HOW MUCH WILL YOU NEED TO RETIRE?


Austin L. Peterson, CFP®, CLU®,MBA | January 24, 2019
Share|

How much money will it take for you to retire in style? Will $1 million do the trick? How about $5 million? Or perhaps you can get by on less.

If the question leaves you scratching your head, you're not alone. Just 36 percent of American workers have talked with a financial advisor about retirement planning, according to the Employee Benefits Research Institute. One of the biggest risks retirees may face is running out of money while they're alive. It's an all-too-possible scenario, even if you have substantial assets.

An extended market slump, excessive spending, soaring health care costs and other factors can wreak havoc on your chances of securing a comfortable retirement—as well as meeting other financial goals such as transferring wealth to heirs or charities. The good news: There's plenty you can do right now to determine what your ideal retirement is likely to cost, and plan accordingly. Start with a review of the key retirement income issues, such as:

Your life expectancy

Thanks to medical breakthroughs, retirees today are living longer than ever. Considering that the average life expectancy once you hit age 65 is 19.3 more years for males and 21.6 more years for females, according to the Social Security Administration, you could live much longer—so it pays to aim high. You should anticipate living to 100, which is a reasonable number these days. It's smarter to plan for a longer retirement and not get caught short.

Your retirement expenses

Once you leave the workforce, expenses such as business clothing, commuting costs and perhaps even your mortgage might fall or disappear entirely. However, your spending may spike for travel and leisure, gifts to family members and—perhaps most importantly— medical care and prescription drugs. Your financial planner can help you review your current expenses and whether they are likely to change over time. In general, retirees may need roughly 75% of their pre-retirement living expenses (adjusted annually for inflation) to retire comfortably. And long-term care insurance can help defray the often enormous custodial care costs that can devastate an income stream.

Your portfolio

As part of the retirement planning process, your financial planner will estimate the average annual rate of return your savings and investments must earn to help meet your spending requirements and other goals. Then, an optimal portfolio of investments will be crafted that takes the lowest level of risk necessary to earn that potential return. Chances are, that portfolio will include a healthy dose of stocks for growth potential and to help protect your purchasing power. The fact is, even retirees need equity exposure to outpace inflation. For example, a retired couple with current expenses of $85,000 will need approximately $153,500 to pay for their expenses in 20 years, assuming a modest 3% annual inflation rate.

Your withdrawal strategy

The amount of money you draw from your portfolio each year will have a huge impact on how long your nest egg lasts. The appropriate withdrawal rate varies for each investor, of course, based on factors such as how much income you might receive from Social Security and a company pension, taxes and if you wish to leave money to any heirs or charities, but is generally estimated to be no more than 3% to 4% of your total. You'll also want to discuss with your financial planner whether it's best to tap any tax-deferred plans first or start taking income withdrawals from taxable accounts given your situation and goals.

Estate planning and philanthropic goals

Investors planning to gift assets either while alive or bequest assets upon death must factor in how their wealth transfer goals might affect their expenses and cash flow in retirement. For instance, you might want to consider strategies for leaving more money to heirs and charities, and less to estate taxes if you have a sizeable estate. Tools such as charitable trusts and insurance can help strike a balance between meeting current living expenses and providing for future objectives.

Hopefully your analysis will reveal that you're well on your way toward achieving a secure retirement. If not, don't fret—there are plenty of ways to get back on track. Consider looking for ways to spend less in retirement, such as trading down to a smaller home or working part-time. Retirement is often the perfect opportunity to pursue professional interests that you didn't have time for during your working years.

Conversely, if you're several years or decades away from retiring, saving and investing more aggressively now may help you build greater wealth over time. But remember, there is no assurance that by assuming more risk a portfolio is guaranteed to achieve better results. In the end, the process of mapping out your retirement income needs will give you an important benefit: the knowledge of where you are today, and what it will take to help obtain the retirement you desire.