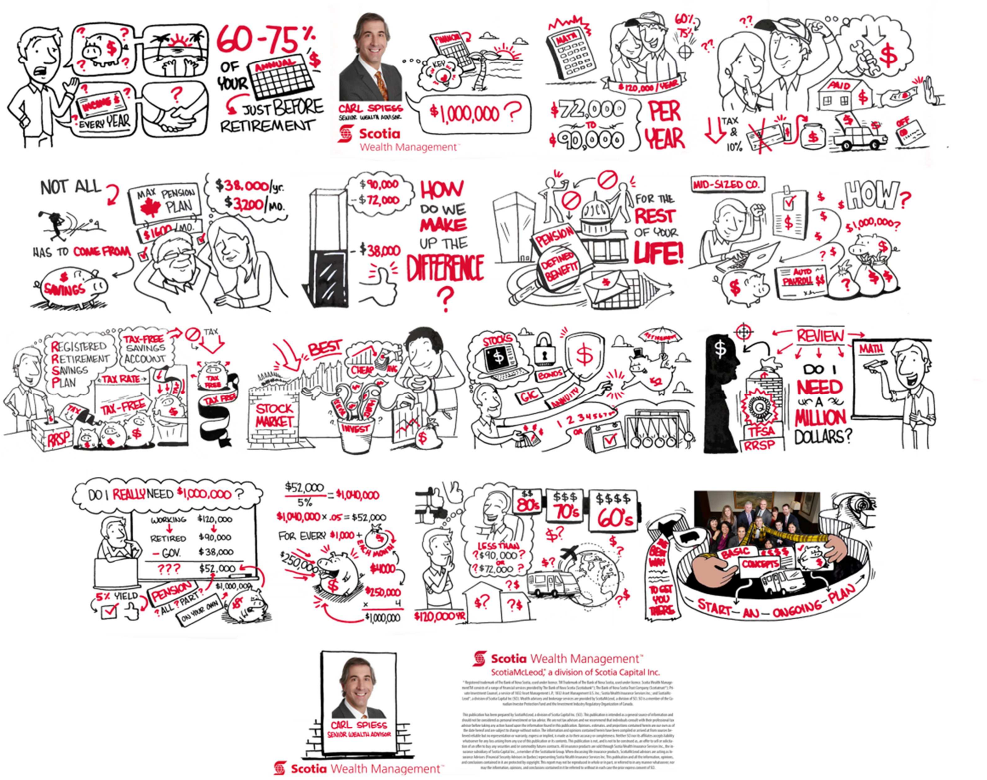
Do you really need to save a million dollars?

Carl Spiess – Whiteboard video text – Dec 2015

Many Canadians will ask: How much do I need to save up for retirement? In fact you should be asking: How much ***income*** will I need every year after I stop working?

The generally accepted answer is; 60 to 75 % of your annual working salary just before retirement.



Hi, my name is Carl Spiess, and I'm a Senior Wealth advisor with Scotia Wealth Management. I want to share some key ideas behind financial planning for retirement and hopefully answer the "million dollar" question for you.

We'll do some simple math along the way. If we take a typical Canadian couple that earns a combined $120,000 a year before retirement, targeting retirement income at 60 to 75 % would mean living on $72 to $90,000 a year.

Working Income / month:	$10,000	
Mortgage and debt	$1,500	cross out
Child costs	$1,000	cross out
Work expenses / commuting	$500	cross out
Income Taxes	$2,500	down arrow
Retirement saving	$1,000	cross out
Groceries & dining	$1,000	
Transportation	$500	
Home utilities, taxes, repairs	$1,000	
Lifestyle expenses	$500	
Miscellaneous	$500	
	$10,000	$6,000?

You may wonder how you can suddenly get by on so much less than your working salary. Well, hopefully your mortgage and personal debts are paid off, your kids are independent, and you don't have commuting or work-related expenses. You'll also be paying less tax and you won't have to save part (we recommend 10%) of each paycheck to build your retirement fund.

