
How much
MONEY
Do I Need
TO RETIRE?



TODD TRESIDDER

Praise For

How Much Money Do I Need To Retire?

This is a great little book to get you on the right track for your retirement goal. It's concise and to-the-point. I recommend it.

David Bates, Publisher – ProtectYourNestEggInRetirement.com

When you finish this book you realize there are many options and alternatives to have the lifestyle and retirement that works for you. It is a practical, hands-on book that cuts through all the clutter. Not only do I have a better understanding of the retirement planning process, I also have renewed hope, energy, and optimism that I can reach my retirement goals in 7 years or less.

D.J. Richoux, Business Owner – Vancouver, Canada

When I hit the “7 Questions” it was like 20 years of investment advice came together. You had me hooked, and the rest of the book was a page turner that I couldn't put down. By the end I realized I could retire now if I really wanted to—22 years earlier than conventional retirement planning.

Dan Cosgrove, CEO – Mercantile Systems, Inc.

Before reading How Much Money Do I Need To Retire? I naively thought this question had a simple answer. Now I understand the

many variables that can affect the answer and have a broader view of what retirement can actually look like if you think outside the box. The clarity I got from reading Todd's "Three Rule System" gave me a simplified concept of retirement that actually makes more sense than trying to factor in so many unforeseen and unpredictable variables.

Lisa Cary – Hawaii

This is a great book to get you thinking. The first half helps define the basic concepts while the second half helps even the expert work out real numbers and come up with good workable projections... By applying some of the non-conventional methods in this book you may even be able to retire sooner than you think.

Tim McMahon, Editor – InflationData.Com

Your information cuts through the usual hype, misinformation, and general rip-off artists who disguise themselves as financial planners. You are the first one who has given me an honest appraisal and understanding of this subject. Kudos to you!

Don Hazzard – Hawaii

The information in this book provides the best and most comprehensive answer to the "How Much Do I Need To Retire" question that I've ever read.

Larry C. Weber – Lacey, Washington

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Introduction

“The ultimate security is your understanding of reality.”

H. Stanley Judd

Traditional retirement planning has failed.

- According to the New York Times, 75% of Americans have less than \$30,000 in their retirement accounts, and 49% of middle-class workers will retire poor or near poor.
- According to Hewitt Associates, 4 out of 5 workers will fail to meet all their financial needs in retirement.
- Employee Benefit Research Institute reports that 81% of workers nearing retirement age (45 or older) have less than \$250,000 in savings and an astounding 48% have accumulated less than \$25,000 as they approach retirement.
- Only 14% of American workers are confident they will have enough money to retire according to the annual Retirement Confidence Survey.

The evidence is overwhelming that something is wrong with traditional retirement planning. It's an old world model in need of a major facelift.

The problem is inherent in how the retirement system is designed—it's not realistic. The skills and knowledge required to successfully execute a traditional retirement plan are beyond most worker's abilities:

- You must voluntarily save a significant portion of your income with discipline throughout your career (8%–30%, depending on the age you begin saving).

- You must develop sufficient investment expertise to implement smart asset allocation and investment decisions.
- You must know in advance when you and your spouse will die to know how much savings are required.
- You must know in advance when you will end work—either voluntarily, due to sickness, or possibly because of lay-offs out of your control.
- You must know what the future inflation rate will be over your remaining life (even though trained economists can't accurately predict this number even one year in advance).
- You must know what your investment portfolio will return over your remaining life.
- You must be disciplined enough to never raid your retirement nest egg when adversity strikes like getting laid off, health problems, kid's college, or getting divorced.
- And then, to top it all off, you're supposed to manage your retirement savings so that you spend your last dollar as you exhale your last breath.

Yeah, right! No wonder most workers are failing at retirement planning.

