For the many American families whose spending is higher than the median family, a higher level of savings will be needed to secure financial freedom. (UBS)

Is being a millionaire enough to retire?

19 April 2024, 7:08 pm CEST, written by UBS Editorial Team

A recent story on CNBC found that Americans believe they need $1.46 million to live comfortably during their retirement. This is a 15% increase from last year where Americans said they would need $1.27 million, and a 53% increase from 2020 when they believed they would need $951,000.

Inflation could play a part in this surge in expectations, everything from housing to prices of food are variables that could impact retirement expenses.

There is a large disparity between these figures and the average amount that US adults have saved toward retirement, which is only $88,400, and a February report from the Senate's Health, Education, Labor and Pensions Committee found that nearly half of people 55 and older have nothing saved at all.

The amount needed to retire depends on a few key factors: planned retirement spending and age of retirement, life expectancy, and investment returns. Inflation also plays a role, although some costs in retirement will rise more quickly than others, and families tend to shift their spending categories as they spend as they move through retirement.

According to research from the UBS Chief Investment Office (see **Modern retirement monthly: Beyond the 4% rule: Am I ready for retirement?**), a family planning to sustain a 40-year retirement can afford to safely withdraw about 3.3% of their portfolio in the first year of retirement, and increase that withdrawal dollar amount by inflation every year, without outliving their wealth in 85% of market return simulations.
Now let's consider the $1.46 million target for a moment.

A $1.46 million portfolio would be enough to support a 40-year retirement with an annual withdrawal of about $48,000/year (3.3% x $1.46 million). This number doesn't account for taxes on retirement account withdrawals, but it also doesn't include Social Security income. The average family collects about $23,000 per year from Social Security once they begin collecting that income.

Adding $48,000 of portfolio withdrawals to $23,000 from Social Security suggests that a $1.46 million portfolio would support about $71,000 of annual spending. When you compare that result to the median US household income of $67,000, it does appear that $1.46 million could be a feasible target for financial independence for the median family.

For the many American families whose spending is higher than the median family, a higher level of savings will be needed to secure financial freedom. As a rule of thumb, the UBS Chief Investment Office recommends building an investment portfolio that's worth around 30 times your planned spending in the first year of retirement. If you plan to spend $100k in retirement, you may need to save about $3 million in order to safely fund your spending from portfolio withdrawals.

This rule of thumb can be helpful for starting the discussion with a financial advisor, but it does not account for all your family's unique goals and concerns. To get a better understanding of your retirement readiness, here are 3 considerations to bear in mind when speaking with a financial advisor:

1. Be as specific as possible when developing goals for your financial plan, assigning a relevant inflation rate for each goal. For example, assign a separate healthcare goal to account for higher inflation in that part of your budget.

2. Think of your retirement in phases to improve estimates of future expenses. Some expenses, such as mortgage payments, may end during retirement. Other potential expenses, such as long-term care expenses, are likely to begin later in retirement.

3. Consider the role of guaranteed income in your plan. Income from Social Security, pensions, and annuities can alleviate some of the burden from your portfolio and help to protect against the risk that you will outlive your wealth. Especially after the recent rise in interest rates, annuity income has the potential to materially boost the safe level of a family's retirement spending, or help to allow for an earlier retirement.

Just as the cost of a comfortable retirement is abruptly climbing, the average family's savings is also far below what is needed. This situation underscores the need for improved financial education and planning. Addressing this knowledge gap can help families to better prepare themselves to meet their retirement goals amidst evolving economic challenges.

Main contributor: Shawn Awan, Research and Communications Associate