Furthermore, not all of your retirement income has to come from your savings. As Canadians, the maximum Canada Pension Plan and Old Age Security benefits will pay $1,600 a month total per person. That's $3,200 of income a month for a couple, or around $38,000 a year.

That's a pretty good start, but it's still far short of $72 to $90,000 that the couple in our example might still want. So how do we make up the difference? Do you have a pension plan through your employer? If you work for certain large businesses or the public service, you may have a defined benefit pension that will pay a guaranteed monthly income for the rest of your life… and yes, that's as good as it sounds.

But if you are self-employed or work for a small business, chances are that you might not have an employer sponsored plan at all.

And for those working for mid-sized employers, you may be lucky enough to have a retirement savings plan through work. So you may have already been doing some saving for retirement through convenient payroll deduction. But depending on the amount of the contributions, you may need to save some additional money. Is a million dollars the right number though? – And how can you save that much?

When Canadians think about retirement savings, we first think about Registered Retirement Savings Plans. Your contributions to an RRSP can give you a helpful tax deduction, and your savings grow tax-free until they are withdrawn and taxed – likely at a much lower tax rate.

And depending on you marginal tax rate, I would also suggest looking at a Tax-Free Savings Account. Your TFSA contributions do not give you a tax deduction, but your savings grow tax-free and can then be withdrawn tax-free.

Your retirement savings held in your RRSP or TFSA will not grow unless you invest them. So what are you going to invest in? Hands down, the stock market provides the best returns over the long term, but the short-term volatility can be an emotional rollercoaster ride. We recommend stock based portfolios for younger investors who can wait out the ups and downs of the market and take advantage of the downturns and to buy cheap when the market is down. See how that line goes up and down a lot, but also how historically it goes up quite substantially over time.

The closer you get to actually spending your retirement savings, the less one can tolerate those short-term swings in the market. You'll want your investments to be more predictable, even if they don't grow as much as they used to. Now you can sell some of the stocks from earlier days, locking in any profits, and then replace them with more defensive investments like bonds or guaranteed investment certificates (GICs) or convert to annuities.

Along the way, there are thousands of investment options that can be customized just for you. Or to keep it simpler, a professionally managed retirement target date fund will simply rebalance it all for you automatically over time.

So let's return to our Canadian couple and review where we are right now. We targeted a retirement income of 72-90k, we have chosen the best investment accounts, the RRSP and TFSA, and we put our money in professionally managed high quality growth investments that are appropriate based on your current age and risk tolerance.

Now we get to that big question "Do I really need a million dollars"? Bear with me while we do a bit more math to determine how much to save.

A 5% income off your retirement assets is generally considered a good rule of thumb.

Target?	$90,000
Government	$38,000
Replace	$52,000

So, if you want to retire with a sustainable income of $90,000 a year, and you count on receiving $38,000 from government sources, you're still going to need to find another $52,000 from somewhere else.

If you have an employer-sponsored pension, it may provide all or part of that missing 52k. If you don't have an employer plan, you may indeed need to try and save just over $1 million before retirement to reach that missing $52,000 of annual income you want. Here's how we get that answer

$52,000 / 5% = $1,040,000 $1,040,000 x .05 = $52,000

An alternative way to think of this is that for every $1,000 of additional retirement income you want each month; you will need $250,000 in savings.

(eg. $12,000 / $250,000 = roughly 5%: 4.8% to be exact)

So if you want $4,000 a month – you'll need 4x$250,000 = A Million dollars.

If you earn $120,000 a year right now, could you enjoy retirement with less than $90,000 or even $72,000 per year of income? Many people do, especially if your home will be paid off and you no longer have mortgage payments.

But it really boils down to the lifestyle you expect in retirement, and how much that will cost. The good news is that, retired people generally spend the most money in their 60s, less in their 70s, and even less in their 80s and 90s.

The Spiess McGlade Team at Scotia Wealth Management can take these basic concepts, add in your personal financial information and your retirement expectations, and start an ongoing plan just for you. It's the best way make sure that you'll have the money you need for the lifestyle you want. I hope that maybe we can help you in the future and look forward to your comments and questions.

View the full video at: www.youtube.com/CarlSpiessScotiaWealth

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