Longview "INSIGHTS" Newsletter

"helping clients grow, protect and distribute their wealth"

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This is a report published by Five Star Wealth Manager Keith Tufte of Longview Wealth Management, LLC with insights on investing and wealth management.*

INVESTING QUOTE OF THE MONTH:

"Build a pile of savings, keep adding to it, and NEVER touch the pile.
A penny saved is a penny and a half earned (after taxes)." – Keith Tufte

ARE YOU SAVING ENOUGH? FIDELITY SAYS YOU NEED 8X SALARY

Are you saving enough? Most Americans are not saving nearly enough for a comfortable retirement. Fidelity Investments recently came out with some guidelines to help people see how much they need to save to be successful in retirement.

FIDELITY'S RECOMMENDATIONS:

Age	Annual Savings as % Salary	Total Savings as A Multiple of Salary
25	6%	
35	15%	1X
45	15%	3X
55	15%	5X
67	15%	8X

Fidelity makes a number of assumptions in this analysis including: the goal to have 85% of pre-retirement income in retirement, Social Security still exists in the future at today's payout rates, you earn 5.5% investment returns per year, you save consistently without interruption, you start saving at age 25, you retire at age 67, and you live to be 92 years old. Is 8X enough? For many it is not. Financial planning experts used to say 10% of savings per year over the course of your career was enough, then they went to recommending 12% of salary per year in savings, and now are going to 15%. If you wait to age 40-45+ to start saving, the percentage of savings required is obviously higher.

WHY DO PEOPLE NEED TO SAVE SO MUCH NOW?

1. Very few people have pension plans any more.
2. Current low interest rates create lower returns and income from bonds and cash (vs. history).
3. People are living longer, and have more years to support themselves in retirement.
4. Medical costs keep increasing, and medical costs can be expensive for retirees.
5. Social Security and Medicare may be less generous, means tested, or bankrupt in the future.

WHAT ARE THE KEYS TO A SUCCESSFUL SAVINGS PLAN?

1. **Start saving at a young age.** The power of compounding can then work for you for decades.
2. **Save a lot.** Most people need to spend less, and save much more than they are now.
3. **Save consistently. Don't ever stop saving.** Don't stop saving because the stock market drops 20% and it seems too scary to invest at the time. Keep saving and keep investing.
4. **Automate your savings plan.** Have the money taken out of your paycheck automatically so you don't even see the money, and you won't miss it. Save first, spend what's left.
5. **Use tax advantaged investment vehicles** (such as 401k, IRA, SEP-IRA, etc.) and your company 401K match if it offers one. Max out the company match.
6. **Increase your savings rate** 1% per year until you get up to the 15% target (or more). You will barely notice the difference each year.
7. **Invest in a diversified portfolio.** While accumulating savings, invest in a diversified portfolio of mostly equities and stay there.

RETIREMENT RULES OF THUMB

Rules of thumb are helpful to many people because they simplify the process and give them a way to easily understand things and get started. The first two retirement rules of thumb regarding retirement are 1) you are likely to need about 85% of your pre-retirement income to live on in retirement and 2) the 4% rule: you can spend about 4% of your portfolio each year in retirement and be confident

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you will not run out of money over the course of a normal 25-30 year retirement. We think these are pretty good rules of thumb. Rules of thumb are generalizations and can be helpful, but it is much better to have a customized long-term financial plan based on your own personal situation and assumptions. Every family is different.

THE FIDELITY 8X RULE OF THUMB IS DANGEROUS

Unfortunately, we think the Fidelity 8X rule of thumb is dangerous and misleading, and will not be nearly enough for most people. The Fidelity rule works reasonably well for a couple making $50,000 per year, with the critical assumption that Social Security and Medicare will remain as generous as they are now. That may be a shaky assumption. The Fidelity 8X rule is seriously inadequate for higher income families. **We think higher income families will need more like 20 times (not 8 times) their final salary to enjoy retirement at 85% of their pre-retirement income.** Higher income families are also the ones most likely to have their Social Security and Medicare benefits cut back in the future by "means testing." If you plan to retire before age 67 like many people do, you will likely need an even higher multiple than 20 times since you will have more years to support yourself in retirement.

> *Let's take a simple example to show how the Fidelity 8X rule is inadequate, while using the 4% rule mentioned above. Assume a couple has a pre-retirement income of $200,000 per year, and they are set to get $23,000 a year in Social Security at retirement (age 67). Using the Fidelity 8X rule, the couple should aim for a portfolio size at retirement of $200,000 times eight or $1.6 million. If we apply the 4% rule to this $1.6 million, it says they can spend $64,000 of this portfolio per year in retirement and be confident they will not run out of money in old age. If we add the $23,000 in social security to this $64,000 in portfolio spending the couple will have total retirement income of $87,000 per year (pretax). $87,000 in retirement income is only 44% of their pre-retirement income of $200,000, not the 85% Fidelity is shooting for. Most people would not find a big 50%+ drop in retirement income a success. The Fidelity 8X saving rules of thumb may be a good starting point or a minimum initial goal for the average American who is behind in their savings plan. The 8X rule should be viewed as seriously inadequate for higher income families or couples with only one future social security income stream. We also recommend people have a plan to pay off their mortgage by the time they retire.*

It is somewhat dangerous to use a simple multiple of income as your guide. There is no one-size-fits-all number. Retirement costs vary considerably from one part of the country to another. If you are going to use a multiple of something to target the size of your retirement portfolio, it should be a multiple of your annual spending not your annual income. What is your current net worth (excluding your primary residence) divided by your annual spending? That is a relevant number, and the closer you can get that number to 20+ by the time you retire the better. If that number is over 25, you are in very good shape.

The large numbers for required retirement portfolio size can seem impossible for many people. There are only a few things you can do about it; earn more, save more of what you earn, work longer, or reduce your expected standard of living in retirement. Or do a combination of all four.

OUR APPROACH

We do long-term customized financial planning for our clients out to age 90+. Our models consider inflation, college costs, Social Security, pensions, inheritance, sale of a business, purchase/sale of a second home, savings levels, gifting, and other factors that each family may have. The long-term financial plans we do for clients help them feel confident they are saving enough for retirement, they know what their safe target level of spending will be in retirement, and they will not run out of money in their later years. Our plans also help guide estate planning needs and legacy gifting goals. We encourage you to increase your savings levels if you are not saving enough, and to talk to us to see how we might be able to help.

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