It is an almost unbelievable list of skills and knowledge that few (if any) workers possess. It requires you to have the savings discipline of a celibate monk living in a brothel, investment skills that exceed most pension and mutual fund professionals, and the actuarial skills of an insurance expert. **Those sound like pretty demanding standards for someone who aspires to quit work.**

There must be a better way, and that is what this book attempts to show you.

I “retired” back in 1997 at the ripe old age of 35 and fumbled with the traditional models making my share of mistakes to learn what works, what doesn’t, and why. I’ve spent more than two decades studying retirement planning through popular books and the latest academic research. Trust me, there’s more to the “how much to retire” question than is commonly understood. It’s a controversial subject where even the experts can’t agree on the best solution.

The problem is obvious once you see it. It’s baked into the cake of the traditional retirement planning model. To estimate how much money you need to retire, the traditional model requires you to input a laundry list of assumptions about things you can’t possibly predict 20–50 years into the future. It’s impossible. **That is the core problem and there’s no real solution.**

Just look at that list of skills and knowledge required. Nobody knows when they will die, what inflation will be, or what their investment portfolio will return. It’s not only impossible—it’s ridiculous.

The future is not predictable for even a few years, and 20–50 years into the future is a gross approximation at best. It’s classic “garbage in equals garbage out.” The need to predict the future is a fundamental, inescapable limitation to the conventional retirement planning process that converts the precise façade of science with all the computerized retirement calculators into the vagary of art.

The good news is that I have figured out workable solutions that’ll be explained in this book. Retirement planning done right is built on three separate models. I want you to have a quick overview of all three models now because this overview sets the context for everything you will discover in this book:

1. The first model is conventional retirement planning. **It’s dangerously misleading because it appears scientific, but it’s actually a fiction based on flawed premises.** It works acceptably well for retirements up to 20–25 years in dura-

tion because it's built on spending the principal in your savings account, but it runs into serious problems when your retirement time horizon exceeds 30 years. The first half of this book explains the problems with the traditional model with workaround solutions so you fully understand how to apply this model wisely

2. The second model focuses on the increasingly important role creative lifestyle planning plays in modern retirement planning. The New Retirement is redefining the word "retirement" and completely changing the math behind how much money you need as a result. This section provides powerful planning tools that can help you close the savings gap or retire with greater financial security several years earlier than expected.
3. The final model in this book presents an entirely different approach to understanding how much money you need to retire **based entirely on cash flow instead of assets**. It's valid for retirement time horizons exceeding 30 years, eliminates any need for difficult assumptions, simplifies, and is more robust (but also more difficult to attain).

In other words, this book will show you three different ways to answer the "how much to retire" question that flow together to form a composite picture: the traditional asset based approach with all its warts and blemishes, the creative solution where retirement is redefined thus changing the financial picture entirely, and the cash flow solution. I find it helpful to think of each of these three solutions as providing different yet compatible viewpoints on the "how much to retire" question.

The integration of these three approaches is what gives you a complete picture. Any one model without the other two is a dangerous half-truth. You'll want to understand how the composite picture fits together because each of these three models builds on insights from the previous model. They connect. When you put them together,

you'll fully understand how to build a retirement plan that perfectly fits your personal situation. It's a very empowering solution.

I've been teaching this subject to financial coaching clients and living the answers in my own retirement since 1997 and I can tell you that this is the definitive solution. Nothing more is needed. It's what works in practice, even if it doesn't appear as neat and tidy as the magic number spewed from a retirement calculator.

Before I show you how all this fits together, starting with the first model, it's important that I warn you about a few common potholes that readers sometimes fall into so that you don't make the same mistake.

The first pothole is to confuse the simplicity of how I explain these complex topics as synonymous with an incomplete or technically unsophisticated answer. Readers of my *4% Rule and Safe Withdrawal Rates* book (www.amzn.to/MZrGgM) know I'm deeply versed in the rocket science of retirement planning. I've been published in a peer review academic journal and readers familiar with that work expect math equations and elaborate statistical proofs.

