

Maximising your income in retirement

On average, Australians spend around 25 years in retirement. That's more than half the time many of us spend in the workforce. While many people can tell you what type of lifestyle they want in retirement, they may not know if they have enough money to achieve this lifestyle or how long their money will last.

Having a modest or comfortable retirement will depend not only on your day-to-day expenses but also on the activities or travel plans you might want to undertake and where you want to live.

If you are seeking a comfortable retirement, a recent survey* stated that a single person will have an annual shortfall of \$22,299.16 after the full age pension is taken into account (as shown in the following table). For couples, this increases to \$28,115.88, which means retirees need to fund the shortfall from private and superannuation savings.

Table 1 – A modest or comfortable retirement*

	Modest (per week)	Comfortable (per week)
Singles	\$414	\$764
Full age pension	\$335.45	\$335.45
Shortfall	\$78.55 or \$4,084.60 pa	\$428.83 or \$22,299.16 pa
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Couples	\$599.56	\$1,046.39
Full age pension	\$505.70	\$505.70
Shortfall	\$93.86 or \$4,880.72 pa	\$540.69 or \$28,115.88 pa

* Source: Westpac-ASFA 2010, December Quarter 2010 and age pension rates as at March quarter 2011.

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The following are five areas that you need to consider to help maximise your income in retirement.

1. How much capital do you need in retirement?

The answer depends upon:

- your personal circumstances
- your desired level of income (including standard of living)
- how long you think you will live.

At present, the average standard wage¹ is \$66,976 and commonly, people retire on 65 per cent of their pre-retirement income. Based on this, the average Australian will need \$43,535 pa in retirement. As an example, Mark is single and aged 60. How much capital will he need in retirement? The answer is \$482,000² based on his life expectancy of 22.7 years.

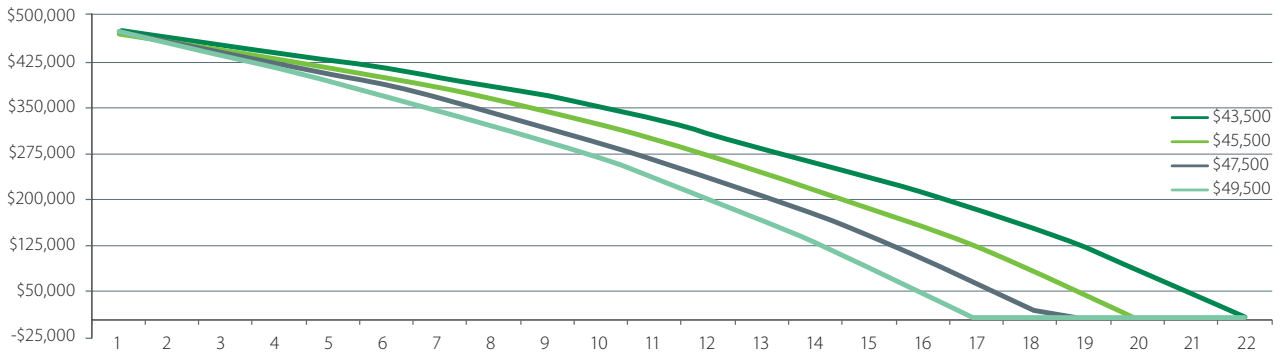
If Mark's annual living expenses increased, for whatever reason, by \$6,000 to \$49,500 pa, his capital will run out after just 17 years instead of the planned 22.7 years (as shown in graph 1). That will leave him with only the age pension income to live on for the remaining 5.7 years.

¹ Average Weekly Earnings, Australia, February 2011 taking into account both males and females.

² Assuming an earning rate of seven per cent (after fees).

How long would your money last? Different levels of living expenses.

Graph 1



Assumptions

- Male aged 60 and life expectancy of 22.7 years
- Standard wage \$66,976 pa
- \$43,500 pa living expenses
- Investment return of seven per cent pa (after fees).
- Capital of \$482,000
- Ignores age pension entitlements

2. How long will you live in retirement?

No one really knows the answer to this question. However, the Government has statistics to help provide us with a guide which can be found in the Australian Bureau of Statistics' website www.abs.gov.au

In the case of Mark, his life expectancy may be 22.7 years when he retires at the age of 60, but as he gets older, the life expectancy does not reduce in parallel with each year. In fact, when he turns 65, his life expectancy will be 18.54 not 17.7 (22.7 years – 5 years).

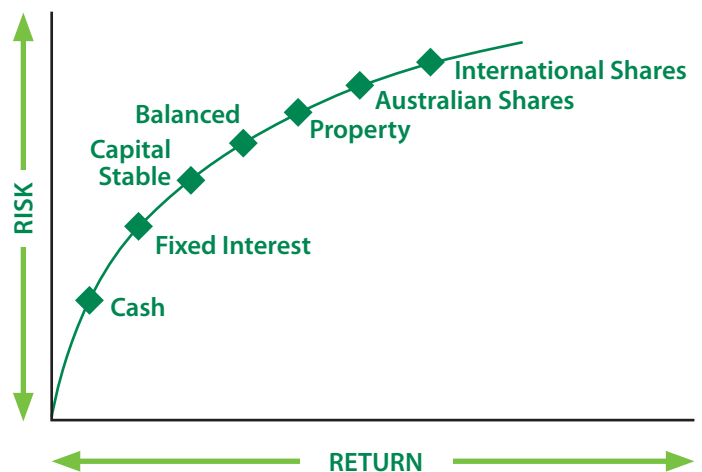
Females live longer than their male counterparts and their life expectancies are much higher. For example, a 60 year old female has a life expectancy of 26 years.

