

NEW WAYS OF THINKING: ADVANTAGES FOR PRE-RETIREEES

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While the economy appears strong, there are significant structural issues bubbling under the surface.

Geopolitical, economic and demographic trends indicate that the U.S. will likely encounter some combination of higher taxes, higher inflation and higher interest rates perhaps for the next few decades. Given these conditions, pre-retirees may need to reconsider the age and manner in which they leave the workforce.

ECONOMIC CONSIDERATIONS

Consider the abundance of factors:

Higher Taxes

- ✓ **National debt.** Currently, the U.S. national debt is a mind-blowing \$34 trillion and growing. Interest payments now approximate the amount paid for Social Security and will soon exceed expenditures for national defense. Higher taxes will likely be needed to meet surging budgetary demands.
- ✓ **Pension and health care.** Due to demographics and income distribution, the demand for social services — including health care, education and Social Security — is straining our government budget. As populations age and health-care costs escalate, further tax hikes may be warranted.
- ✓ **Defense.** Recent geopolitical events have demonstrated why the U.S. must maintain its global military supremacy. Nations such as China, Russia, Iran and North Korea are intent on repudiating the global foreign exchange and free-trade

system established under U.S. leadership. Protecting international trade, preserving infrastructure, partnering with allies and preventing terrorism requires tremendous expense, likely much more than is allocated today.

Higher Inflation

- ✓ **Restrictive trade policies.** For decades, the global economy benefitted from the implementation of global free-trade agreements. Unfortunately, the more affluent often derived the greatest rewards from globalization. The middle and lower classes often suffered as manufacturing jobs were shifted abroad. As a result, we are now seeing the rise of political populism and isolationism. This is driving organized labor and concepts such as friendshoring which restricts free trade. This policy reversion will have a long-term inflationary effect.
- ✓ **Demographics.** Global demographic trends are downright disturbing. Virtually all major economies are contending with rapidly aging populations and a decreasing supply of labor. With fewer people actively participating in the workforce, there is less capacity to meet the demand for goods and services, potentially leading to supply shortages and price increases.
- ✓ **Supply chain disruptions.** Interconnected supply chains have heightened vulnerabilities to disruptions, as evidenced by recent events such as the COVID-19 pandemic and the military conflicts in Ukraine and the Middle East. These disruptions can lead to shortages, bottlenecks and rising production costs, all of which contribute to inflation.



Higher Interest Rates

- ✓ **Normalization of monetary policy.** After years of extraordinarily accommodative monetary policy measures, central banks are gradually shifting toward higher interest rates to counter inflation concerns and risks to financial stability. During the last few months in particular, the Federal Reserve has urged investors to remain patient and anticipate interest rates that Fed Chair Jerome Powell says will be “higher for longer.”
- ✓ **Government borrowing costs.** Rising government debt levels and fiscal deficits may prompt investors to demand higher yields on government bonds to compensate for increased credit risk. Further debt downgrades by rating agencies will only exacerbate this problem. As a result, governments may face higher borrowing costs, which could translate into higher interest rates.
- ✓ **Capital flight and exchange rate pressures.** In an environment of rising interest rates, investors may seek higher returns by reallocating capital to countries with more attractive yields. This capital flight can exert downward pressure on domestic currency values, prompting central banks to raise interest rates to defend exchange rates, further contributing to higher borrowing costs.

WITH ADVERSITY COMES OPPORTUNITY

Higher taxes, increased inflation and rising interest rates present a clear economic threat; however, this economic adversity may yield opportunity for pre-retirees. The traditional path toward retirement suggests that retirees simply stop working at a given age. However, the U.S. economic juggernaut and the perpetual demand for skilled labor means that pre-retirees should consider working on a part-time, flexible basis.

Even with inflated immigration, there is a substantial shortage of workers in the U.S. According to the Federal Reserve Bank, our current LFP (Labor Force Participation) rate is 62.5% which is the lowest in generations. Moreover, this problem is anticipated to worsen in the coming years. Population replacement depends on a fertility rate of 2.1; the U.S. birth rate is currently 1.84. By comparison, according to cia.gov, the U.K.’s rate is 1.63, Germany’s is 1.58 and China’s is 1.45. This data suggests that as the U.S. economy continues to expand, there may not be a sufficient supply of qualified, skilled labor. Technological development and productivity can bridge some of the gap, but it will take years — perhaps decades — for the benefit to fully materialize. Pre-retirees are ideally suited to fulfill this need.

ADVANTAGES OF PART-TIME WORK

Professionals working part time in their 60s can derive several advantages:

- ✓ **Maintain health benefits.** If workers qualify for employer-provided benefits, they can sustain healthcare coverage and continue saving for retirement. In addition, many employers also provide inexpensive life insurance and long-term disability insurance options.
- ✓ **Reduce taxes.** Earning income from part-time work allows retirees to implement tax-planning strategies to manage their tax burden, including the following:
 - **Contributing to retirement plans.** Contributions to tax-advantaged retirement accounts such as IRAs and 401(k) plans provide compounded tax-deferred earnings and can reduce taxable income.
 - **Postponing collection of Social Security.** By earning additional income, clients retain the option of postponing the collection of Social Security. Doing so further enables retirees to increase the amount ultimately received each year once they file their claim.

- **Leveraging new Secure Act laws for later RMDs.** Since retirees are now permitted to postpone their required minimum distributions (RMDs) into their early 70s, this allows for better coordination from retirement accounts and taxable investments to minimize tax consequences. This can help manage tax liabilities and preserve portfolio growth potential.

- ✓ **Hedge against inflation.** Unlike fixed-income investments, part-time wages have the potential to keep pace with rising prices, helping retirees maintain their purchasing power over time.

- ✓ **Save for longevity.** As the quality of health care continues to improve, many clients will ultimately live longer than they might expect. The extra earnings generated during pre-retirement, along with the aforementioned advantages, can provide a substantial boost to long-term savings.

- ✓ **Boost mental health.** By staying active and engaged, retirees can ward off feelings of isolation, depression and cognitive decline, leading to a more fulfilling and satisfying retirement experience. Keeping the mind stimulated and the body active promotes a positive outlook on life and contributes to overall mental and emotional resilience during the later years.

Rapid improvements in technology, swirling economic conditions and a variety of geopolitical threats pervade the landscape. The longer people live, the greater the risk with which they must contend; it therefore becomes prudent to maximize flexibility when evaluating long-term decisions. Rather than planning for retirement with a permanent mindset, clients would be well-advised to consider a more gradual approach that sustains assets but still permits time to enjoy their later years. 🧩

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