Wealth Management
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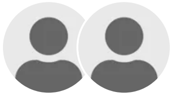
Longevity Is the Biggest Risk Facing Clients Today

What will your clients do if they outlive their financial assets?



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Trade tariffs with China. The Federal Reserve's stance on monetary policy. The slope of the yield curve. Geopolitical risk with North Korea and the Middle East, plus countless other issues are all concerning factors that impact the daily movement of financial markets. This volatility can cause your clients to lose sleep at night. However important and uncertain these issues may be, they pale in comparison to the biggest risk your clients face, outliving their money.

In 2020, the federal estate and gift tax exemption will be $11.58 million per person (or $23.16 million per married couple)—more than double the amount it was five years ago. On the other hand, if you have clients based in New York or other states with an estate tax, you need to take that tax into account when planning. For example, the New York gift tax remains at zero while the New York estate tax, which also reaches gifts made three years before death, approaches rates as high as 16%. With such a large federal exemption (that's scheduled to go back down to roughly half the amount in 2026) and such a potentially large disparity between the a state's estate tax and the gift tax (a 16% difference in New York), many of your clients will undoubtedly consider making substantial gifts during their lifetime rather than following the typical "they'll get it when I die" motto. It makes a lot of sense. Not only will your clients avoid the hefty New York (or other states') estate tax (assuming estate tax rates don't substantially decrease), but also, all the appreciation of assets gifted will occur outside of their estates. It seems like a win/win. They'll make gifts using a portion of their $23.16 million federal exemption incurring zero federal or state taxes, either to their heirs directly or, more likely, to trusts created for their heirs' benefit. But can your clients really afford to do this? How will they be protected from outliving the assets they have left after these gifts are made?

Aging Population

An aging population is putting strains on the intended legacy of passing down financial assets to support future generations. In addition, people are retiring earlier yet living longer. Health care costs continue to rise. The expectation to help fund the education of children and grandchildren to confront the ever-rising costs of college tuition continues. To maintain their desired standard of living after a substantial gift is made, your clients' remaining financial assets could be stretched. Moving from the accumulation phase of their financial life to the distribution phase can be unsettling. Given interest rates in the global bond market have been at or near historic lows for over a decade, in general, your clients have been forced to take on more risk by owning equities, when it might not typically fit their investment profile. We believe that the days when your clients could simply take "100 minus their age = their Equity/Fixed Income allocation" are gone and that a more thoughtful approach to risk management and total return is imperative to preserve and grow your clients' financial assets to continue building generational wealth.

According to an analysis by J.P. Morgan, there's a 90% chance that one spouse of a married couple will live into their 80s, and a 49% chance of one of them living into their 90s.

Think about that: if a client retires at age 65, chances are he and/or his spouse will live for another 20 years. Nearly 30% of his life could be without earning an income. Your clients are relying on their financial assets to fund their current cash flow needs yet trying to protect or create generational wealth and, at the same time, attempting to protect their heirs from paying substantial estate taxes. We must ask the question: Are your clients' financial assets positioned to achieve this triple objective?

Many assume holding cash is a way to protect against potentially volatile financial markets. This may be true in the short term, but over time, the "silent risk" of holding cash is that inflation and taxes will eat away its purchasing power.

Fixed income has proven to be the port in the storm when equity markets become volatile and provides an important level of diversification for a portfolio. However, with interest rates low, bonds can no longer be solely relied upon for income.

With the need for higher returns comes higher risk, but the scars of 2008, and even the fourth quarter of 2018, are still fresh on our minds, so taking on a higher allocation to stocks can be unsettling.

What are your clients to do?

Manage Risks

Stay focused on managing risk, but not just among stocks, bonds and cash. Diversify their cash flow streams. Investing in a mix of securities such as bonds, stocks, real estate investment trusts, master limited partnerships, preferred stocks, bank loans, emerging markets debt and high-yield bonds that are earning a higher yield than that of an investment-grade bond portfolio, yet are historically less volatile than a pure stock portfolio, is a prudent way for your clients to achieve their goals. Focusing on protecting the "quality" of the income stream by favoring companies with a strong balance sheet, business models that generate high levels of free cash flow and management teams committed to the dividend, is also of utmost importance.

Today's environment is markedly different than it was a generation ago. The financial world was turned upside down in 2008. Your clients are living longer, and their next-gen heirs may be relying on inheritance to provide for their growing families. In response, your clients need an active approach to their cash flow needs to live out their financial legacy.

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