

# Saving for Retirement



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April 2009

Although most of us recognize the importance of sound retirement planning, few of us embrace the nitty-gritty work involved. With thousands of investment possibilities, complex rules governing retirement plans, and so on, most people don't even know where to begin. Here are some suggestions to help you get started.

## **Determine your retirement income needs**

Some experts suggest that you need anywhere from 60% to 90% of your current income to enable you to maintain your current standard of living in retirement. But this is only a general guideline. To determine your specific needs, you may want to estimate your annual retirement expenses. Use your current expenses as a starting point, but note that your expenses may change dramatically by the time you retire. If you're nearing retirement, the gap between your current expenses and your retirement expenses may be small. If retirement is many years away, the gap may be significant, and projecting your future expenses may be more difficult. Remember to take inflation into account. The average annual rate of inflation over the past 20 years has been approximately 3%. (Source: Consumer price index (CPI-U) data published by the U.S. Department of Labor, 2008.) And keep in mind that your annual expenses may fluctuate throughout retirement. For instance, if you own a home and are paying a mortgage, your expenses will drop if the mortgage is paid off by the time you retire. Other expenses, such as health-related expenses, may increase in

your later retirement years. A realistic estimate of your expenses will tell you about how much annual income you'll need to live comfortably.

## **Calculate the gap**

Once you have estimated your retirement income needs, take stock of your estimated future assets and income. These may come from Social Security, a retirement plan at work, a part-time job, and other sources. If estimates show that your future assets and income will fall short of what you need, the rest will have to come from additional personal retirement savings.

## **Figure out how much you'll need to save**

By the time you retire, you'll need a nest egg that will provide you with enough income to fill the gap left by your other income sources. But exactly how much is enough? The following questions may help you find the answer:

- At what age do you plan to retire? The younger you retire, the longer your retirement will be, and the more money you'll need to carry you through it.
- What kind of lifestyle do you hope to maintain during your retirement years?
- What is your life expectancy? The longer you live, the more years of retirement you'll have to fund.
- What rate of growth can you expect from your savings now and during retirement? Be conservative when projecting rates of return.
- Do you expect to dip into your principal? If so, you may deplete your savings faster than if you just live off investment earnings. Build in a cushion to guard against these risks.

## **Build your retirement fund: Save, save, save**

When you know roughly how much money you'll need, your next goal is to save that amount. First, you'll have to map out a

savings plan that works for you. Assume a conservative rate of return (e.g., 5 to 6%), and then determine approximately how much you'll need to save every year between now and your retirement to reach your goal. The next step is to put your savings plan into action. It's never too early to get started (ideally, begin saving in your 20s). To the extent possible, you may want to arrange to have certain amounts taken directly from your paycheck and automatically invested in accounts of your choice (e.g., 401(k) plans, payroll deduction savings). This arrangement reduces the risk of impulsive or unwise spending that will threaten your savings plan. If possible, save more than you think you'll need to provide a cushion.

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