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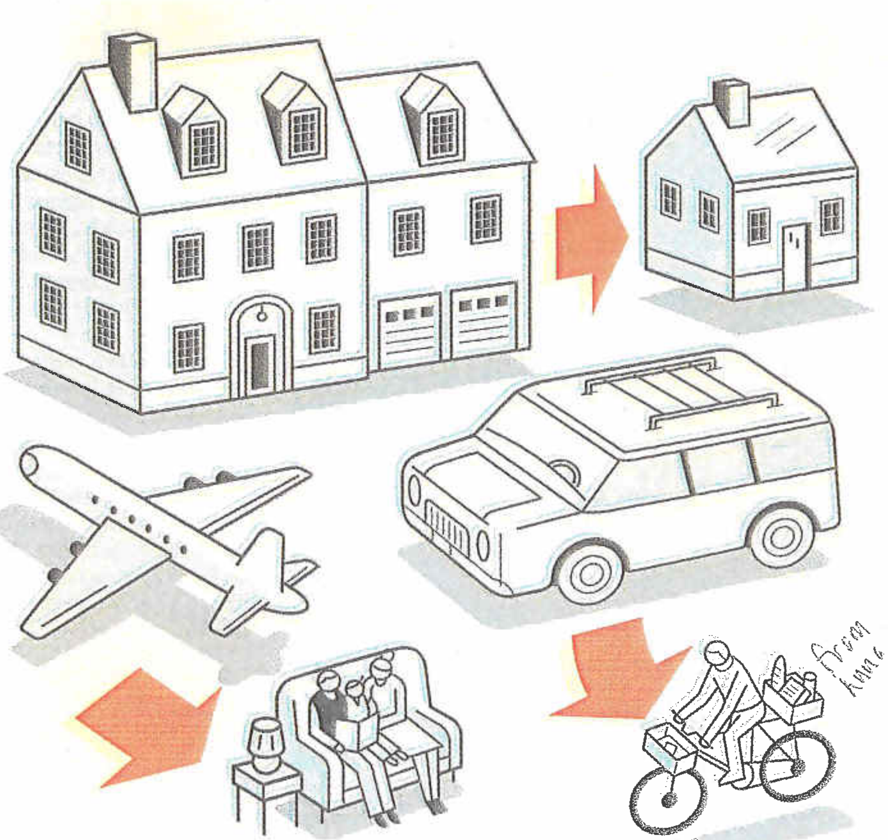

Low-Cost Retirement

Your later years can be golden without being gold-plated. Most retirees are frugal by necessity—but no less happy

By Paul J. Lim and Emily Brandon

Having spent much of his career helping others with their finances, Don Peterson knew the importance of saving as much as possible before retiring. But when the 82-year-old former stockbroker left the workforce in 1988, he realized that retirement isn't just about money.

In his case, Peterson retired a bit sooner than he had planned—and with less money in the bank. But that was partly due to bad timing. Shortly after a few of his investments went bad in the 1987 market crash, his wife, Bobbie, decided it was time to retire from her career as a hospital laboratory administrator. And soon after that, one of the couple's daughters asked them to move from Eau Claire, Wis., to Nashville to be closer to her and the grandkids.

So even though the Petersons had less than $100,000 in their accounts and just one pension between them—hers, which paid out only around $500 a month—they quit their 9-to-5 life and shuffled off to Music City.

Their challenge was one that millions of older Americans are faced with every day: finding a way to lead a comfortable—and, yes, happy—retirement with only a modest nest egg.

For the vast majority of today's older workers, this is the reality of retiring in America. While financial planners and retirement experts debate how many millions of dollars families should save—and how to invest that money to make it last—most households are retiring on meager sums. Nearly two thirds of workers 55 and older have less than $100,000 saved for their golden years, according to a recent study by the Employee Benefit Research Institute. And 56 percent of those workers who are already retired have less than $50,000 to last them for the rest of their life.

from Anne

Happy campers. Yet somehow, "people often find a way to get by," says Gayle Oboy, a financial planner in Marion, Ohio, who works with many middle- and working-class clients. "They adjust. They find ways to cut back but still be content." In fact, studies show that more than 60 percent of seniors find retirement "very satisfying." Most also say retirement is more satisfying than their working careers were.

Sometimes, it does take a bit of creativity. The Petersons, for instance, leveraged two assets they had—time and a love of animals—and started a pet-sitting business after "retiring" to Nashville. It wasn't a glamorous job—"my wife jokingly says I have a Ph.D. in cat litter," Don Peterson says. But the modest income they derived from dog-

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and cat-sitting "made all the difference in the world," he says. "It helped pay for the groceries and helped cover property taxes." It also gave the couple the freedom to retire on their own terms.

