PACIFIC LIFE insights

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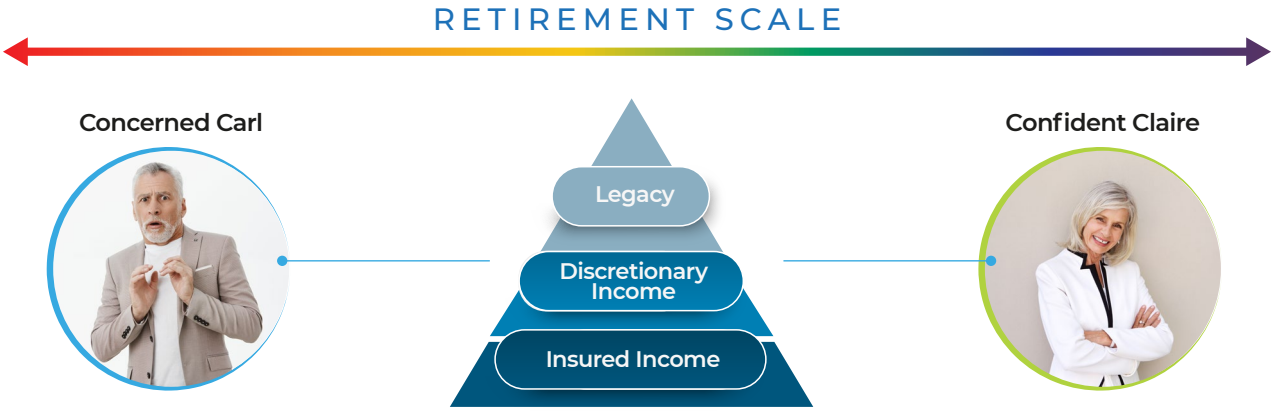
CREATING RETIREMENT INCOME: ARE YOUR CLIENTS CONFIDENT OR CONCERNED?

Assets saved during the client's working years now are used for the daunting task of creating a predictable paycheck. How can you best prepare them?

Understanding your clients' investing biases may help you provide advice they're more likely to stick to for the long term.

Retirement is a significant life change for clients. Ideally, your clients have saved for many years, so they will have a nest egg sufficient to support a comfortable lifestyle. But when the time comes to turn those savings into income, inherent biases can affect what choices work for each client. Understanding those biases can help you design an effective retirement-income plan that aligns with each client's behavioral profile. Remember: In retirement, the consequences of a financial misstep can be harder to correct or overcome.

The Retirement Client Spectrum



Consider These Two Client Types: Concerned Carl and Confident Claire. A careful review of each client's financial information shows that their balance sheets and financial circumstances are identical. Both also want the same type of retirement lifestyle. So, will the same plan work for both? Maybe. But very likely not. Client biases and conditioning can affect how they will feel about—and whether they will follow—a retirement-income plan.

How Can You Help Clients Create Plans That Fit?

A first step could be to help a client identify his or her cognitive biases and determine how those biases might steer them toward a particular plan. As an example, Concerned Carl may allow availability (also known as recency) bias and loss aversion convince him that a market downturn is permanent. Carl may think the market will never recover, so all assets should be invested in safe choices where no loss can occur. This increases the risk that inflation will negatively impact his lifestyle later in retirement. Carl may benefit from both understanding his biases and having sufficient guaranteed income to cover his basic monthly expenses.

On the other hand, Confident Claire may view market volatility as simply part of investing. After all, she has always done reasonably well over time. Her overconfidence may allow her to forget that she has certain expenses due every month. If she relies too much on her invested funds to cover her essential monthly expenses, sequence of returns risk may create permanent losses in her account.

Claire may benefit from understanding that applying a more conservative approach, such as protected income, to cover monthly expenses can reduce sequence of returns risk, allow her to invest for more growth, and help with portfolio sustainability.

What Are Some Helpful Ways to Discuss Biases With Clients?

How a conversation is framed can help a client understand and manage concerns. For example: Asking Concerned Carl "How would you invest differently if, for a fee, you had guaranteed income that will cover your monthly expenses?" can help reduce his uneasiness about covering monthly bills. Another question for Carl might be, "How would you invest if you knew your downside risk was protected?" If Concerned Carl knows he can limit his risk of loss, he may be more willing to invest for growth and potentially reduce his inflation risk.

A good question for Confident Claire might be, "Would you be willing to pay an additional fee for options that allow you to stay invested in the market, but provide you income protection?"

For Claire, the idea that she can benefit from market upside with reduced risk of market volatility may be a solution to make sure her essential monthly expenses are covered.

What Should a Client Consider When Building an Income Plan?

A successful retirement-income plan should be easy to follow and provide income that supports the retiree's lifestyle. Some questions to consider include:

- **Are essential expenses covered?** Each client can determine what expenses are essential. If an expense is essential, then the retirement-income plan should provide guaranteed or protected income to cover it. The level of protection needed will be affected by the client's inherent biases and assets.
- **Is discretionary income managed appropriately?** Once a client determines essential income, the discussion can shift to discretionary income. Again, a client's biases may help lead to the formulation of an appropriate plan. A cautious client may need additional principal and inflation protection to remain invested for growth. A confident client may be comfortable with a balanced investment portfolio to help manage sequence of returns risk.
- **Will the client be able to stick to the plan?** The best plans are built to suit each unique client. When determining an income plan, you must consider whether the client will be able to stick to it in up and down markets as well as in good and bad economic environments. A client with a plan that accounts for personal biases is most likely to be followed over the long term.

Next Steps

Information is only beneficial if it is used. This is a perfect time to contact your clients who are in the retirement-planning stage and determine if they are "concerned" or "confident." Start the conversation and review whether or not adjustments should be made today!

Additional Resources and Links

Common Investor Behaviors that Hurt Investments - Pfau

Does Your Mindset Affect How You Make Retirement Income Decisions? - Pfau

Female Savers: Keep Their Retirements on Track with Behavioral Finance

For more information about retirement planning, please contact our Retirement Strategies Group at RSG@PacificLife.com or (800) 722-2333, ext. 3939.
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