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How sustainable is your retirement?

Using a Retirement Planning Dashboard to understand the key trade-offs: income, bequest and sustainability

To better understand the important trade-offs in the retirement investment planning process, we will consider a simple case study. James and Catherine are a married couple, both aged 65, approaching retirement with joint accumulated assets of £500,000. They could purchase a Lifetime Annuity, which would provide an annual income of around £31,000. However, they believe they could live comfortably on a slightly lower income level and are very keen to leave some form of Bequest to their children and grandchildren should they die. They are concerned about giving up the lion's share of their accumulated nest egg over the next few years.

In order to start to think about potential solutions to James and Catherine's retirement needs, we need to consider the important measures of success and risk that James and Catherine might use as a 'Dashboard' to assess any possible retirement plan:

Retirement Planning Dashboard	
Retirement Plan	Details of James & Catherine's retirement plan, including: initial fund amount, product choice, investment option.
Retirement Income Account	The specified annual income level: the higher the better, presumably!
Retirement Income Sustainability, RIS (%)	The chance of sustaining the specified income level for the rest of their lives. Clearly James and Catherine wish to get this number to be as close to 100% as possible and should certainly plan to get the RIS number above 80%.
Bequest Value, EBV (%)	The value of the bequest or legacy they can expect to leave to their dependents. This can be measured as a % of the initial retirement fund value.

James and Catherine met a financial advisor who suggested that an Income Drawdown plan might be suitable. Based on a risk profiling exercise, he suggested a typical 'Balanced' investment strategy: 60% Equities, 40% Bonds. They plan to draw an annual income of £28,000 – 90% of what they would have received by buying an annuity.

We can evaluate the Retirement Planning Dashboard for this chosen investment strategy.

Retirement Planning Dashboard: James and Catherine	
Retirement Plan	<£500,000 Income Drawdown (Balanced – 60% Equity)
Retirement Income Account	£28,000 pa (90% of annuity)
Retirement Income Sustainability, RIS (%)	53 %
Bequest Value, EBV (%)	68%

Having selected a "Balanced" investment strategy and picked an income level lower than the immediate annuity, they might be shocked to find that their retirement plan has a sustainability of around 50%! Like most retirement customers, James and Catherine feel that a '50:50' chance of sustaining their target level of income is far too low.

The question is how can James and Catherine adjust their retirement plan to improve the outcome?

Case 1 - Base Case

The key trade off is between the level of income, the sustainability of this income, and the value of Bequest available to dependants.

Action	Impact on Retirement Planning Dashboard
Reduce the annual income level (Retirement Income Amount)	Increase RIS Increase Bequest Value
Use part of their retirement nest egg to buy some type of Lifetime Annuity	Increase RIS Reduce Bequest Value
Change investment strategy (Equity allocation)	Impact on RIS and Bequest depends on income level

The Retirement Planning Dashboard can be recalculated for a wide range of different planning options, to help James and Catherine decide which best suits their own preference. A few examples are given below:

Considering alternative retirement options

Case 2 - Reduced Income

By reducing the initial income level (from 90% of the annuity income level to around 80%) sustainability increases from 57% to 71%.

Retirement Planning Dashboard: James and Catherine	
Retirement Plan	<£500,000 Income Drawdown (Balanced – 60% Equity)
Retirement Income Account	£25,000 pa (80% of annuity)
Retirement Income Sustainability, RIS (%)	71%
Bequest Value, EBV (%)	75%

Case 3 - Reduced Equity Allocation

They can increase the income sustainability further by adjusting the asset allocation.

Retirement Planning Dashboard: James and Catherine	
Retirement Plan	£500,000 Income Drawdown (Cautious-20% Equity)
Retirement Income Account	£25,000 pa
Retirement Income Sustainability, RIS (%)	81%
Bequest Value, EBV (%)	68%

Case 4 - 20% of Fund Annuitized

However, to get the sustainability level up to 90%, they can annuitize £100,000 of their retirement fund.

Retirement Planning Dashboard: James and Catherine	
Retirement Plan	£400,000 Income Drawdown (Cautious-20% Equity) £100,000 Fixed Lifetime Annuity
Retirement Income Account	£25,000 pa
Retirement Income Sustainability, RIS (%)	90%
Bequest Value, EBV (%)	61%

These simple examples illustrate the actions that James and Catherine can take to increase the sustainability of their retirement plan. There are many other possible retirement portfolios (and products) which James and Catherine may wish to consider. The Retirement Planning Dashboard forms the basis behind Barrie & Hibbert's Retirement Portfolio Planner - a tool enabling advisors and investors to evaluate different retirement options and to understand the trade-offs required to build a sustainable retirement plan.

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