Financial Preparedness Series

The Final Stretch: Reminding your 60-Something Members of the Importance of 'Considered Spending' in Retirement

After years of delays and development challenges, the launch of The Pensions Dashboards is getting ever closer. Once fully operational, the dashboard will allow many who are not currently in receipt of their pension benefits, a single view of what they have accumulated for retirement

While the introduction of the dashboard is an important step in the right direction, we believe that pension scheme members would still benefit from additional guidance. It's why we've created our Financial Preparedness Series where, in each article, we focus on a different demographic of retiree to give you insights and tips to support them in their retirement planning with or without the Dashboard.

The retirement countdown

The more your members understand the potential implications of the data provided by the dashboard, the better prepared they will be to make the right decisions, now that the reality of retirement living is getting closer for them.

This, the first article in the series, is aimed at people approaching retirement age who, having seen their pensions dashboard, are now wondering how they should manage their retirement planning —as well as their spending— at retirement. We hope this article is useful in helping you explain to members that, how we spend our money during retirement has almost as much a bearing on our financial wellbeing in our twilight years as how we save for it.

Vague ideas will not suffice

In a recent survey for BlackRock, the world's largest fund manager, a whopping 65% of Gen X and pre-retirees reported having only a vague idea of how long their retirement savings might last. Unfortunately, when it comes to retirement spending, vague ideas will not suffice.

A common rule of thumb is that retirees will need around two-thirds of their salary to be able to live comfortably during their retirement. However, as with most rules of thumb, this does not capture many people's reality. The two-thirds figure is little more than a rough - and highly subjective - guess that doesn't accurately consider a number of factors including one's cost of living during retirement.

The Pensions and Lifetime Savings Association (PLSA) Retirement Living Standards has suggested that a single person needs between £13,400 and £43,900 annually for retirement, depending on the desired lifestyle (minimum, moderate, or comfortable). For a two-person household, these figures roughly double, ranging from £21,600 to £60,600. These figures are estimates and will vary based on individual circumstances, location, and spending habits. (Source: Pensions UK - Retirement Living Standards)

Either way, at least now that the pensions dashboard is (almost) ready to go live, it will soon be possible for most pre-retirees to see how much they have accumulated in each pension pot, including the state pension. This should make it somewhat easier to plan for retirement.

But what things do members need to keep in mind once they have all this information at hand?

Remind them to cross check their pensions within the dashboard

Although the Pension Dashboard will bring a single view for most people it may still have missing information. For schemes who have under 100 active and deferred members there is no requirement to connect to the dashboard.

Should members take a lump sum cash amount at retirement?

There are various ways in which people can elect to take a lump sum at retirement or future lump sum payments during retirement. A key consideration is: do members need that tax-free lump sum? Is that once-in-a-lifetime cruise or long-planned-for luxury caravan really necessary? If so, do they need to take out the full total tax-free amount of 25% of their pension pot at retirement, or will a smaller amount suffice?

To have a clear idea of how large a lump sum they might need requires mapping out, as precisely as possible, their future spending. It's important to keep in mind three basic things when it comes to budgeting for retirement: basic day-to-day living costs, special treats along the way (e.g. holidays, academic courses, home improvements, etc.) and unexpected expenditures.

- Will their home(s) need expensive maintenance work—bearing in mind the tougher rules planned by the government for things like energy efficiency and fire safety?
- How about cars? Will they need replacing in the coming years?
- Will children need help from the Bank of Mum and Dad to put down a deposit on their first mortgage? Will grandchildren need additional support through university?

These are all questions that will need careful consideration before deciding how much money to take as a tax-free lump sum.

Optimise income during retirement

During retirement, spending can ebb and flow, so some might argue that it makes little sense to have monthly payments at all. Instead, for Defined Contribution members, they say, retirees should take out money as and when needed. Naturally, this implies much more pro-active control and management of one's withdrawals, which may be easy enough in the early years of retirement but is likely to become more difficult with time, especially if cognitive decline sets in.

As we'll go on to explain in the next article in this series, inflation can erode a member's future spending powers, especially if their pension schemes are not inflation indexed. Therefore, it's particularly important to highlight to your members that the purchasing power of their pensions may fall over time.

With inflation set to remain a persistent feature of the economic landscape for years to come, how members invest their money post-retirement is as crucial as how they spend it.

If you would like to discuss any of these matters further, please get in touch with your usual contact at Cartwright.

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