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The Future of Retirement Income

Financial advisors need a new business model for delivering clients' monthly paychecks.

The lingering economic crisis has caused many clients to rethink retirement -- putting fundamentals like "How?" "What?" and "When?" into high relief.

As George Walper, president of the strategic consulting firm Spectrem Group, bluntly frames it: "The whole planning of retirement changed in the last 12 months."

Not surprisingly, according to survey after survey, anxious investors are clamoring for retirement planning guidance. At the same time, forward-thinking financial services companies, in a huge top-down initiative, are trying to create new products and processes to help them. Strangely out of the loop in all of this: the financial advisor.

A research study this past summer by Cerulli Associates found advisors continue to exhibit "ambivalence" toward retirement income planning. "We've been almost surprised by the lack of change. It's odd," observes Bing Waldert, a Cerulli director. "What's interesting is even in spite of the market, that same ambivalence came through."

The topmost obstacles cited by advisors to providing retirement income support: lack of consumer awareness and the fact that it is time-consuming.

Meanwhile, a survey from Spectrem Group says many financial advisors are unprepared for retirement planning and dated in their knowledge of products and strategies -- even though more than 60 percent expect retirement income planning to be a huge part of their business in years ahead.

Why the disconnect?

"It's just not what advisors have been trained to do. Yes, most are unprepared," notes Francois Gadenne, executive director of the Retirement Income Industry Association. "The mission is no longer to sell hope and things that could be, but to deliver a floor, then expose to the upside. Because your client is moving from an investment focus to a retirement focus, your business model has now changed. Your job is now not just to collect the AUM's and have a nice day. Your job is to deliver a monthly check. It's a completely different business model -- and not something you adjust to lightly."

There are indicators -- big and small -- that suggest the landscape may be changing. At its annual meeting in October, for example, RIIA launched a new professional designation: Retirement Management Analyst. The first cohort of candidates has just been selected. The takeaway from a recent RIIA webinar on Brightwork Partners' retirement income research? "Retirement income is maturing as a practice focus. It's not a contrived fad."

And while research conclusions on the topic of retirement income planning may diverge at points, they do converge on one key issue: the significant market opportunity that the mass affluent represent.

"This is a real challenge for the industry -- and a real opportunity. It's a big chunk of the population and it's where retirement planning will play big. If you really think about it, the financial life of regular people who have worked their entire lives is much more complex than it was in the past and it is approaching that of a very wealthy person," according to Sean Cunniff, research director for The Tower Group. "Insurance, health care -- you're dealing with all these issues. It really is a complex problem and it becomes more so in the retirement income phase." And, in what could be a harbinger of things to come, Merrill Lynch Wealth Management in late October introduced to its 15,000-plus advisors a retirement income platform process. Developed in conjunction with independent consultants and the firm's "best of best" retirement planning advisors, the process starts with the client's risk-weighted retirement investment strategy, continues with an annual income plan that includes drawdowns, and finishes with a cash management component.

The latter, called My Retirement Income, connects a client's Merrill Lynch brokerage account to his Bank of America checking account.

Aimee DeCamillo, head of personal retirement for the firm, said the platform will evolve over time. Notably, Merrill Lynch corporate has never before dispensed specific advice and guidance to advisors related to the drawdown of a retirement asset.

"Retirement needs have changed, frankly. The industry is evolving, client need is evolving. And you see advisors in different stages. Some have been way out in front of this for many years now and those are the ones we turn to to create a best-of-best approach to bring to our core advisor base," she said. "But there's always more advanced thinking we can do."

A Changing Picture

Advisors don't need a poll to tell them retirement expectations have changed in the last 12 to 14 months.

But consider these findings:

• SRI Consulting Business Intelligence in February returned to households it had surveyed between April and August 2008 and learned that one-half of all households' expectations for retirement had changed since September 2008.

Thirty-seven percent said they had lower expectations for how they would live in retirement, and nearly 25 percent said retirement was no longer an option for the foreseeable future. "How do you say all this without getting really depressed? I guess the good side is that those expectations for retirement were based on antiquated ideas anyway," notes Larry Cohen, SRI's director of Consumer Financial Decisions. "This will accelerate the new idea of retirement as a whole life stage."

• Sun Life Financial's Unretirement Index reports that the most popular reason cited by American workers for why they would continue to work past age 67 shifted in December from "to stay mentally engaged" to "earn enough money to live well."

