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Create a Retirement Strategy

Most of us would like to retire someday with the peace of mind that we can take care of ourselves financially. Because the length of your retirement may equal the number of years you were in the workforce, you may need to support yourself financially for a retirement that lasts decades! It makes sense to create a retirement strategy and start to implement it as early as you can.

Begin with your budget

Creating a written budget, also called a spending plan, can be a valuable tool for living within your means and setting aside the savings you'll need to retire. A budget will help you to see your overall financial situation today and how much money you can potentially save and invest before you retire.

After making your budget, you may find that there's not enough money to go around. What do you do then? Since your fixed expenses may be difficult to change, look for ways to decrease your flexible expenses (for example groceries and long distance phone calls) and expenses that are discretionary (like clothes or home decorating). Also consider ways to increase your income.

Create a projected budget to get a realistic sense of how your financial picture is likely to look after you retire. This will help you see how much you can afford to spend each month and not outlive your retirement savings.

When you make your pre- and post-retirement budgets, try to be realistic. It's important to create a budget you can live with over time. Review your budget periodically and adjust it as needed.

Pay down your debts

Many experts recommend that you pay off major debts, such as home mortgages, college loans and other significant cash-flow drains, as quickly as you can. That way, you can greatly reduce the amount of money you'll need each month during retirement.

Consider your costs

When it comes to creating a retirement strategy, there's no such thing as "one size fits all." Everyone's circumstances and financial situation are a little different. How much money will you need in order to retire? To a large extent, the answer depends on several key factors:

- where you plan to live and the cost of living there;
- how many years you'll live in retirement; and.
- how much your healthcare expenses will be during that time.

Remember that various factors may change over the course of your retirement years, including your state of health. You may develop new healthcare needs and have increased healthcare costs. The average life expectancy for American women is approximately 80 years old, and for men around 75; but you may live a lot longer. And retirement years are when most people are most vulnerable to rising costs in health care.

Create a Retirement Strategy (continued)

Also, consider the fact that in future years you may want to adjust your living situation to suit your changing needs. Do you anticipate living with family members or on your own? Some senior communities now offer healthcare and assisted living as part of a complete package of services. Explore some of these options in advance so that you have a realistic understanding of the potential benefits and costs.

As a general guideline, many experts recommend that you aim for 75–85% of today's income after you're retired.

Where will the money come from?

For most people, retirement funds come from five sources:

1. The money you've **saved**, i.e. your retirement "nest egg." Many experts recommend that working people try to set aside 15% of what they earn into long-term savings.
2. After you retire, you may add to your nest egg with money you **receive**, such as social security or a pension.
 - Today there's a lot of talk about social security and what's going to happen to the program in the future. But whatever happens, the reality is that most people cannot rely on Social Security to fully fund their retirement years. For example, in 2012, the average monthly benefit nationwide was \$1,230. That's just \$14,760 a year, an amount that's not likely to give you the retirement of your dreams.
 - Not too many people are lucky enough to have a pension. Even when pension plans were at their peak in 1985, fewer than half of Americans working for private companies were covered. By one current estimate, only 17% of those employed outside of government agencies can expect to receive traditional pension checks in retirement.
3. You may **earn** more money by continuing to work. Many people who are officially "retired" still earn money by working part-time, running a small business, or cycling between periods of employment and leisure. In addition to the income, continuing to work helps many people to feel connected, useful, and satisfied with life.
4. You may take a portion your savings and **invest** it. Investing means taking some risk with the goal of earning a higher return over time. If your employer offers a 401(k) plan, don't miss out on the opportunity to participate. Take advantage of the new "catch up" provision starting at age 50 to maximize the amount of money you contribute.

Create a Retirement Strategy (continued)

Where will the money come from? (continued)

5. If you're a homeowner, another source of funds might be the **home equity** you have accumulated over the years. Equity is the difference between how much the house is worth and how much you still owe for it.
 - If you have equity, you may be able to borrow money using your home as security. A home equity line of credit can provide you with financial flexibility and options before and after you retire. Just remember that as you use it, you'll have to make monthly payments to your lender.
 - Some retirees sell their home, downsize to a smaller and less expensive location, and add the profit they make to their retirement savings.
 - Many financial experts recommend that—if you can—you pay off your mortgage by the time you're ready to retire. This will not only take away any worry about making loan payments, it will also give you a good financial cushion in case you need the money for other needs or a financial emergency.
 - In your retirement years, another way that homeownership might benefit you is a "reverse mortgage." This is a loan designed in a way that's the opposite of a traditional mortgage loan: instead of paying your lender, your lender pays you. Instead of building home equity, you reduce your home equity by withdrawing it as income. The ability to turn your equity into tax-free income is what makes reverse mortgages appealing and valuable to many senior homeowners. You can use these cash advances from your home equity for any purpose you choose.

Try this formula

Many studies indicate that if you want your retirement savings to last, you should withdraw no more than 4% to 6% of your savings each year.

Here are two examples: Let's say someone has \$100,000 in savings and withdraws 5% a year. Five percent of \$100,000 is just \$5,000 a year. With a million dollars in savings, at the same 5% withdrawal rate, the amount grows to \$50,000 a year...which sounds like a much nicer retirement!

Try this formula yourself to see how your current retirement savings compares to your goal, and to calculate the nest egg you'll need to generate the retirement income you want:

The exact percentage you'll want to withdraw depends on many factors, including how long you live. Obviously no one has a crystal ball to see into the future, but if you're in good health and retire at a relatively early age, withdrawing a smaller percentage each year will help insure that your savings last as long as you do! The amount of savings that you spend each year will also depend on how much you receive from other sources of income such as part-time work, social security, etc. If your other sources of income are significant, you'll have some flexibility about which pool of money you choose to spend—your savings or your other sources.

A financial advisor can help you decide the best strategy for you. If you don't expect to have much income other than your savings, you need to be more conservative with your withdrawal rate. If you're still working now, try to save as much as you can at the best interest rate possible before it's time to retire.

Create a Retirement Strategy (continued)

Consult your retirement strategy team

As you begin to define your retirement strategy, there are a number of resources who can help you. These include your employer, tax advisor, banker, home mortgage consultant, and an investment counselor. Think of these individuals as your retirement strategy team. Take advantage of the information and advice they can offer you. If you work for a company, a great place to start is by talking to your employer or your union. (If you're self-employed, you can seek outside professional advice.) Here are some of the key questions to ask:

Ask your employer

- What retirement benefits will you receive? The answer will help you determine how much longer you want and need to work (and save) to help ensure a financially secure retirement.

Ask your CPA or other tax advisor

- Which retirement income sources should you spend first in order to minimize your taxes?
- At what age can you begin withdrawing money from a tax-deferred savings plan without incurring a penalty? (Currently, the answer is age 59½.)

Ask your investment counselor

- How much can you realistically expect to earn on your investments? Remember, investing always involves risk and there are no guarantees. Some investments carry more risk, and more potential reward, than others.
- How should you allocate your assets to manage your income in retirement while seeking continued growth for your savings?

But be sure to check the credentials of any financial advisor you use. Make sure they have a solid track record and reputation. Remember: lots of good information is available about retirement planning at low or no-cost—in books, magazines, and on the Web—but if you do pay someone to advise or assist you, be sure you understand how (and how much) you'll be charged.

Guessing can cost you much more than paying for professional help. And financial advice doesn't have to be expensive. Some financial services companies will answer basic financial questions for free, or create a basic financial plan for as little as a few hundred dollars. Paying for that advice now can be a bargain if it helps you make smart financial choices that pay off in the long run.

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