As a rule of thumb, it is important to plan for longer than your life expectancy. Medical advancements and increases in living standards mean that you might well outlive the life expectancy indications.

3. How will your investment strategy impact your retirement?

An integral part of maximising your income during retirement will be your investment strategy. This could include investing into asset classes such as fixed interest, property, Australian shares and international shares. It is essential to have an investment strategy which combines the different asset classes and takes into consideration your tolerance to risk.

Investing only in cash or fixed interest could mean your desired income during retirement may not be possible due to lower long-term investment returns in comparison to Australian shares. Investing in growth assets (shares and property), on the other hand, involves greater risk but could mean higher returns which will fund a higher income in retirement. It is important to bear in mind that the share market could produce a negative return.



4. The longevity of your capital will depend on your investment returns

If we revisit the example of Mark, the higher the investment return, the longer his capital will last during retirement. This is evident in the following graph which demonstrates different levels of investment returns. Achieving an investment return above seven per cent per annum means his capital will last past his life expectancy of 22.7 years.

This might sound good but having an appropriate investment strategy with an acceptable level of risk combined with defensive assets (such as cash or fixed interest) is essential. Seeking advice from a financial adviser will assist you with your investment strategy whilst maximising your income during retirement.

5. What sources of income will be available?

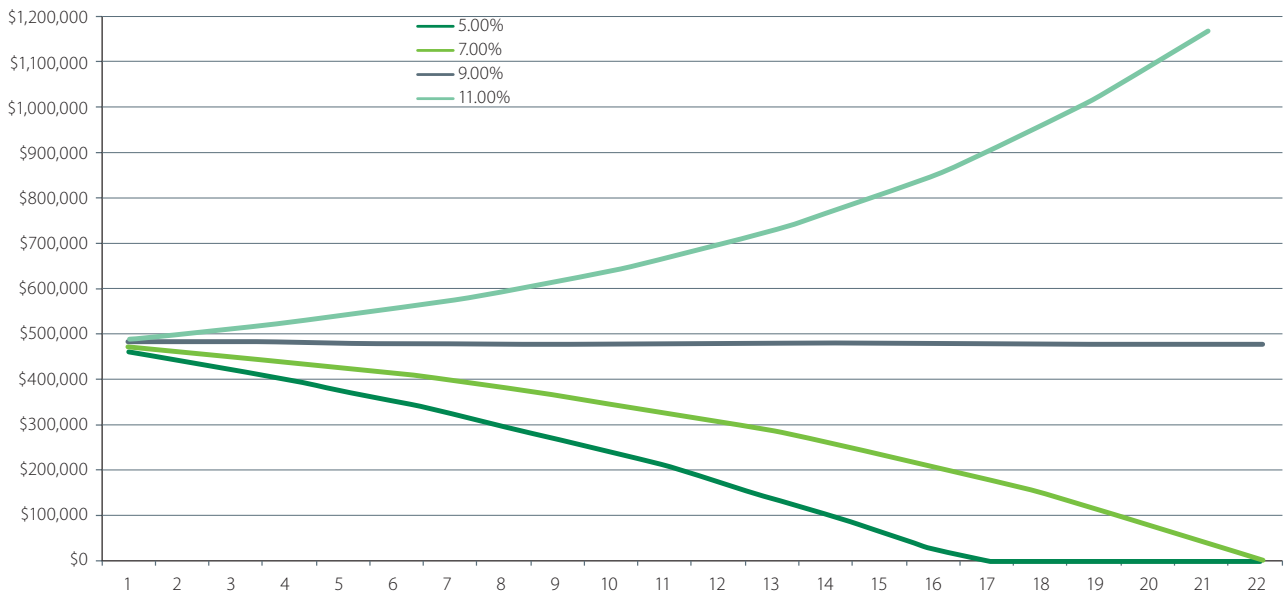
Your sources of income during retirement can come from your private savings (such as shares or bank accounts), superannuation savings as a regular income stream and the age pension.

Relying solely on the age pension will provide you with a very modest lifestyle in retirement. To achieve a comfortable lifestyle, you will need an appropriate level of private and superannuation savings to supplement the age pension. The structure of your savings is critical, as it can impact your eligibility for the age pension.

Speak to your financial adviser about how to maximise both your savings and your entitlement to the age pension; and to achieve a comfortable standard of living during retirement.

How long would your money last? Different levels of investment returns.

Graph 2



Assumptions

- Male aged 60 and life expectancy of 22.7 years
- Standard wage \$66,976 pa
- \$43,500 pa living expenses
- Investment return of seven per cent pa
- Capital of \$482,000
- Ignores age pension entitlements

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