Do I Have Enough to Retire?

Four pieces of information are necessary to determine whether you can retire comfortably: (1) retirement living expenses, (2) amount of fixed income expected, (3) dollars currently invested, and (4) the real investment growth rate you expect. Once this information is collected, a simple mathematical formula can tell you if you've met your goal or how much you have left to go.

1. Living Expenses
You know what your current income is. How much less or more will you need to live as you want to after you retire? If your home will be paid off soon, will your living expenses go down at that time, or will you instead spend that money on another purpose? Don't forget to include any new post-employment expenses you may incur, such as health insurance premiums or increased spending on hobbies and travel. Be sure to include federal and state income taxes in your living expenses.

[A] The income (pre-taxes) we will need each year to meet our living expenses is $____________

2. Fixed Income
Will you or your spouse receive a pension after retirement? If so, how large? How much social security will you receive each month? Do you have any investments that pay you a fixed income (annuities, treasury bonds, trust funds, etc.) that you plan to continue owning? If so, how much income do these provide?

[B] The annual income we can expect from fixed sources is $______________

3. Retirement Savings
How many dollars do you have invested in stocks, bonds, mutual funds, CDs, money market accounts and savings accounts? If you will receive a lump sum from your employer as your retirement package, how large? If you have stock options, what value would they have if you sold them today? What is the value of your real estate investments, excluding your main home? What is the value of your other investments? (If you included the income from an annuity or bonds in your Fixed Income calculation, do not include the value of that investment in Retirement Savings. If you plan to sell those investments to raise cash to invest, do include their value under Retirement Savings, but not also under Fixed Income.)

[C] The current dollar value of our retirement investments is $______________

4. Real Investment Growth Rate
The Real Investment Growth Rate is the rate at which you can expect your invested dollars to grow after allowing for inflation. As the rate of inflation rises and falls, investment returns also rise and fall to compensate, so that real investment returns (after adjusting for inflation) remain basically steady. The level of risk in a specific investment explains why it earns higher or lower returns, on average, than does another investment.

Over an investment cycle of 3 to 8 years, a properly diversified investment portfolio should yield, on average, at least 5% more than inflation each year, using low risk (low volatility) investments. (Actual earnings each year will vary, but average out to 5% more than inflation.) A portfolio with moderate risk should yield at least 8% more than inflation.

If you prefer low-risk investments, assume a Real Investment Growth Rate of 0.05. If moderate risk is acceptable to you, assume a Real Investment Growth Rate of 0.08.

[D] The appropriate Real Investment Growth Rate for our investments is _____

Calculating the Answer
Simply put, in order to retire comfortably, you must have enough retirement savings that their annual growth is sufficient to pay that part of your annual living expenses which is not covered by

your fixed income sources. This leaves your initial Retirement Savings untapped, so that it can continue supporting you indefinitely, assuming that Living Expenses and Fixed Income both keep pace with inflation. Your initial savings also provide a cushion in case of extended market downturn or unexpected major expense (however, if such an event occurs, you may need to adjust your living expenses to compensate for the loss of investment principle).

To calculate whether you have enough assets to retire, subtract your annual Fixed income [B] from Living expenses [A]. Divide this number by the Real Investment Growth Rate [D]. If the result is equal to or greater than your Retirement Savings [C], then you should be able to comfortably retire today.

If the result is less than your Retirement Savings [C], then you need to change one or more of your expectations. This might require you to:

- Continue working until your retirement savings are greater.
- Supplement your retirement income by working several years part-time at something you enjoy.
- Scale down your expected living expenses by giving up or reducing a luxury.
- Accept higher market risk, so that your savings will grow faster.
- Move an investment (such as an annuity) from Fixed Income to Retirement Savings by cashing it out, so that those dollars can be invested for a higher return.