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Personal Financial Literacy

Lesson 7

Planning for Retirement

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مجلس أبوظبي للتطوير الاقتصادي
ABU DHABI COUNCIL FOR ECONOMIC DEVELOPMENT

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Planning for Retirement

Retirement is the time in life when the major sources of income changed from earned income to employer-based retirement benefits, private savings and investments, and/or government provided benefits, etc. This will be your responsibility. Governments are moving away from guaranteed pension benefits and are requiring their citizens to manage their own retirement funds.

Retirement Savings Goal (or Retirement "Nest Egg")

You should begin to build your retirement savings as soon as possible, even before you save for your children's college savings. Why? There are many more ways to pay for your children's college expenses than there are to establish a retirement savings. Build your nest egg during your working years and live off of it during retirement. There are some basic questions you'll need to address:

1. How long will you work and how much can you afford to save?
2. How long will you live?
3. What, if any pensions will you have?
4. What annual budget will you need to enjoy the life style you desire?
5. Keep in mind here that some costs decline in your later years, but others such as health care increase dramatically.
6. Don't forget to consider inflation which can unfavorably impact your savings.

Once you've addressed these questions calculating the amount you'll need to save is a simple exercise in time value of money and investing. There are a variety of calculators available from various websites, but be sure to use one from reputable and trusted source.

Now that you have estimated the lump sum you'll need at the age you'd like to retire you must establish an investment plan that meets these needs. Since this plan is different from your regular investment plan there are some steps you should take that are different.

Your retirement savings are very important, so you don't want to take foolish risks, but that doesn't mean you should rely solely on safe investments such as bank CDs and money-market funds. To build an amount large enough to see you through retirement, which may last 30 years or more, you'll need the growth that stocks provide.

From 1926 through 2009, stocks – broadly speaking, using the S&P 500 index as a measure – have posted an average annual return of 9.8% versus just 5.4% for bonds, according to Ibbotson Associates.

Given stocks' superior long-term returns, some financial advisers recommend that investors whose retirement is still 20 years or more away put the lion's share of their portfolio in stocks and stock funds.

Of course, a 100% stock portfolio can provide undue risk for extended periods. In the 1973-74 bear market, for example, U.S. stocks lost 43% of their value and took three-and-a-half years just to get back to where they started. Similar results occurred recently in the market downturns during 2001 and again in 2008. Portfolios that are overly concentrated in the equities markets may suffer even more dramatic ups and downs.

Therefore, a more prudent course is to include other more conservative investments such as bonds. Putting 70% of your portfolio into stocks and 30% into bonds, for example, will let you capture most of the long-term growth of stocks while sheltering your investments somewhat during meltdowns.

As you approach retirement age, the idea is to shift more into fixed income, such as bonds. But even in retirement, which can last a few decades, it pays to maintain a healthy dose of stocks (maybe upwards of 50% in your 70s, and up to 30% in your 80s).

Take care, however, to understand the kind of companies you're investing in. More volatile stocks may not be appropriate for you at the later stages of your life.

In considering your planning, there are many resources available in the UAE, some of which are listed below:

Agency	Website for Information
Ministry of Health	www.moh.gov.ae
Abu Dhabi Pension and Retirements Fund	http://www.pension.gov.ae
General Pension and Social Security Authority	http://www.gpssa.ae