WINTRUST
WEALTH MANAGEMENT

GUIDANCE

Planning Ahead for Retirement Healthcare Costs

According to healthcare cost projection software company, Healthview Services, a healthy 65-year-old couple retiring this year can expect to spend $322,000 (today's dollars) on Medicare premiums and dental insurance.

Add deductibles, copays, hearing, vision, and dental cost sharing, and that figure rises to $404,000. Future public policy decisions could increase these figures if the federal government implements reforms to Medicare—such as premium support—that would shift a greater share of the out-of-pocket burden to retirees. For most people, this means healthcare will be one of their largest expenditures in retirement.

Accordingly, pre-retirees would be well-served to carefully evaluate planning strategies that can help mitigate retirement healthcare costs. Retirement timing, and two tax-advantaged vehicles that can play a role—health savings accounts and Roth IRAs—are three areas to consider.

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Delayed Retirement

One approach to hedge healthcare costs is to work a bit longer and delay filing for Social Security. A delayed filing can boost retirement income significantly. Social Security's primary insurance amount rises by 8% for every 12 months of delay beyond full retirement age (currently 66) until age 70—a powerful boost to income that can help fund rising healthcare costs. Furthermore, the annual cost-of-living adjustment helps keep up with inflation, albeit at a slower pace than medical inflation. Working longer also means more net years of employer-subsidized health insurance (and fewer years of Medicare premiums and out-of-pocket costs). It also provides an opportunity to save more in a 401(k), perhaps utilizing catch-up contribution limits.

HSAs

Health Savings Accounts are available to workers in high-deductible health insurance plans. The accounts can be used to meet ongoing deductible and other out-of-pocket healthcare costs. This year, plans can have a maximum out-of-pocket cost of $6,550 for individuals and $13,100 for families. Some employers help offset those costs with contributions to the accounts; this year, combined employer-work contributions can be made up to a combined total of $3,400 for individuals and $6,750 for workers with family insurance coverage. After age 65, an HSA can be used to pay a variety of qualified medical expenses, including Medicare premiums (with the exception of Medigap premiums) or long-term care premiums. Details can be found in IRS publication 969. The tax benefits associated with HSAs are compelling. Contributions are tax-deductible, investment growth and interest are tax-exempt, and withdrawals spent on qualified medical expenses also are tax-free. Note, however, that funds withdrawn for nonmedical expenses are taxed at the account holder's marginal tax rate; if before age 65, the funds are subject to an additional 20% penalty. Further, HSAs do not have required minimum distribution requirements, and they are portable as they are individually owned and not tied to employers. The triple tax benefit increases buying power, especially when compared with the benefit

RETIREMENT HEALTHCARE COSTS

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of drawing down from a 401(k), which is subject to ordinary income tax on contributions and investment gains.

High-income retirees can enjoy another tax benefit from HSAs in that qualified withdrawals are not reported as income, which means they are not counted in the formula that determines whether you must pay high-income surcharges on Medicare Part B or D premiums. One caveat: it is important to carefully navigate the interaction of HSAs and Medicare during the transition period away from workplace insurance. The key issue is that HSAs can only be used alongside qualified high-deductible health insurance plans, and Medicare does not qualify as a high-deductible plan. That means that if a worker or a spouse covered on the employer's plan signs up for Medicare coverage, the worker must stop contributing to the HSA, although withdrawals can continue.

While most HSAs are not structured to be strong as both spending and investing accounts, many experts think health savings accounts will evolve into a platform for long-term saving to meet retirement healthcare costs.

HSAs have been around only since 2003, however, and thus far long-term investing has taken a back seat to usage of the accounts to meet current expenses. To wit, 96% have their funds in cash, according to research by the Employee Benefit Research Institute. A recent Morningstar study further noted that 10 of the most popular HSA plans offer mediocre and high-cost investment options. And just one of the plans was found to be compelling for use as both a spending vehicle and an investment vehicle.