Those who don't want to or can't work during retirement are starting to take advantage of another asset: their homes. Thanks to the run-up in home values during this decade, some retirees are starting to downsize to cheaper digs and using the remainder of their home equity to finance retirement, says Jean Setzfand, director of financial security for AARP. Others are choosing to relocate to less expensive parts of the country, which is what the Petersons did. "It's an insurance policy of sorts," Setzfand says.

What's more, a small but growing number of seniors are opting to supplement their retirement income through so-called reverse mortgages. By taking out this type of loan, you can receive a certain amount of your home equity in a lump sum, a line of credit, or monthly annuity payments for life—while still living in your home. And you don't have to repay the loan so long as you live in that house.

The catch is, when you die or move, the proceeds of the home sale will be used to repay the mortgage. And you have to be at least 62 and own a single-family residence to qualify for a government-insured loan. Because this involves the eventual sale of your home, Setzfand says, this strategy shouldn't be taken lightly. And keep in mind that like an annuity, the terms of the reverse mortgage will improve the longer you wait to take one out.

Of course, the simplest solution for some retirees is to find ways to limit spending—without sacrificing your retirement experience (checklist, Page 57).

Take Gary Hutson. After retiring in 2001 following two decades as a railroad union leader, the 65-year-old now spends his time in far less stressful circumstances. Hutson and his wife, Kathy, are both artists in Spokane, Wash., and they use their free time—and the serene backdrop of eastern Washington—to paint wildlife scenes, carve wooden and metal sculptures, and do bead work.

When the Hutsons aren't creating artwork, they find plenty of other low-cost activities. For example, "we love garage sale-ing," says Kathy. And they also take frequent trips to a cabin they inherited on Sacheen Lake, 45 miles away.

Lower expenses. The good news for cost-conscious retirees: "All the numbers show that you don't need the same amount of money in retirement as you needed before," says Alicia Munnell, head of the Center for Retirement Research at Boston College. Once you retire, you stop saving for retirement. Your taxes are often lower, since your income is likely to drop. "And you don't need to buy work clothes or take transportation to work," she says.

Workers making $40,000 to $90,000 a year need to replace about 75 percent to 80 percent of their preretirement income on average, according to a 2004 analysis by Georgia State University and the insurance giant Aon. So if you earned $40,000, you would need to generate only about $32,000 in annual income to live as comfortably in retirement as you did during your working career.

And for the current generation of retirees, Social Security still covers around a third to more than half that amount, depending on income. So if you earned $40,000, you may need to generate only about $11,600 a year on your own—or through a pension, if you have one—to maintain your standard of living in retirement.

OK, but what if you still fall short?

"The answer with the biggest payoff is employment," says Munnell. Not only does finding work boost your current income, but it also delays having to tap your personal resources. And the longer that you can keep money in tax-deferred accounts like 401(k)'s and IRAs, the better. Plus, by working a bit longer, says Rande Spiegelman, vice president for financial planning at the Schwab Center for Investment Research, you may be able to wait before drawing your Social Security benefits.

That's what Marlene Adams did. A decade ago, the Torrance, Calif., resident was all set for a traditional retirement when the utility company where she worked offered her a modest buyout package. Adams was then 55 and thinking of funding her retirement with private savings first, followed by early Social Security benefits.

But after talking to a financial planner, she took a temp job instead, and it eventually turned into a full-time position working in customer service for an air freight company. By doing so, Adams was able to hold off on taking Social Security until her full retirement age of 65 (that age has been pushed back to 67 for those born in 1960 and later). And that increased her Social Security payments

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ON THE JOB. Roy Walls earns spending money by working part time.

Making even a few thousand dollars a year can mean delaying tapping your savings or waiting longer to take Social Security.

from around $1,200 a month to $1,650. Now, after paying her rent, she still has about $500 left over each month—and that's not counting her personal savings. "I feel like I'm blessed," says Adams, who is now close to retiring for good.

To be sure, not everyone can find full-time work later in life as Adams did. In fact, many workers mistakenly assume they'll be able to keep working to cover any financial gaps. A recent EBRI survey found that most workers plan to retire at 65 or older. But in reality, nearly 2 in 3 Americans wind up leaving the workforce before they reach 65, often because of unexpected health problems or layoffs.

Spending money. But even if you can't work full time, small jobs can help. Just ask Roy Walls, another Southern Californian. Walls, a former equipment manager for an aerospace company, retired in 1999 at 62 with an early-retirement package. Between his pension and Social Security, he and his wife, Loretta, lead a relatively comfortable retirement. Still, Walls decided to take a part-time job as a crossing guard for a nearby school district. During the school year, Walls helps kids cross the streets near his home for about an hour and 15 minutes each morning and 45 minutes in the afternoon.