• And Merrill Lynch Wealth Management's "Affluent Insights Quarterly" survey, released in October, found that 50 percent of respondents felt that their current retirement plan was an area of "high" concern. Their foremost worry: the risk associated with rising health care costs.
If nothing else, the market meltdown has put the spotlight on risk -- and it is emerging as a key driver as advisors consider their clients' retirement needs, particularly as it relates to the mass affluent.

"The broader overarching question for the industry is: Has risk tolerance fundamentally changed? This is one of those places where you will start to see advisors dial it back a bit," says Waldert. Also in play: a distrust by advisors of packaged products.

"They want to see through to what the risk is. If it's an annuity with a living benefit, they need to understand that underlying risk," he adds. "The desire for due diligence reaches a whole new level." And, anecdotally, Waldert has heard from broker-dealers and asset managers who have reconfigured their risk tolerance profiling to "make it more real, to put it in more absolute terms." And nowhere is the risk more pronounced than it is for the mass affluent, defined by Cerulli as people with $1 million to $5 million in net worth. As Waldert puts it: "It's the mass affluent who are in for the biggest surprise. Everything says to you that this is the at-risk retirement income population."

In a Spectrem Group survey last December, 90 percent of investors with $500,000 and above in net worth, not including their house, called the economic crisis the biggest financial event of their lifetime.

Spectrem's Walper says the fallout includes hugely impacted baby boomers who won't have the time to recover their assets as fully as younger investors, as well as advisor satisfaction levels that continue to drop. And even as the market rebounds, Walper says investors for the next five to seven years will be more conservative and far more involved in creating their financial blueprint.

"Advisors who are hoping things will be better if the Dow is over whatever are sorely mistaken," he adds. "If the market gets up to 12,000 it will feel good but investors won't be saying: 'Gee, this is all behind me.' This has been a shock that will last many, many years. Advisors have to realize that their business model has to change."

Lynne Ford, head of retail retirement at Wells Fargo, says she is beginning to see a shift in advisor thinking. As examples, the four or five informational retirement income "summits" the firm has staged for advisors in the last year have been "completely oversubscribed" and Ford says many fee-based advisors who previously wouldn't get near an annuity are now asking for education on how a guaranteed income stream fits into an overall portfolio.

"I'm really beginning to see the tide turn in terms of advisors understanding the critical importance and the heavy weight of creating, as an advisor, an income strategy for you the client in retirement," she says. "We have years of education to get out to advisors on the whole income story: How do you as an advisor build that portfolio to generate income? This is what asset allocation was in the '90s. We're going to be spending the next three to five years with an intensive focus around income planning."

While innovation has started in the product arena, Ford believes process is the end game. "We need to be able to show a monthly paycheck on our statements so clients can see: Here's my monthly paycheck. Here's my target portfolio. And here's the cash that's coming out of that. We need to do a better job at that."

A Look Ahead

Retirement income planning is a diverse, complex area and going forward, advisors will require significant guidance and support.

As Cunniff observes: "One huge problem is not enough advisors are capable of offering true retirement advice. It's really hard. If you think about it, the skill set in a lot of advisor channels is still a sales skill set in a lot of ways."

To support a broad audience like the mass affluent, Cunniff says advisors are going to have to become relationship managers supported by what he calls "centers of excellence:" call centers, strategic partners and subject experts at the home office.

"If you're an advisor, particularly if you're a successful advisor, your thinking right now is: 'If it ain't broke, I've got nothing to fix.'

"But just because advisors don't make a change in their business model doesn't mean the world isn't changing around them," Cunniff adds. "I frankly think you're starting to see a handful of advisors pick this up. It's an opportunity for advisors to set themselves apart."

Research from Brightwork Partners suggests that retirement income planning at the moment is more of a rollover opportunity for advisors --which then can lead to a retirement planning conversation.

"This is a great business development opportunity for advisors on the make," noted Brightwork's Merl Baker, "They control the discussion in this channel."

Elvin Turner, managing director of Turner Consulting, said it may be unreasonable -- in a year that hasso tested advisors and clients -- to expect advisors to embrace change, even change that is so clearly in the forecast.

"Right now the name of the game for advisors is to survive until next year. It's not been a good year and people are short-term focused," he said. "I don't think you can judge the opportunity of the marketplace based on people's reactions right now."

Still, he added, every trend points to a wave of retirees -- despite many advisors' seeming ambivalence.

"The Romans were ambivalent about the Huns. It's coming," Turner noted. "There's nothing anybody can do to stop that. The issue is how quickly do you adjust?"