



# MARKET MONITOR

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## Health Care Costs: A Common Cause of Angst for Retirees

BY: MICHAEL ALEXENKO, CFA

Let's say that you've saved and invested well and that your retirement nest egg is \$2.4 million. You own your home debt free that is valued at \$700,000 and you and your spouse qualify for \$66,000 in annual social security benefits. Your three children are all graduated from college and have been fortunate enough to stay employed in an uncertain labor market. For a couple who were in an upper-middle income category while employed this description frames a good example of a likely financial profile.

A couple as the one described above could expect to draw about 4% to 5% from their retirement accounts and thereby enjoy about \$14,500 in monthly inflation adjusted income, which permits them to maintain purchasing power through their retirement years.

A husband and wife who are retired (age 65+) and in good health with about \$175K in annual income could look forward to some relaxing years that include nice vacations and taking pleasure in being with their grandchildren. But the seemingly comfortable conditions laid out don't exactly guarantee a worry-free life.

The key variable that perhaps disrupts serenity for any retired couple is their health, and it's an expenditure that has the potential to result in catastrophe. The good news is that for 95% of people with \$175K in retirement income, the costs of health care can be quite manageable. If

you're planning for retirement, you should be aware that today, a couple's total cost of health insurance would be about \$13,000<sup>1</sup> per year. Plan on that figure increasing at over the standard inflation rate or about 4% annually for years to come.

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The \$13K figure includes the premiums paid for Medicare Part A, B and D and the premiums for a supplemental insurance policy to pay for costs not covered by Medicare. What the \$13K does not cover is long term care (LTC) expenses and thinking about those costs probably create the most anxiety for those in retirement or nearing retirement age. No one looks forward to being admitted to a nursing home, and moreover the cost that's associated with the experience makes the thought of it more unpalatable.

Another aspect of health issues and LTC that make them vexing is their uncertainty. It's difficult to know how much LTC we could need and for how long and those are the factors that will drive possible costs. Fortunately, there are some statistics that can help us to make some preparations for potential risks.

It's estimated that a couple 67 years old in 2025 will spend about \$415,000 on costs associated with normal health care issues; those costs being doctor visits, short term hospital stays and prescription drug expenses<sup>2</sup>. All of the costs would be covered by the \$13K annual medical insurance premiums.

That leaves us with the exposure to LTC and what those costs could total. It's important to note that many individuals will not need high cost LTC. The data are somewhat sketchy and contradictory on the percentages of people who require nursing home care. But, in general there is consensus that a period of two years in a LTC facility would be a rather lengthy stay. Government statistics suggest that 70% of the population will need some type of LTC<sup>3</sup>. Keep in mind this includes home health care, assisted living and family members providing needed aid, which is why the percentage is so high. Other sources suggest that about only 25% of people die in a nursing home and that most people admitted into a nursing home spend less than six months there<sup>4</sup>. Knowing that information, the question becomes how to quantify the potential cost of LTC using the various statistics so you can adequately hedge against the risk.

A fair estimate for private paid LTC in a private room is about \$10,625/month. If our 67-year old couple who we began our conversation with were forced to pay for two years of

<sup>1</sup> American House Senior Living

<sup>2</sup> <https://communications.fidelity.com/wi/tools/retirement-health-care/>

<sup>3</sup> Longtermcare.gov

<sup>4</sup> [www.haymsalomonhome.com](http://www.haymsalomonhome.com)



## Know the Factors to Determine the Value of LTC Insurance

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nursing home expense today it would deplete \$255,000 of assets. That leaves our surviving spouse with more than \$2.1 million if all costs are paid from their investment balances, which hardly creates a financial catastrophe. If they purchased LTC insurance at the age of 40, it might improve their residual net worth, but the complexity and costs of those insurance policies need to be closely scrutinized to discover what the

potential value of the hedge from the policy might actually be. If they think about offsetting their risk today by buying a LTC policy, the chances that it benefits them more than the insurance company are close to 0%. The alternative is to make use of Health Savings Accounts (HSAs), which are excellent tools to pay for future medical expenses. The Trump Administration would be wise to spend more time and political capital

promoting these and other market-based reforms of our healthcare system rather than villainizing foreign trading partners (except China).

There can always be statistical outlier events, (eg. \$500K in LTC costs) but the best approach is to prepare for the most likely outcomes and allow some cushion for more extreme situations.

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## Market Snapshot:

### An AI Fed Could Help to Keep Focus on Earnings and Economy

BY: MICHAEL ALEXENKO, CFA

Did you know that the Federal Reserve didn't exist until sometime in 1914? After 138 years, political leaders convinced the public that if a central bank was created it would help smooth economic activity. There were a number of depressions prior to the Federal Reserve Act, but they usually lasted no more than a couple of years. It was after the Fed was created that the USA suffered its worst depression that lasted for over twelve years. Maybe the protest song of 1970 should have been titled "FED, what is it good for?" rather than, "War, what is it good for?"

After more than 110 years of a checkered Fed record consisting of asset bubbles, stiff recessions, and a bloated Fed balance sheet, we find ourselves with a pugnacious president in an open "war" with the Fed chairman because he doesn't like what he believes to be a monetary policy that is constricting our economy. Fed officials fire back that they need more data to know when the right time is to cut interest rates. They expressed shock at the weakening of the labor market after the August 1<sup>st</sup> report, but should they have been shocked? It

seems that we pay the scholars at the Fed to interpret a collection of data to determine the state of our economy and its expected performance. If they are simply waiting for the September labor and inflation reports that are available to everyone to determine the state of the economy, then what is the Fed good for?

Before artificial intelligence was part of our vocabulary, a renowned economist, John Taylor proposed the replacement of the Fed with an objective monetary policy model that could dispassionately implement money supply and interest rate policies. In today's artificial intelligence age, that model tool could be strengthened and investors could spend much less time on guessing about the Fed's next move and more time focusing on economic growth and corporate earnings to discover the appropriate price for stocks and bonds. In the absence of an AI Fed, what we'll have is more price volatility from needlessly clinging to every word coming from a bureaucratic organization that isn't much better at economic forecasting than the ordinary investor.

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