COGNITIVE DECLINE AND DESIRABILITY OF PROTECTED INCOME

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The greatest threat to the financial security of many older adults is not a recession, market correction, or inflation. It is the risks posed by health-related events and costs.

Roughly 78% of adults over the age of 55 in the U.S. have been diagnosed with at least one chronic illness, like diabetes or asthma or arthritis, and 64% over 65 suffer from two or more.[1] About 116 million Americans have hypertension,[2] and 800,000 people in the US experience a heart attack each year.[3] In 2022, about 1.9 million people were diagnosed with cancer.[4]

But perhaps the greatest health-related threat to financial wellness and retirement security is cognitive decline. Unlike the progress we are seeing in other medical fields like cancer and heart disease, success in finding a cure for dementia has been elusive. There have been over 200 failed Alzheimer's disease trials in the past two decades.[5] Alzheimer's is the only disease among the top 10 causes of death in the US that cannot be prevented, cured, or even meaningfully slowed.[6]

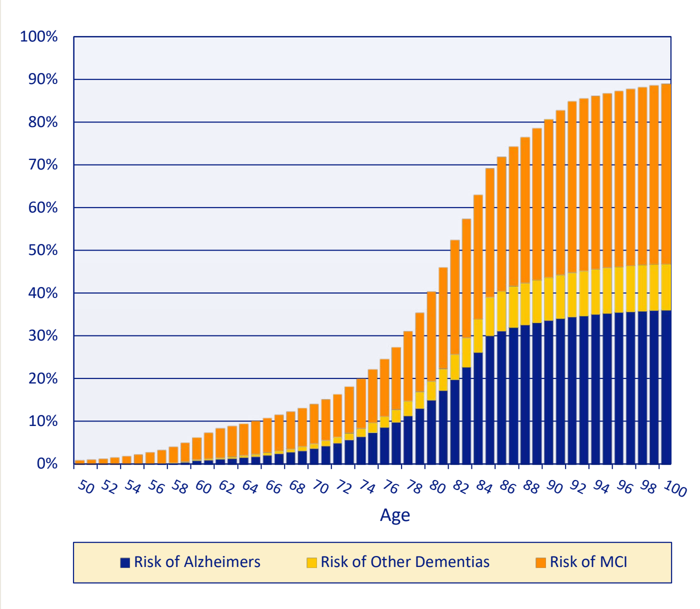
Cognitive decline can have devasting consequences for personal finances and sound financial decision-making. Studies have shown that the ability to manage finances is one of the first cognitive skills to deteriorate.[7] Cognitive decline leaves individuals and families increasingly vulnerable to sub-optimal financial decision-making, including being victimized by an ever-growing array of scams perpetrated by sophisticated financial predators.

As the population ages, the likelihood that someone you know experiences cognitive decline will increase. An estimated 11% of adults over the age of 65 in the U.S. today are living with Alzheimer's, the most common form of dementia, and an additional 3% suffer from related illnesses, like vascular or frontotemporal dementia.[8] So roughly 14% of adults 65 and older in the US have dementia. It's safe to assume that anyone suffering from dementia is incapable of making sound financial decisions.

But many older adults also suffer from what medical specialists refer to as mild cognitive impairment, or MCI (and sometimes now described as mild neurocognitive disorder). MCI is different than dementia and "describes a level of cognitive decline that requires compensatory strategies and accommodations to help maintain independence and perform activities of daily living (ADL)".[9]

Adults with MCI experience cognitive decline that goes beyond "normal aging". It is reasonable to conclude that most if not all adults with MCI should also not be making important financial decisions on their own. An estimated 15% of adults over 65 in the US suffer from mild cognitive impairment (MCI).[10]

Figure 1. Risk of Dementia or Mild Cognitive Impairment (MCI) by Age



Together, the estimates suggest that about 29% of adults 65 and over are already having difficulty making sound financial decisions. And like many diseases, likelihood of having dementia or MCI increases with age. By age 82, there is a 50% chance that a person has either dementia or MCI. And by the time they reach age 90, there is better than an 80% chance they have dementia or MCI.[11] (See Figure 1.)

Unfortunately, sub-optimal financial decision-making is likely to occur even earlier. A comprehensive study found that financial decision-making mistakes follow a U-shaped pattern, with the "peak age" of financial decision-making occurring at around age 53.[12] This suggest that difficulties with financial decision-making for many people begin *well before* the onset of a serious cognitive illness. Another study found that bill payments started being missed six years before an official diagnosis of dementia,[13] implying that even "normally aging" adults may have difficulty making sound financial decisions.

These findings dispel many of the common misconceptions about aging and financial decision-making: "I'll be fine as long as I don't get Alzheimer's". It is a virtual certainty that all of us will experience a decline in the ability to make sound financial decisions as we get older, especially as we get into our 70s and beyond.

So, what can we do to protect ourselves and our loved ones? A good strategy is to reduce the number of consequential financial decisions we need to make on an ongoing basis. We can all benefit from simplifying our personal finances and putting as much of our decision-making as possible on (safe) autopilot.

The execution of financial transactions, even minor ones, can present opportunities for accounting mistakes, judgement errors, memory lapses, impulsive decisions, or financial scams. The downside risks associated with the need – or desire – to sell an existing asset, make a new investment, or pay a bill tend to increase as we get older.

Reducing the number of financial accounts we need to manage, automating bill payments, and assembling a team of trusted family members and professionals can all help lower the frequency of financial transactions and thereby decrease decision-making risks.

Guaranteed income strategies like annuities can provide a similar type of protection. Because they decrease the need for, and frequency of, potentially risky financial transactions, they help to shield individuals and their families from sub-optimal financial decision-making. Protected income products can comprise an important element of a safe and risk-reducing financial decision-making "autopilot" strategy as they provide a regular stream of income, absent the need to execute a transaction.

Protected income products can also help guard against other health-related financial risks, like having a health event that leaves you temporarily or permanently incapacitated (cognitively or physically), outliving your savings, or requiring lengthy long-term care.

Because it is likely to happen to just about all of us as we get older, reducing the decision-making risks associated with cognitive decline should be a major goal of any financial plan. For many adults and their families, protected income products can play an important role in meeting that goal.

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