

Retirement Planning Myths

A financial plan is only as solid as the assumptions and foundation upon which it is built. Make sure that you are reasonable about major, “big picture” issues surrounding your retirement years. That way, you’ll be able to enjoy retirement knowing that you’ve got your financial bases covered.

Longevity

For whatever reason, most people planning for retirement underestimate how many years they will live. With average life expectancy consistently on the rise, it should come as no surprise that, even at age 65, there is a significant likelihood that you will live another 20 years — or longer. However, the tendency is for individuals to assume that whatever assets they have saved will last them through their final years. Be realistic when running calculations aimed at determining your asset needs during retirement. If you are in good health and have a strong family health history, assume that you will live a long time.

Expenses

Many people make the mistake of assuming that their fixed costs will go down dramatically during retirement. In turn, there’s a tendency for people to think that they may not have to replace a significant portion of their income. Expenses such as the cost of commuting, dry cleaning, workday lunches out, and Social Security and Medicare taxes may go by the wayside. However, increased health insurance premiums and other out-of-pocket medical expenditures, leisure activity expenses, and other costs may more than make up for the savings associated with no longer working.

Inflation may prove to be the costliest underestimated expense of all. Even at a modest pace, over the course of a 20-year retirement, inflation will significantly erode the purchasing power of your retirement dollars.

Some people plan to transition into retirement under the theory that they can live off the interest or earnings generated from their nest egg without tapping into the principal. The problem with this planning perspective is, again, underestimating the progressive impact that inflation is likely to have over the course of retirement. Assume, for example, that your retirement expenses equal your income in year one of your retirement. Over the course of a 20-year retirement, if your earnings averaged 7% and the inflation rate was 4%, you would have to tap into your principal in the second year to meet expenses, and you would have exhausted your entire principal at the end of 20 years.

Income Replacement from Other Sources

Although a dying breed, defined benefit pension plans provided by private employers do still exist. However, their existence may result in an ill-founded complacency about the need to replace income. Even if a private pension and Social Security retirement benefits each replaced 30% of your preretirement income, there would still be a need to supplement those sources through your 401(k) or other personal retirement savings.

Wait ’til Later

Some people operate under the premise that they can wait until later in their working years to start saving and, at that time, simply save more to make up for lost time. Countless studies have shown how difficult it is to make up for the power of time and compounding. Waiting even five years to start saving can have a tremendous impact on the amount accumulated in your nest egg by a given retirement age.

Talk to Us

Our firm can answer many of your questions associated with retirement savings. Please contact us well in advance of making significant financial decisions affecting your retirement years.