The truth is that all of that stuff doesn't work for figuring out how much money you need to retire. The complex equations and technical jargon get in the way of the simple truths that truly govern what does work. For that reason, I intentionally don't waste your time on any of the fancy mumbo-jumbo so we can focus on the few actionable ideas that actually produce workable results. As Pareto's Law implies, 80% of the details will produce 20% of the results. This book focuses on the 20% that makes or breaks 80% of your results. Paying attention to the critical 20% is what will secure your financial future. Don't make the mistake of getting lost in unnecessary details.

The next mistake nearly everyone makes when calculating their retirement number is to pursue additional data in a futile attempt to increase accuracy. I know this will sound counterintuitive to you, but it actually doesn't work that way.

The truth is that there are just a couple of key numbers that will determine your success or failure in retirement planning. The rest are details that confuse more than they clarify.

I'm always amazed when self-proclaimed experts complain that I didn't include separating spousal assets, changing tax rates after retirement, or whatever pet peeve they choose from the millions of details intentionally excluded from this book to make the primary message clear. If you're one of those people, then please pay special attention to the second section of the book where I take you through an exercise so you can prove to yourself what key numbers make or break your financial security. I don't want you to fall prey to the intellectual trap of pursuing increasing detail in a futile attempt to increase accuracy. The simple stuff is what works in practice.

The final mistake is to not be clear on the focus of this book. I've purposely excluded topics like long-term care insurance, strategies on when to begin Social Security benefits for maximum payout, Roth conversions, IRA rollovers, asset allocation, and Medicare supplemental insurance because this book is exclusively about how much money you need to retire. It's not the complete guide to retirement planning. Sure, these topics are important and valuable, but they would detract from the book's focus (which is complicated enough without adding distractions).

Okay. So now that you know the three models we will cover in this book and the three common potholes to avoid when reading this book, it's time to begin calculating how much money you need to retire.

The Key Numbers That Make Or Break Your Retirement Security

*“Whenever you find yourself on the side of the majority,
it is time to pause and reflect.”*

Mark Twain

Let me share a story with you. My Ultimate Retirement Calculator often gets featured in reviews about retirement calculators. All too frequently a misinformed writer wages criticisms like the following:

- It doesn't include separate inputs for each spouse. (Answer: Who needs the complication? Just aggregate both spouses together. It's called community property for a reason.)
- It doesn't provide separate tax rates before and after retirement. (Answer: Who cares? Different tax rates would only be marginally meaningful if your income fell dramatically after retirement. Are you planning on poverty?)
- It doesn't include varying asset allocation with age. (Answer: You can't even model the performance of a single asset allocation accurately for 30 years. The idea that you can model a changing allocation with any greater accuracy is lunacy.)

Each of these critics is making the same mistake. They believe in the magic number myth. They seek to add more details and sophisticated modeling in the vain pursuit of increased accuracy when no such accuracy is possible.

The cause for this erroneous reasoning is they don't understand how retirement planning math works in practice. All those little details

are dwarfed in significance by one or two critically important “big numbers” that will make-or-break your analysis. Get these big numbers right and all the other details barely matter. Conversely, get just one of the big numbers wrong and your analysis will fail completely no matter how many small details you got right.

What are those critically important numbers?

Critical Number 1: Percentage of income saved versus income spent.

In the article on my website, “How Anyone Can Retire in 10 Years (or Less!),” (<http://bit.ly/dRFJCc>) I demonstrate how a super-aggressive savings rate would allow you to skip all the calculators by reducing retirement planning to one simple ratio that forecasts with scientific precision how long it takes to become financially independent. The numbers are as follows:

- 10% savings rate = 42 years
- 20% savings rate = 32 years
- 40% savings rate = 21 years
- 50% savings rate = 17 years
- 60% savings rate = 14 years
- 70% savings rate = 10 years
- 80% savings rate = 7 years

(Please note, these numbers are only scientifically valid for very high savings rates (60%–80%) because longer time horizons introduce complications from compound returns and inflation. Lower savings rates (or longer time horizons) are shown for illustration only. See the full article for all the details: (<http://bit.ly/WGSb0D>).