The job pays less than $5,000 a year. But that money helps cover the cost of dinners out and movies on the weekend, Walls says. And it allowed him to recently help a son out financially—without having to dip into his savings.

For those without pensions to fall back on, earning even a few thousand dollars a year can be the difference between outliving your money and your money outliving you. Academic research shows that you probably can't afford to withdraw more than 4 or 5 percent of your nest egg each year. That means if you saved $250,000, you could withdraw no more than $12,500 annually.

But what if you needed $17,500 a year—in addition to Social Security and other benefits—to maintain your lifestyle? Well, says Schwab's Spiegelman, instead of tapping 7 percent of your account, which might deplete it too quickly, why not get a part-time job paying $5,000? That way, you can keep your withdrawal rate at the safe 5 percent level and still meet your income needs.

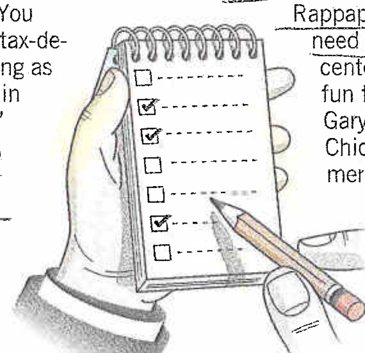
It's one of the ironies of retirement, says Spiegelman. Workers are taught that to retire well, they need to save huge amounts of money. "Yet small amounts of money can still make all the difference," he says. And that's what a new generation of retirees is finding out.

CHECKLIST

Six Sure Ways to Save

It takes a provident person to make a life's savings last for 20 or 30 years in retirement. Figuring out how much you can afford to spend so you won't outlive your money is "no easy thing," says Carol Nowka, a financial planner in Grand Island, Neb., who retired five years ago. You must set priorities, spend less than you take in, and plan for unexpected expenses. Many new retirees spend more at first than they did while working, according to Donald Haas, a financial gerontologist in Southfield, Mich. Then they get scared enough to cut the budget. Here's how to be a frugal retiree.

Spend money from taxable accounts first. "You want to hold your tax-deferred assets as long as you can and cash in your taxable first," says William Gale, director of the Retirement Security Project. Let your holdings in IRAs and other tax-advantaged accounts grow as long as possible before tapping them. When withdrawing money from those accounts, watch out for penalties.



Downsize your house. Your home is likely to be your biggest retirement expense. To cut costs, "you could downsize," says Anna Rappaport, a Chicago actuary and retirement planning consultant, or even share with somebody. Retirees can also move to an area with lower housing costs. Grace Wellwerts, president of Rocky Mountain Planning Group in Avon, Colo., where the median home price is $514,900, says clients often plan to "be here for 10 years and then move to a less expensive place to live." That could be Twin Lakes, Colo. It's only about 50 miles away, but a typical house there costs $235,000. Check out property and income tax rates before moving.

Slash transportation costs. Mary and Robert Atkinson downsized from two cars to one, giving their newer car to a daughter and keeping an older model on which insurance and taxes were lower. Some retirees stop driving completely. Joyce Dunn, 82, a retired accountant, gave up her car when she moved to downtown Chicago and opted for public transportation. "Downtown it's $200 just to park your car," she says. "Spending that type of money when you retire is not a good thing."

Find low-cost and free activities. While retirees have more leisure time, they haven't always saved enough for spending on leisure, says Rappaport. But entertainment need not be expensive. Senior centers often provide great fun for thrifty retirees. Jim Gary, 65, a retired banker in Chicago, enjoys free summer concerts in Millennium Park and other events. And don't forget to take advantage of senior discounts at movies, museums, and restaurants.

Compare prices. "Use the power of the Internet to do comparison shopping, especially for significant purchases," recommends James Knaus, a financial planner with Global Wealth Advisors in Troy, Mich. Many retirees can save money by eating out less often or finding early-bird specials and discount coupons. Look for deals in grocery shopping, too, and "buy food in bulk whenever possible or appropriate," says Haas.

Travel smart. Even retirees on a tight budget can travel. "If you are flexible in retirement," says Wellwerts, "there are deals . . . like last-minute travel." Or travel with other seniors and share the costs. Dunn has enjoyed Elderhostel trips with other retirees to New Zealand, Brazil, California, Texas, and the Rockies: "These wonderful trips go a week at a time, and it only costs you about $800. It's a good deal." *–E.B.*

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