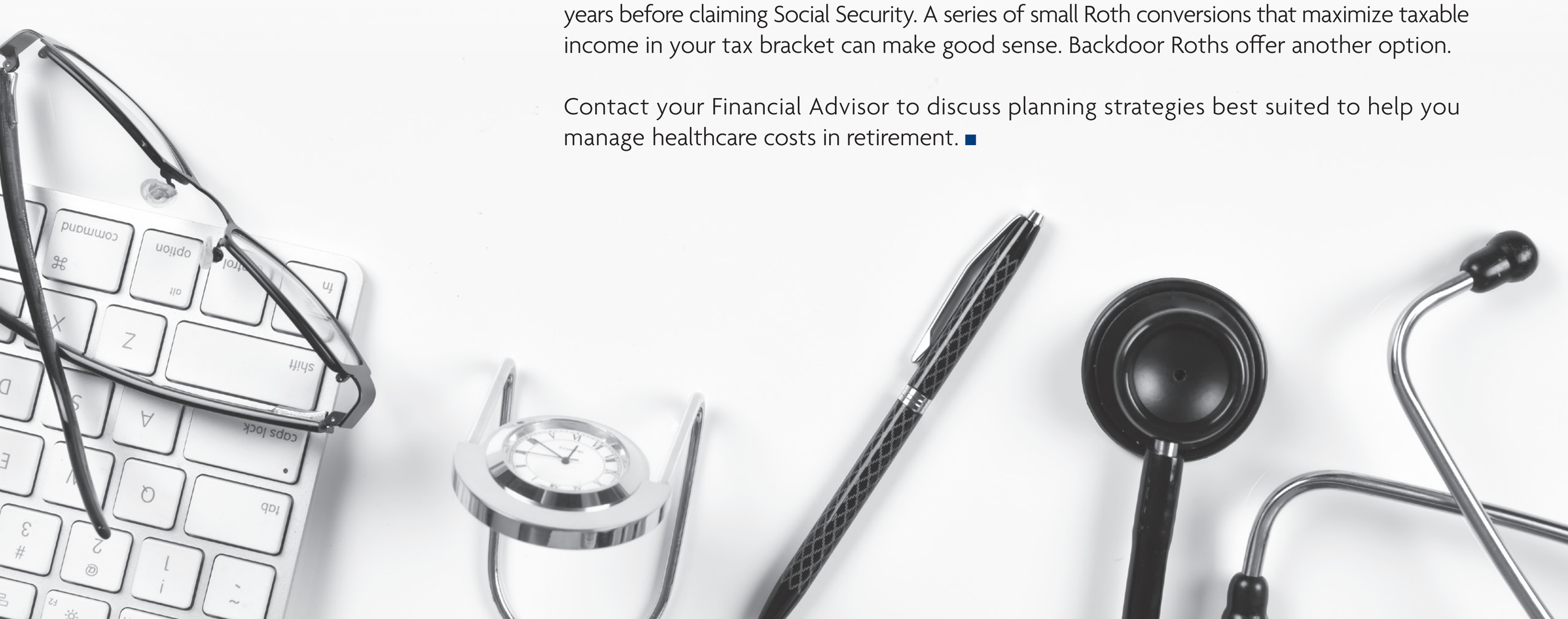
While most HSAs are not structured to be strong as both spending and investing accounts, many experts think health savings accounts will evolve into a platform for long-term saving to meet retirement healthcare costs. If you are eligible for an HSA, the right plan can be a powerful tax-advantaged vehicle.

Roth IRAs

Finally, if you are not eligible for an HSA, investing in a Roth IRA—or doing a Roth conversion—can provide a second-best option. Much will depend, of course, on the specifics of your tax situation. Roths get the income tax out of the way upfront, allowing tax-free withdrawal of contributions and investment returns down the road. Roths also are not subject to required minimum distributions (during the lifetime of the owner), which means you can preserve assets to meet healthcare expenses.

Be mindful that conversions can bring some undesirable near-term tax consequences. To avoid these, consider conversions in low-marginal-income tax bracket years, especially in the years before claiming Social Security. A series of small Roth conversions that maximize taxable income in your tax bracket can make good sense. Backdoor Roths offer another option.

Contact your Financial Advisor to discuss planning strategies best suited to help you manage healthcare costs in retirement. ■



In-Retirement Withdrawal Rates

The withdrawal rate from a portfolio can make or break a retirement plan. Yet as important as withdrawal rates are, the ideal withdrawal rate for any given retiree is necessarily an educated guess, based on what is known about market history. As is the case with asset allocation, the optimal withdrawal rate will be apparent only in hindsight. Reassuringly, there is a broad consensus in the retirement-planning community about many withdrawal-rate matters. Following is a roundup of some of the widely agreed-upon points.

Much of the research on retirement withdrawal rates centers on the notion that retirees would like their incomes to be stable in retirement—similar to what they had when they were earning a paycheck. Indeed, supporting a stable standard of living is what financial planner Bill Bengen had in mind when he developed the widely used 4% guideline for retirement-portfolio withdrawals. Thus, the 4% guideline assumes that a retiree takes out 4% of his portfolio in year one of retirement, then inflation-adjusts that dollar amount in ensuing years. For example, a retiree with an $800,000 portfolio who is employing the 4% guideline would take $32,000 initially, $32,960 in year two of retirement (assuming a 3% inflation rate), and so on.

That said, anyone who has managed a household budget knows that spending is not a flat line. There might be several years when spending clusters in a tight range, as well as budget-busting periods when there are splurges for the big-ticket vacation or multiple unplanned expenses—car repairs, big outlays for home repairs or improvements, vet bills, and so on. Retirement is no different. In fact, due to lifestyle factors, retiree spending may be even more erratic than spending during the working years. Morningstar research has identified a pattern it refers to as the "Retirement Spending Smile." Their research has found a tendency for retirees to spend more during the early years of retirement on things such as travel, followed by a period during which they spend a bit less during the middle years of retirement, followed by a period of accelerated spending toward the end of life, when healthcare and long-term care outlays often increase (but not enough to completely offset lifestyle-related spending declines). How retirees expect their lifestyles to evolve during retirement should play a role in their spending plans.

