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Retirement Planning: Back to Basics

By admin

In the aftermath of the US housing market bust and the ensuing financial meltdown that led to global stock market declines of 2008, people are getting back to the basics as far as their retirement planning goes. Although the stock market has recovered, many pre-retirees have lost a lot of ground in their retirement accounts and are facing a new reality. Retirement may not be what they had originally envisioned; but with some **retirement income 101 basics,** most people should be able to get back on track.

Start with Realistic Assumptions

To determine your retirement income needs, you have to **start with some realistic assumptions about the future.**The most important assumption is how long you will live. With life expectancies expanding, most people who reach the age of 65 can expect to live beyond the age of 85. If you're married, there is a good chance that one of you will live beyond the age of 92! That's a range of 20 to 32 years of life in retirement.

A lot of people assume that, when they retire, their expenses will decrease so they won't need the kind of income they were earning while working. Over the years, several different rules of thumb have been tossed around, such as 70% of earned income is sufficient for retirement income needs. That probably won't cut it for **today's retirees who can expect to live 25 years or more.** Studies have shown that the early years of retirement are the most expensive. Then as people age, they are less likely to travel or spend money on entertainment; but medical or long-term care costs tend to increase in the later years.

Determine Your Savings Need

Using your assumptions, you need to determine the amount of money you will need at your target retirement age that can generate an income flow for 25 or more years. The old rule of thumb was the amount of money needed was based on a draw down of 4% per year to make it last. Recent studies revealed that, at that rate, retirees were exhausting their savings much too soon. Experts now say that the amount should be based on an annual draw down of 2 or 3% of their total retirement portfolio (tax-deferred RRIFs, TFSAs & regular savings), adjusted annually for inflation.

The Inflation Factor

The impact of inflation on an income that has to last for 30 years can be devastating. Essentially, **a 3.5% inflation rate would cut the purchasing power of your money in half in 20 years.** All assumptions and future income needs should include a realistic forecast for inflation or you are likely to find that your income sources come up short.

The Need for Growth

As more people approach their retirement target dates with diminished RRSP accounts, and with increasing prospects for inflation resurgence, pre-retirees will need to maintain a **growth orientation in their portfolio** even after they retire. The key to achieving long term growth, while maintaining relative portfolio stability, is to create a well-rounded and fully diversified investment portfolio.

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