This is not some crazy math theory. It explains exactly how I retired

at age 35. I saved roughly 70% of a substantial income and never allowed spending to rise with income. It didn't take long for my assets to grow sufficiently large to support my lifestyle.

It's a brain-dead simple, scientifically accurate way to retire young and know with certainty how much money you need to retire. No fancy math, impossible assumptions, or retirement calculators required. It just plain works.

The principle taught by this critically important number is if you want to retire faster, then reduce your spending or raise your income so your savings as a percent of income grows. The higher the percentage, the faster and more reliably you'll reach the goal.

Again, don't get hung up on distracting details. Just pay attention to your savings rate in relationship to your earnings and spending needs. It's a critically important number.

Critically Important Number 2: Return on investment minus inflation.

The reason I spent so much time explaining the investment return assumption earlier in this book is because it's the most important number (along with inflation) determining your retirement failure or success. The relationship between inflation and portfolio return will literally make or break your retirement. It is The Big One. Nothing else comes close when planning retirement with paper assets.

The reason is simple—compound returns multiply little differences into huge differences over long periods. This isn't about turning mole hills into mountains; this is about turning grains of sand into the Himalayas. I'll repeat that point for emphasis because I don't want you to miss it. **Both inflation and return on investment have a compounded effect on your estimate for how much money you need to retire.** That's why they're so critically important.

But don't take my word for it. Prove it to yourself right now. Go to my Ultimate Retirement Calculator (www.financialmentor.com/calculator/best-retirement-calculator) and enter the numbers that best represent your life situation. Seriously, do it before reading any further. Don't worry about perfection. Your best estimates from earlier in the reading are good enough for this exercise.

When inputting expected lifespan, use age 100 unless you have known health issues. Notice how the calculator allows you to reduce spending during retirement just like the research by Bernicke indicates. If you're just reading along but not taking action, then you're shortchanging yourself because you'll get a lot more value from this if you do the exercise right now. Please, don't just trust me; prove it for yourself. It'll only take two minutes and could be the most eye-opening two minutes you spend all week.

Once you fill out the calculator with your base level numbers, then write down the "magic retirement number" that it provides.

Next, try perfecting your magic number by tweaking a few variables like tax rate, retirement age, and other details similar to the critical comments cited earlier. The only rule is you can't touch the two key inputs highlighted in this chapter: return on investment and inflation. Everything else is fair game.

Notice that your magic number changes with each variation, but the changes are only marginal. Your estimates for how much money you need to retire remain in the same ballpark as your original number. The calculation is relatively stable.

Now, using the exact same inputs as before, raise your inflation rate by 2% while simultaneously reducing your return on investment by 2%, but make sure you're sitting down first.

See what I mean? For most people, this small change will literally multiply the amount you need to retire several fold. It should knock your original estimate right out of the ballpark, over the

river, and into the next state.

That is why I call all the other variables “details” and label these two ratios “critical.” It’s just the way the math works.

Principle: Small changes in a few key numbers multiplied over long periods of time have huge impacts on your ability to retire with financial security. Therefore, focus on those key variables and don’t worry about the minute details.

The conclusion is clear: If you’re going to plan your retirement using the traditional asset-based model, then retirement calculators should only be used for scenario analysis, not determining your magic number.

- Use retirement calculators to model a wide range of variables to produce a confidence interval estimating the assets you supposedly need.
- See what happens if you add 10 years of additional income—part-time work, consulting, or whatever might interest you—to take the pressure off savings and allow your assets more time to grow.
- Try modeling real estate rental income that adjusts for inflation and rises when you pay off the mortgage.
- Try modeling what happens when you receive a lump sum inheritance or sell a home or business.
- Try modeling the difference between a conventional asset allocation and a dividend growth portfolio.
- Try modeling if it’s better to delay Social Security or start payments early.
- Try modeling several factors together.