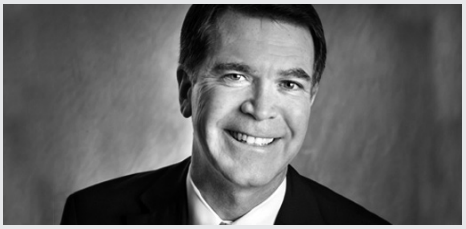
In addition to expected spending levels and patterns, anticipated portfolio performance will also factor in determining an appropriate withdrawal rate. An open question, therefore, is whether the market environment assumed in establishing the 4% guideline is a good representation of the future. Given the current low interest rate environment and the likelihood of rates continuing to trend higher, investors employing overly conservative portfolios (that is, holding 50% or more of their portfolios in bonds) ought to also be conservative when setting their withdrawal rates. Moreover, the combination of low starting bond yields and relatively high equity valuations make this a particularly challenging time for sequence-of-return risk—that is, that new retirees could encounter a challenging confluence of events at the outset of their retirements that in turn could crimp their portfolios' sustainability. Taking too much out of a portfolio in a weak market environment can deal a portfolio a blow from which it might never recover. That argues for recently retired and soon-to-be retirees taking a cautious tack on their upcoming withdrawals, beginning with withdrawals of less than 4% and being willing to rein them in further if a calamitous market drop materializes early on in their retirements. Retirees who have been drawing for their portfolios for several years already are less at risk for a market shock; they will have losses amid an equity-market downturn, too, but they have already made it through their most vulnerable years.

One final consideration is the type of funds withdrawn from a retirement portfolio(s). Spending a portfolio's bond and equity-dividend income counts as a "withdrawal" as much as spending capital gains and principal; but the effect of doing so on the long-term viability of the portfolio(s) is not the same. It is wise, therefore, for retirees to stay flexible on their portfolio's source of cash flow, being willing to harvest income distributions as well as to engage in rebalancing to help source the cash flow needed. In addition, employing a cash "bucket" of retirement assets to provide liquidity in years when tapping principal or harvesting income is ill-advised (like when the market is down), is a savvy move.

Each retiree's anticipated spending needs, retirement portfolio(s), risk tolerance, and time horizon are unique. Accordingly, each retiree's withdrawal rate is unique. To better understand your ideal retirement withdrawal rate, talk with your Wintrust Wealth Management Financial Advisor. ■

Morningstar's "Retirement Spending Smile" refers to a pattern by which retirees spend more during the early years of retirement on things such as travel, followed by a period during which they spend a bit less during the middle years of retirement, followed by a period of accelerated spending toward the end of life.

Autumn 2017 Economic Outlook



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Despite the considerable political and economic noise in the news recently, one persistent signal has come from the Federal Reserve Board of Governors in its efforts to re-normalize monetary conditions. To wit, the Fed Funds rate is now above 1% for the first time in 13 years. However, the rise in the Fed Funds rate has not been matched by an appreciable rise in the 10-year Treasury yield. Consequently, the yield curve has flattened, which typically presages an economic slowdown. Most data do not indicate a slowdown is occurring just yet, with the possible exception of weaker housing starts and building permit prints, but the matter warrants close monitoring.

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Most of the second quarter saw a continuation of first quarter themes in the U.S. equity markets. Once again, shares of companies with larger market capitalization outperformed, paced by the Russell Top 200 Index's 3.2% gain. There was also a continuation of the trend of growth stocks outperforming value stocks across the capitalization spectrum.

In the U.S. fixed income markets, corporate bonds led the way in total return. Comments by key FOMC members regarding concerns over the raising of rates in the face of low inflationary pressures adversely impacted the treasury market, as rates on the 10-year and 30-year bond jumped in the final days of the quarter. Nonetheless, long-bond returns were positive, as the yield curve flattened much as it did in the beginning of 2016. The yield on 10-year U.S. Treasury Notes closed at 2.27%—80 basis points higher year-over-year, but 12 basis points lower than March 31, 2017. Finally, oil prices declined 9% during the quarter while the U.S. dollar weakened almost 7% against the Euro.

Overall, the Trump Administration has found it difficult to implement its legislative agenda, leading some to question the likelihood of an acceleration of U.S. economic growth over its current modest pace of expansion. Despite much anticipation, clear signs of boosted economic activity have yet to appear.

The Federal Reserve has done more than many thought plausible to prop up our economy. Those efforts have worked, and worked well. Now, however, policy has reversed, whereby the Federal Reserve is concentrating its efforts on unwinding its massive balance sheet without disruption. Europe is in a similar position. This shift in the direction and goal of monetary policy raises the level of risk in the markets heading into the latter half of the year. ■

ESTIMATED ECONOMIC VARIABLES AND INTEREST RATES

	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018
Real GDP	2.40%	2.20	2.30	2.50	2.40
Consumer Price Index	2.20%	2.30	2.10	2.00	2.30
3-month Treasury Bill	1.44%	1.61	1.79	2.02	2.18
10-year Treasury Note	2.45%	2.65	2.77	2.87	2.99
Unemployment	4.40%	4.30	4.30	4.20	4.20

Source: Bloomberg