



## Setting a retirement budget

New rules mean those approaching retirement now have far more freedom as to how they use their pension. But before people can decide what to do with their retirement savings, they need to know what income they'll need to cover day-to-day essentials and future bills.

Below we look at how to set a realistic retirement budget.

### Budget basics

Most of us are familiar with Charles Dickens budgeting advice, from Bleak House.

**"Annual income twenty pounds, annual expenditure nineteen pounds nineteen and six, result happiness. Annual income twenty pounds, annual expenditure twenty pounds nought and six, result misery."**

For those looking for financial happiness rather than misery, in their later years, this basic principle remains the same. But the challenge for those retiring is to have a clear idea of what their future spending requirements will be, as well as understanding what income their pension pot will generate.

### How much will you spend?

Drawing up a budget can seem simple – the difficult bit is to ensure it is accurate. It is easy to overlook many 'one-off' expenses, or simply assume that the outgoings in one month are a fair reflection of your spending for the rest of the year.

Both can mean you underestimate what you spend – putting any budget out of kilter. In retirement this can mean people end up drawing down their capital far more quickly than they planned and potentially outliving their savings.

When planning a retirement budget it can help to think about different spending needs.

#### ■ Start with the essentials

Work out what you need for day-to-day living expenses – be it bills, petrol, food, clothes and so on. Look at what you've actually spent over a three month period to get a realistic idea of where your money goes. Don't forget to make allowances for unexpected 'essential' expenses – be it the MOT, a boiler breaking down or other emergencies. Although these may be harder to predict, they are bills that need paying as and when these circumstances arise, so you need to plan your finances to cover these.

#### ■ Discretionary spending

Next think about the money you spend on holidays, decorating, Christmas, birthdays, socialising and so on. Think about what you spend at present and whether this is likely to increase or decrease in retirement. More free time can inevitable mean these costs increase. A part of these costs may be covered in the 'essential' list.

#### ■ Future costs

Finally, think about how your spending will change as you age. Poorer health may mean fewer holidays and many people may need to make adaptations to their home. You may also need additional support and care, which you might have to fund yourself.

# Setting a retirement budget

## How much income will you have?

Before deciding what to do with your pension funds, calculate what income you have from other sources.

### ■ Earnings

Many people continue to work past their State Pension age, often in a part-time capacity. If you do work past your State Pension age you will not need to pay National Insurance (NI) on your earnings, so net pay may be higher. Similarly some pensioners can also benefit from a higher personal allowance, so less of their earnings are taxed.

### ■ State Pension

The new State Pension system was introduced in April 2016. The full amount is £155.65 a week in 2016/17, however not everyone will get the same amount. Few people have any idea exactly what they will receive as a State Pension. Much will depend on the NI contributions made or credited during your working life. Get an up-to-date pension forecast from the **Department for Work and Pensions**. If it's lower than expected investigate whether making additional NI payments will boost this pension.

### ■ Company pensions

Some older company schemes and most public sector schemes, pay a pension linked to your salary. The rate at which you accrue this pension will vary from scheme to scheme, but as a rule the longer you worked for the company, the more valuable these pensions are. Many of these pensions are also index-linked so will increase in line with inflation. Contact your previous employers to find out what these pensions will be worth at retirement.

## Pension options

Once you know what income you've got coming in and what expenditure this has to cover, you can think about what to do with other pension savings.

Most company and private pensions are 'defined contribution' schemes, meaning savers have the option of either cashing in these pensions, buying an annuity, or keeping them invested and living off the investment returns (also known as pension drawdown).

**REMEMBER: This doesn't have to be an either/or decision. It's possible to buy an annuity with part of your pension to cover day-to-day living expenses, but leaving the rest invested for future spending needs. Having a clearer understanding of your spending needs can help you make these decisions:**

- If you can meet day-to-day living expenses from your state and company pensions you may opt to keep private savings invested. This means your pension pot can continue to grow and give you the option of leaving surplus funds as an inheritance.
- If you cannot meet day-to-day living expenses from the State Pension, you may want to take out an annuity which guarantees a fixed income, regardless of how long you live for. These are complex decisions, please call your financial adviser if you need more information or advice.

### Important Information

This information is not investment advice or a recommendation for any particular product, service or course of action. Pension and retirement planning can be complex, so if you are unsure of the suitability of a pension investment, retirement service or any action you need to take, please speak to your financial adviser. The value of investments can go down as well as up and you may get back less than you invested. Eligibility to invest into a pension depends on personal circumstances and all tax rules may change. With pension products you will not be able to withdraw money until you reach age 55.

## What to do if you need help?

If you want to discuss your retirement options please speak to your financial adviser.

The Government's Pension Wise service offers free, impartial guidance to help you understand your options at retirement. You can access the guidance online at [www.pensionwise.gov.uk](http://www.pensionwise.gov.uk) or over the telephone on 0800 138 3944.