Brent Sheather's RESEARCH

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SAVING FOR YOUR RETIREMENT – HOW MUCH DO YOU REALLY, REALLY NEED? - Part 2

In my last column we looked at various claims by fund managers and financial advisors selling KiwiSaver (KS) that NZ'ers aren't saving enough for their retirement. One KS provider is even arguing that individuals need to be saving 12% of their wages. The conflict of interest here is pretty obvious but not much work seems to have been done linking "what you need to save" with "how much you've saved will produce in decumulation". Today and in two week's time therefore we will have a go at quantifying what level of income would support a "comfortable" retirement, what nest egg would be required to produce that level of income and then compare that number with the terminal sum likely to result from saving 6% of the average wage.

The default KS contribution level is 3% of before tax pay and employers are required to contribute another 3%. Most individuals who opt for the default rate or higher will receive another $521/per from the government. So that is a total of about 6% of one's salary.

First off we need to define what "comfortable" looks like to the average person and, importantly, distinguish between retirees in one person households and two person households. Probably the best source of information on this topic is the NZ Retirement Expenditure Guidelines paper produced each year by Massey University's Financial Education Centre. The latest of these was produced in June 2023 and as the table below shows they estimate that for a no-frills budget retirement a single person living in a metropolitan area will incur $826 a week in costs versus $689 a week for an individual living out of the main cities. For comparison NZ super at that time was $496 per week, after tax. For a two per person household the numbers are $982, $850 and $763 respectively.

Table 1 – Estimated Expenditure/Week For A "No Frills" Budget Retirement

	1 – person household		2 – person household	
	Metro	Provincial	Metro	Provincial
Total weekly expenditure	$826	$689	$982	$850

Source: Massey University – NZ Retirement Expenditure Guidelines (June 2023).

So if we accept these numbers as reasonable and assume that National Super will continue then a worst case scenario for a no-frills retirement is a one person retired household sustaining costs of $826 a week versus $496 in income from National Superannuation, leaving a deficit of $330/week. We now need to estimate what level of nest egg will produce an

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income, increasing with inflation, to plug that deficit. The decumulation model we use to do this assumes that income will be supplemented by a withdrawal of capital such that the value of the portfolio at age 93 is around zero. To simplify things we assume a constant asset allocation of 50% bonds and 50% equities with long term returns forecast at 5%pa and 8%pa respectively. Given the above and assuming conservatively that the individual retires at age 65, management and financial advisory fees of 1% pa and tax at 17.5%, the model suggests a sum of $350,000 is required to produce around $330 per week after tax and increasing with inflation, assumed at 2.5% pa.

So the $350,000 invested in a relatively conservative portfolio will produce the level of income needed, over and above National Superannuation, to meet Massey University's estimate of the income required for a no-frills budget retirement. Whilst that is considerably less than what the finance sector suggests is required they would probably be of the view that this level of savings wouldn't meet their definition of a "comfortable" retirement. However we must keep in mind that individuals working in the rarefied world of finance might also likely opine that the average wage didn't provide a comfortable working life either!

For people living in the real world i.e. not investment bankers or fund managers, a realistic perspective as regards an income of $826 per week can be derived by comparing that level of income with the average wage in NZ today. According to the Statistics Department the average wage in 2024 is about $1,386 per week, or around about $1100 after tax. The $826 per week total income after tax, inclusive of National Super, estimated in this scenario represents some 75% of the after tax average wage.

That doesn't sound like a disaster to me but even that comparison is conservative - as Dr Biggs pointed out in the last column average household spending in the US "drops by roughly 40% from age 65-90". For example a retired individual won't be contributing to KiwiSaver and won't be buying nappies, unless they are Al Pacino (he is 82 and Mrs P is 29). Most people aged 65 probably won't be paying off a mortgage either. Therefore for a fair comparison we should estimate those numbers and deduct the total of those expenses from the average wage then compare that lower number with the $826 per week scenario. My back of the envelope estimate is that the total of these numbers would be around $600/week. So a reasonable comparison, accounting for these non-recurring costs, is ($1100 - $600) = $500 per week vs $826. So it is conceivable that some retirees will actually have more disposable income in retirement than they had in their 30s. This is not altogether surprising as the Grattan Institute, in a study a few years back, reported that, thanks to Australia's high compulsory contributions to super, many retirees earn more in retirement than they did when working and similarly many move to the next life with more money than they had when they retired.

There is NZ evidence supporting Dr Bigg's contention that the finance sector is "scaring people" with unrealistic retirement savings goals. Anecdotal data supports the idea that NZ Super provides a substantial base for a no frills retirement: I spoke to Mary Holm who covers personal investment matters with a particular focus on KiwiSaver in the NZ Herald and she was of the view that, based on letters from readers, that "many people are happy with not much more than NZ Super in retirement". She referred me to a number of letters which made the following points:

- One couple with their own house advised that their outgoings are between $550 and $730 per week and their combined NZ Super is just on $800 per week. Income therefore exceeded their outgoings but they noted that that leaves nothing left over for holidays, major asset replacements or extraordinary costs.
- At the other end of the spectrum, one correspondent said that his wife had Alzheimers and, although in the early stages she was able to live at home, she eventually had to go into full-time care which cost $80,000 per year. This has meant that their savings will eventually be reduced until it reaches the level at which government aid kicks in.
- Another reader wrote that they live in Auckland in their own home. They have $165,000 in savings and that amount, with NZ Super, is more than enough to fund their lifestyle. The reader added that he was sceptical about the advice from the financial sector as regards what you need for retirement adding that he thought the numbers were unrealistically high and would potentially make people worry that they wouldn't have enough for their retirement.

That is more than enough this week - in two weeks time we will calculate what level of savings through one's working life is needed to achieve a terminal sum of $350,000 for a no-frills retirement then do the same analysis for what Massey University refer to as "a choices retirement".

Brent Sheather is a Financial Advice Provider. A disclosure statement is available upon request. Brent Sheather may have an interest in the companies discussed.