In other words, use the retirement calculator to put numbers

behind different life plans for your financial future. Each example will teach another principle just as the examples provided in this chapter and the next chapter teach principles. Retirement planning done right is really about life planning, not calculating magic numbers.

That is how you use retirement calculators properly, and that is why my Ultimate Retirement Calculator is designed specifically to facilitate a simple process for scenario analysis. It allows you to easily model different life scenarios and see how the numbers work.

The Ultimate Retirement Calculator is designed with three specific objectives in mind:

1. It omits meaningless complication and non-essential detail, thus reducing barriers to completing the calculations. It's more important to plan retirement roughly than not do it at all. It's also important to not get so caught up in minute details that you deceive yourself into believing the output is scientifically accurate.
2. It provides a simplified platform so you can model various real-life scenarios using all three asset classes (not just paper assets, like competing calculators). No other calculator allows that flexibility that is essential for the way modern retirements are planned.
3. It allows you to quickly and easily build confidence intervals by varying single inputs and seeing how it affects overall output.

In short, this calculator is designed for scenario analysis—not mythical magic numbers—because that's what is useful when estimating how much money you need to retire using a traditional asset-based approach. The common mistake is to make the process all about asset accumulation when there's far greater value in the life planning aspect.

Calculators are best used for mapping a path and putting numbers behind your life plan. They're indispensable for seeing the financial impact of what-if scenarios so you can make better informed decisions about your future.

Scenario analysis is how you blend life planning with retirement calculators to engineer a realistic roadmap for achieving financial security. It's a practical approach for retirement planning that avoids the myths and traps that have unfortunately become conventional wisdom. It acknowledges the inherent limitations in designing an asset-based retirement plan and provides a practical solution.

Now that you know scenario analysis is the right approach for using retirement calculators, below are 4 rules to help you implement that scenario analysis wisely.

- **Walk Forward Process:** Don't perform the retirement savings goal exercise once, put it on a shelf, and then forget it. Instead, check back every few years and see what assumptions proved valid and which ones did not. Adjust your assumptions, recalculate, and shift your plans accordingly. Rinse and repeat every few years. This way you'll hit your retirement target like a rocket constantly course correcting toward its target.
- **Errors Multiply:** Small errors in estimates compound into large errors in results. Retirement savings are built and spent over multiple decades. A 2% error in inflation or investment return that is manageable over 5–10 years is a complete disaster when compounded over 30–40 years. That's why you must regularly recalibrate over time based on actual results. Small details in key numbers cause huge differences, so pay particularly close attention to the key numbers.
- **Teach Principles:** Retirement calculators are invaluable for teaching essential retirement planning principles. Users

quickly grasp how real return net of inflation is the most important number after just a few quick scenario tests. They also see the importance of time in compounding their way to wealth versus saving their way to wealth without the benefit of compound returns over time. They see the erosive effect of inflation by watching how their spending escalates out of control. Without a calculator these concepts are difficult to grasp, but with a calculator they become obvious for even a layman.

- **Maintain Flexibility:** Avoid calculators that limit your ability to change assumptions. It's shocking how many calculators pre-program assumptions for investment return, inflation, longevity, and other important inputs. When an assumption is hard-coded into a calculator, it reduces your ability to plan scenarios.

In other words, use retirement calculators to plan, test, and hypothesize your retirement future. They're extremely useful when properly applied with a clear understanding of their inherent limitations.

It may seem like the task is impossible given the magnitude of potential error, but with enough practice in scenario analysis, you'll find acceptable workarounds and solutions so you can plan your life in a way that will result in long-term financial security.

In the next chapter, I'll show you a variety of creative solutions in retirement planning that you can model using scenario analysis so you can save years off your retirement date, reduce risk, and increase your financial security at the same time.