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How much do I need to retire?

SAVINGS ADVICE: FIRST YOU NEED TO UNDERSTAND YOUR RELATIONSHIP WITH MONEY

If you are spending less than you earn, that is a great start.

Stephen Katzenellenbogen

A Moneyweb reader asked: I am a 48-year-old female and currently have 17 years left before I retire. I am a single mum with two daughters – a 22 year old and a 16 year old. Both are students, with the older one completing her tertiary education at the end of 2021.

I have thus far saved R836 000 for my retirement – R620 000 is in a provident fund at work (currently contributing R8 765 monthly), while R212 000 is in a retirement annuity (contributing R3 000, increases annually by 10%).

I've recently started contributing R1 000 per month (R4 000 in total thus far) to a tax-free savings account. I am going to increase this amount to R3 000 from March 2022

Will I have enough at retirement? What can I do to increase my savings to retire comfortably?

PILE IT ON. It's never too little – even if the amount seems small, save as much as you can. Picture: Shutterstock

The answer:

As a precursor to your query, it is good to think about and understand your relationship with money and why you want money.

You have indicated you want to save so that you are able to retire comfortably at age 65 – by this I mean financial independence. In other words, working beyond that point will be a choice and not a necessity to earn an income.

The reality is that few people can become a Jeff Bezos – however, financial freedom is within reach of most gainfully employed people. In Morgan Housel's book, *The Psychology of Money*, he tells the story of Ronald James Read.

Ronald Read lived a humble life working as a petrol station attendant and janitor. When he died aged 92, Read's net worth was approximately $8 million (about R120 million).

Here are a few money lessons we can learn from the real-life story of Mr Read:

- It's never too little – even if the amount seems small, save as much as you can.
- Start saving as early as you can and do so for as long as possible.
- Live humbly. Your lifestyle increases should be well below your salary increases. The temptation is to increase expenditure as income increases, but you should instead maintain a comfortable rather than excessive lifestyle.

How you spend your money is as important as saving – don't be wasteful and try to avoid impulse purchases.

- Lesson 4 in the book could be a subject on its own and refers to the long-term benefit of compound interest.

Understanding the workings of compound interest can be a tremendous advantage in your savings journey. You can think of icons like Warren Buffet as an excellent example of someone who understands the power of long-term compound returns.

15%-20%

Percentage of your income you must save

He started investing when he was 10 years old (think back to the point about starting as early as you can). If Buffet had stopped investing at age 60 instead of re-investing, his net worth would be $12 million and not $81 billion.

That is a staggering difference and indicates how powerful compounding is.

The points above are an excellent foundation for addressing your question about what you can do to increase savings. In a nutshell – if you are spending less than you earn and buying less than you can afford, you are off to a great start.

For a few reasons, your questions, the second one at least, are difficult to answer, but here are some comments:

- You have not stated how much you earn. The amount you earn, and how much you spend, will determine how much you can save.
- Typically, saving 15-20% of your income from the start of your career should put you in a position to retire with an income similar to that which you were earning while working. It goes without saying that the more you save, the better off you will be. However, you also need to enjoy life and the benefits of working.
- Have a good look at your spending and see if there are any easy changes you can make to save money. For example, look at insurance premiums and cellphone contracts to confirm you have appropriate packages for the price.

Your first question about having enough savings at retirement is also tricky; there is the esoteric question of "what is enough?"

You also haven't stated how much income you require each month. I've done a calculation to indicate what you could reasonably expect to draw at retirement based on your current savings.

Here are my assumptions for the calculation:

- Current lump sum: R836 000
- Monthly contributions: R14 765
- Contribution increase: 5% per annum
- Return: 8.5% (inflation + 4%)
- Inflation: 4.5%

You have said that your RA contribution increases by 10% annually. I assume your work contribution will also increase and the TFSA contribution will be flat – 5% is an assumption based on these factors.

Based on the above inputs, you would be able to draw R29 500 per month, in today's terms, increasing at 4.5% per annum until you are 95 years old. Your capital will start diminishing at age 79.

These types of calculations should only serve as a guideline as they have several flaws. For example, they do not cater for ad hoc lump sum withdrawals and, more importantly, they assume straight-line returns, which are not possible.

What you invest in will also have an impact on your retirement. Given your relatively long-term investment horizon, you need to embrace appropriate risk and do your best to generate a solid return above inflation.

You do not need to be the best investor with the best return, but you certainly cannot afford to be the worst. To illustrate this point, the difference in the future value of a R1 million investment over 17 years achieving a 7.5% return per annum versus a 9% return per annum is R908 281 – in other words, almost 100% of your initial investment.

Good luck.

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