

THE Guardian

...building better retirement incomes since 1974

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“HOW MUCH IS ENOUGH?”

How much income will you need in retirement? It depends on who you ask.

The widely quoted rule of thumb is 70% of your pre-retirement income. The assumption is that with the mortgage paid, the kids out of the home and the fact you are no longer saving money for retirement, your requirements diminish significantly. However, as we outline below, there are widely divergent opinions on how accurate the 70% rule is.

A Statistics Canada study undertaken in 2005 found that people whose pre-retirement income was \$70,000 or greater tended to retire on 45% of that. Those who retired earning the national average wage (between \$40,000 to \$50,000 at the time) retired on 59% of their pre-retirement income. Further, only 1 in 6 with a pre-retirement income of \$40,000 or more had a replacement ratio of 75% or greater.

Fidelity Investments set off a new debate in 2007 when they published a report on the changing state of retirement in Canada. Fidelity asserted that the replacement ratio was 75 to 85% of pre-retirement income. Fidelity's assertion was that life expectancy is going up, and the median retirement age is going down. The challenge this creates is many retirees will spend as many years drawing down retirement assets as they did accumulating them. Fidelity points out that these younger, more recent retirees are more active and diverse in their activities than previous generations and thus spending more.

FACTORS AND TRENDS TO CONSIDER

In determining requirements in retirement, other factors must be considered.

Health Care Costs – It seems impossible today to pick up the newspaper and not see an article about the rising costs of health care. As our population ages, this issue becomes more prominent. Reasonable insight tells us that future generations of retirees will be spending a greater percentage of their retirement income on health care than previous generations.

Underfunded Pension Plans – Roughly 1/4 of the Canadian work force is a member

of a pension plan. Many of these, including virtually all municipal, provincial, and federal employees are members of a defined benefit pension plan. As a result of low interest rates, under performance of the stock markets in recent years and more members retiring early, many of these plans are under funded. As a result, many pension plans have reduced benefits. The employee who is anticipating a pension fully indexed with inflation at retirement may find themselves disappointed.

Tax Rates – Federal and provincial income tax rates have declined substantially in the past decade. With health care costs increasing as noted earlier and government debt around the globe increasing at dramatic rates, it would be prudent to suggest that further tax cuts will become less likely. Without sounding alarmist, it would also be reasonable to assume that tax rates may have to go up as part of government’s strategy to reduce debt.

The Home as an Income Source? – Houses don’t do terribly well as generators of retirement income. You can sell part of your investment portfolio, but not part of your home. While you can borrow against the value of your home via a bank line of credit or reverse mortgage, you start to run up a bill for interest on the loan. That leaves you with the option of “downsizing”. The problem is that downsizing the physical size of where you live does not necessarily mean downsizing the price, though it is certainly possible to do so. Also, it likely involves moving out of a neighborhood you have become attached to. Finally, retirees wishing to leave an estate tend to look on drawing home equity with less enthusiasm than those less concerned about leaving an estate.

SO HOW MUCH TO SAVE?

Again, there is tremendous disparity in the answer. For the couple comprised of two teachers with full pension benefits, the savings requirement will be close to zero. For the rest of us, Russell Investments’ Rule of \$20¹ provides a helpful equation that takes into account inflation, longevity risk and market volatility. The basic rule states that every \$20 of retirement savings will generate \$1 of pre-tax retirement income. For example, accumulated savings at retirement of \$500,000 will generate \$25,000 annually, increasing at 3%. The formula utilizes the following assumptions:

- Annual payout indexed at 3%.
- Asset allocation post retirement is 35% equity and 65% fixed income.
- Couple, ages 60 and 57.
- The \$20 is within an RRSP account.

No single rule can be general enough to cover an entire targeted population. However, the above rule provides a relatively accurate proxy for how much must be accumulated

to provide a desired cash flow in retirement. Finally, it is important to keep in mind that the Rule of \$20 does not include pensions, government benefits and any other sources of income.

WHAT DO CURRENT RETIREES SAY?

There is no better teacher than experience. Russell Investments in conjunction with Harris / Decima Research, recently conducted a study to determine how recent retirees were faring. The results were largely positive and served to provide future retirees with optimism in regard to their retirement. Results of the survey outlined the following:

- 10+ years prior to retirement, 58% of Canadians say they are concerned about the possibility of outliving their money. This drops to 38% when retirement arrives and 18% a decade after retirement.
 - More than half of pre-retirees expect to work part time in retirement, yet less than a quarter of retirees actually do so.
 - 10+ years prior to retirement, only 56% of Canadians say they expect to experience feelings of happiness, freedom and relief during retirement but almost 90% of actual retirees report experiencing these feelings.
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SO WILL WE BE OKAY?

There is no “cookie cutter answer” to the questions of “how much do I need in retirement?” and “how much do I need to save?” While rules of thumb will help, individual needs and retirement plans will vary from person to person. Further, every generation of retirees face a differing set of circumstances. Many of our Guardian subscribers have gone through a detailed Retirement Income Projection Analysis with their advisors to pinpoint more accurately how their retirement will look financially, and we encourage anyone uncertain about their financial landscape in retirement to do the same. Finally, based on the recent research conducted by Russell, perhaps we can ease some of the financial anxiety concerning retirement as results outlined earlier show that once in retirement, stress concerning finances seems to reduce.

NEW WEST VANCOUVER OFFICE

Our North Shore clients should note that effective May 1, we are re-locating the office two floors down to suite #200. Our new address will be #200 – 100 Park Royal South, West Vancouver. (by appointment only).

¹ Developed by Russell Investments Canada

**REGISTERED RETIREMENT INCOME FUND (RRIF)
STATUTORY MINIMUM MONTHLY INCOMES BASED ON \$100,000
COMMENCING ONE MONTH FROM ISSUE**

Best Current Rate: 4.15%

Age	1st Year	TOTAL PAYMENTS	A R.R.I.F. can also be structured to pay a level income for a shorter period. Based on current interest rates, \$100,000 will produce the following monthly income. For 5 years:\$1821.00 For 10 years:\$1002.00 For 15 years:\$745.00
		TO AGE 100	
55	\$239.00	\$292,144.00	
60	278.00	248,267.00	
65	334.00	212,114.00	
69	398.00	187,813.00	

**MONTHLY ANNUITY INCOMES COMMENCING
ONE MONTH FROM ISSUE BASED ON \$100,000**

Age	LIFE (Payments cease at death)		LIFE 10 Year Guarantee		JOINT LIFE 10 Year Guarantee
	MALE	FEMALE	MALE	FEMALE	MALE & FEMALE
	55	\$577.75	\$530.85	\$566.71	\$526.01
60	625.82	577.66	607.05	568.61	522.03
65	698.54	630.08	661.87	612.75	560.54
71	829.09	724.54	751.21	679.36	626.77

The material contained herein is intended to provide the clients of Solguard Financial Ltd. with advice and guidance of a general nature, and is believed to be accurate at the time of writing. However, due to rapid changes in interest rates, market conditions, tax rulings and other investment factors, readers should seek further advice specific to their situation, before proceeding with investment action.



Peak Securities Inc. is a member of the Canadian Investor Protection Fund.

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