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Evensky: New Choice May Preserve Portfolios, Lower Cash Reserve Needs

APRIL 18, 2012 • KAREN DEMASTERS

By Karen DeMasters

A new type of reverse mortgage may be one key to enabling retirees to preserve portfolios and keep less cash in reserve, says Harold Evensky, a financial planner and nationally recognized expert on retirement issues.

The new federally insured Home Equity Conversion Mortgage, or HECM Saver, allows holders to establish a credit line but not draw on it unless the funds are needed. Payments on interest can be made when the holder chooses to do so or they can be deferred until the home is sold.

Unlike traditional reverse mortgages that provide a lump sum payment, the HECM can provide cash when needed, such as when the markets are down. This prevents the stockholder from having to sell stocks at a loss to get cash. The HECM can then be paid back when the markets are back up, Evensky says, which preserves the portfolio.

The new reverse mortgage is one factor changing the face of retirement planning, says Evensky of Evensky & Katz, a wealth management firm in Coral Gables, Fla. Evensky recently presented his view of changes in retirement planning at a webinar, The Future Ain't What It Used to Be: The Ultimate Guide to Retirement Planning for Baby Boomers.

Each day 10,000 baby boomers turn 65 and that will continue for the next 19 years, which makes the subject of retirement planning crucial, says Evensky, and that planning needs to reflect some changes.

"We are studying this (HECM Savers) now, but I'm reasonably positive it will become an important part of our planning in the future," Evensky says.
The use of HECM Savers can reduce the cash reserve that Evensky would recommend a retiree hold from two years of living expenses to six months because there is the HECM money to draw on if needed.

A HECM is also substantially less expensive than reverse mortgages have been, thereby providing a ready pool of capital to tap into when needed at a relatively low cost, he says.

"When markets regain their strength, the mortgage can be paid back," Evensky adds. "Our studies indicate this will significantly increase the survivability of the portfolio in retirement."

Another factor changing retirement planning is the increased use of immediate annuities, Evensky says. An immediate annuity

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A mistake that financial planners can make in retirement planning is trying to maximize returns. Instead, planners should be maximizing the probability that their clients will achieve their financial goals. Roughly half of Evensky and Katz's clients are in retirement and another 20% are approaching it, so planning correctly is vitally important.

Conventional wisdom says people spend less as they grow older, mostly because of the constraints of poor health. However, Evensky says, in the future people will live longer but not necessarily get sicker until they are near death, so planners should not make the assumption clients will be spending less.

"When you retire you have more time, and time costs money," he says.

Retirement planning should be done in a three-dimensional, rather than a two-dimensional, world, where the factors to be considered are returns, risks and taxes and expenses. Evensky advises hiring money managers who are extremely tax efficient.

The flip side of not saving and investing correctly is under spending and having money left at the end of life. "Your clients should not be so conservative that they deny themselves the lifestyle they will enjoy," he says.

Evensky also believes in what he calls a five-year mantra, since five years is roughly the equivalent of an economic cycle.

"Simply put, we don't believe anyone should be investing funds they may need in the next five years. Otherwise, they may have to sell at the wrong time," he says. "We replenish the cash-flow reserve as we manage the investment portfolio.

"If someone has $1,000,000 in savings and indicates they want to buy a second home for $100,000 three years from now, we would suggest they carve out $100,000 and put it in cash-flow reserve comprised of short-term bonds and cash and invest the remaining $900,000," Evensky explains.

On another aspect of financial planning, Evensky is a firm believer in account aggregation so an advisor can see all assets held by a client, including 401(k) plans and assets that might be handled by a competitor.

"Since the advent of account aggregation, I've been a big believer that it needs to be an integral part of what we do as practitioners because our job is to work with our clients holistically," he says.

Also, the software lets the advisor see how other managers are handling some of the assets and may provide the advisor with an opportunity to show a client he could handle the assets better and therefore gain business, Evensky says.

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