Chapter 22

THE 3 PILLARS OF SPENDING DURING RETIREMENT

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22 THE 3 PILLARS OF SPENDING DURING RETIREMENT

Pillars of Spending during Retirement

Blind Withdrawal

Increase annual expenses withdrawal according to inflation rate

Blind Withdrawal

The first thing that you want to talk about is blind withdrawal. It is a conventional retirement plan or calculator that is built on assumptions that you incrementally withdraw your annual expenses during your retirement years according to the inflation rate to sustain your retirement. But this is absolute nonsense because nobody lives this way and we don't have to retire to know this.

Adjust spending based on our income and economic condition

Blind Withdrawal

Inflation Rate = Lifestyle

In your life, whether we are retired or not, we adjust our spending based on the success or failure of our careers and the income generated by our job or business. So for example, if I was to lose my job today and no retrenchment comes, am I going to increase my expenses until if I don't have a job

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because there's no money inflow? In the post-retirement scenario, the same concept applies. Like why retirement should be any different.

When retirement nest egg takes a hit, it is not sensible to still increase your retirement expenses

Blind Withdrawal

Inflation Rate = Lifestyle

Now if your retirement nest egg got hammered by negative investment returns in the first few years of the critical retirement. Are we still going to increase our annual expenses blindly like a robot year after year during that period, even though our retirement nest egg shrinks? Now of course not that would be so foolish. We would reduce our spending. It's just a realistic thing to do when times are bad; we reduce our spending based on our economic conditions.

When times are bad, we reduce or be more vigilant of our spending

Blind Withdrawal

Inflation Rate = Lifestyle

Prudence is the common sense to do. Common sense in investment and finance is not so common. This kind of thing is rarely mentioned in conventional retirement planning because it's so difficult to put that into the model. But in retirement, we want to put this aspect into our model. The point is withdrawing incrementally intended inflation rate over the years. It cannot be applied blindly.

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Living Expenses

Increase your living expenses or withdrawal per inflation rate

Living Expenses

The second thing that we have to debunk is that living expenses. Now conventional retirement plan or financial plan says that over year after year, you increase your living expenses, and hence your withdrawal to sustain your living expenses increase year over year. The inflation rate increase will increase just to sustain your lifestyle.

Do retirees really have a need to increase expenses year after year?

Living Expenses

Do retirees spend more in their retirement until the day that they die? Now we are not talking about medical expenses and we exclude medical expenses over here. Now it’s very likely that retirees reduce their living expenses as they age. Now in the early years of your retirement, they still have the health, they have the energy to use, the passion to go to travel, and enjoy life if they haven’t done so pre-retirement. So they tend to spend more.

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Declining energy levels translate to lower living expenses

Living Expenses

But as they age, their health and energy declines. They won't be doing so extensive traveling much in the later years of retirement and that relates to living expenses.

Compounding

Your spending pattern is of the utmost importance in retirement

Compounding

It's no Magic anymore

The next thing is compounding. In finance in this case, even if a small percentage of the return value is spread over a long period you can enjoy the magic of compounding over the years. Post-retirement years as compared to pre-retirement shock. So the magic of compounding is not that magical anymore. The truth is less relevant post-retirement compared to 10 or 20 years pre-retirement because the retirement time horizon is usually related to shock the post-retirement years, two things are more important than anything else that is your spending and the total savings that you have in your retirement nest egg.

If there is still some money inflow into your retirement nest egg, what is the amount that you saved and reinvested? So this is the main issue here and it takes down to how little someone can be happy

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spending. If you can keep yourself happy living two thousand a month then, by all means, that's good but if you're only happy by actually living like eight thousand a month with a luxurious lifestyle. Then if you don't have a sizable retirement nest egg, the problem is that you exhaust your retirement fund pretty soon. That is one thing to keep in check during retirement.

It is not sensible to have
0 growth in your retirement nest egg

No Growth?

Bond Funds? Really?

Last but not least is the fact that in retirement planning they say that after retirement your risk and your risk appetite go down. So that's why you invest in something that gives a lot lower risk like a bond fund. If you have bonds of what is you put in like nine - ten thousand in a bond and it's a 10 years bond but you get at the end of 10 years, ten thousand your principal right. So there's no growth in bond funds. You only get your consistent income but there is no growth in your capital. So the recommendation of bond fund for long term post-retirement investment if, you have still like 10 or 20 years to retire. Let's see if you have an early retirement of forty-five years of age and a life expectancy of 80 years old. You still have forty years to go in your retirement years and you should check your capital if you have direct property investment. Capital appreciation in property is capital growth as well as providing income to rental. You have to invest in stocks and real estate investment trusts, stocks that give you capital appreciation income in terms of stock price appreciation, besides the very consistent dividend income that you receive from it. No growth for your retirement is absolute nonsense.

Possibilities

Not Possible in
Conventional Retirement Planning

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There are so many flexible conditions and possibilities that you can consider where you actually can manage your post-retirement plan in management. These are the things that if not shown, rarely demonstrate in conventional retirement planning or management.

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