement. While having a financial plan is a contributing factor to success, plans only work when they’re followed. Advisors can play a key role in countering behaviors that can undermine success.

A concerning risky behavior among seniors is alcohol abuse, with one study finding that approximately one in 10 older Americans binge drink. Alcohol misuse could be due to older adults seeing retirement as a stressor, while for other retirees, alcohol use equates to more leisure time, fewer responsibilities and positive enjoyment.

Other risky behaviors may include prescription drug abuse or problem gambling due to social isolation or the desire to escape everyday stressors. Plus, psychological disorders, depression, anxiety or dementia for instance, may exacerbate these behaviors.
Positive behaviors—being physically active, eating a balanced diet, keeping a healthy weight—along with moderate alcohol intake and not smoking, help maintain and enhance good health.

When advisors take a “coaching” approach with older clients—asking them questions to help them define what they need—it nurtures a sense of resiliency. Clients feel that they can weather the ups and downs to come and that they have the freedom to follow their own paths. In a sense, they end up making the rules that create the plan. The advisor can then suggest the tools needed to meet those rules.

The challenges of transitioning to a satisfying retirement are real and significant. As an advisor, it’s vital to effectively connect with clients prior to and during this important time. Working together, asking questions and creating plans are essential steps in helping clients reduce their anxiety and achieve the security they desire. While the focus may be financial, advisors can serve a larger holistic purpose and have a meaningful positive impact on clients and their families by building strong, long-term relationships.
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