



Estimating cost of living in retirement

Estimating cost of living in retirement can be tricky. The old rule of thumb was to plan on needing 80% of your pre-retirement living expenses. In my experience, that is rarely accurate. Instead, here's how I do it:

1. Start by categorizing your current expenses.

Housing — If you own your home, include property taxes, homeowners/renters insurance, lawn service, security system monitoring, etc. Do not include your mortgage payment here; we will account for that elsewhere.

One big thing that most retirees forget to budget for is maintenance. Back when my husband and I

bought our first home in 2003, my partner, Jim, told us to plan on 2% of our home value per year. You don't always spend that much, but it can accrue towards bigger things that might have to be replaced down the line like windows or the AC. Alternatively, you can redirect unspent maintenance funds every year towards a trip or something fun.

Health care — Copays, prescriptions, and any extras like physical/massage therapy, acupuncture, gym memberships, yoga, etc. Do not include premiums here; we will account for those elsewhere.

Insurance — Include premiums for health, life, disability, cars but not homeowners or renters as that is covered above under housing.

Debt service — This is where you account for a mortgage (not in housing costs above), car payments, student loans, regular credit card payments and the like.

Utilities — The usual water, gas and electric bills as well as telecom expenses like cable/satellite TV, internet and phone service.

Food — This one is up to you. You can include both groceries and eating out here. I prefer to budget for eating out with Discretionary/Lifestyle.



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Personal/Grooming — Clothing, getting your nails done, hair cut/color, etc.

Gifts — Don't forget to include charitable gifts, tithing, and gifts to friends and family, including birthdays and holidays.

Discretionary/Lifestyle — This is everything you like to do, but don't have to do to survive. This could include travel, entertainment, eating out, golf, country club, Netflix or magazine subscriptions, etc.

2. Then back out expenses that will end during retirement.

These could be anything like term life insurance, mortgage or a car loan that has a defined end date, or other expenses like regular dry cleaning, kids' tuition, or disability insurance that will go away when you're not working anymore.

3. Revisit those health care costs.

Based on publicly-available cost-of-care studies and Medicare expenses that are published annually, I currently use a default cost of health care in retirement at around \$6000 per person per year. If you have employer-provided retiree health insurance or are already on Medicare, you can use these numbers instead. Don't forget to account for inflation — based on historical trends, we assume that health care costs will rise on average 6% per year.

Here's the scary part: If you or your spouse needs long-term care at any point (and statistically speaking, more than 2/3 of retirees over age 65 will) those costs are significantly higher. Genworth annually publishes a cost-of-care study covering 440 regions across the U.S. In the Dallas area, for example, a home health aide averaged \$4000 per month in 2017. Assisted living facilities averaged \$3775 per month and a private room at a nursing home cost around \$7000 per month last year.

It is a common misconception that Medicare will pay for long-term care, but it's simply not the case. From the Medicare website:

Long-term care is a range of services and support for your personal care needs. Most long-term care isn't medical care.

Instead, most long-term care is help with basic personal tasks of everyday life, sometimes called activities of daily living.

[Medicare doesn't cover long-term care (also called custodial care), if that's the only care you need. Most nursing home care is custodial care. Get more information about nursing home care.

4. Don't forget about one-time big expenses.

Most retirees need to replace a car at least once in retirement. Whether you plan to pay cash or take out a loan, don't forget to budget for this and any other big expenses like weddings or helping out grandkids.

One strategy many of my clients choose is to "bucket" sources of income and expenses. For example, they try to limit their necessary expenses (housing, insurance, debt service, utilities and food) to their guaranteed retirement income from sources such as Social Security, pensions and annuities. They reserve another bucket of assets and/or income for health and/or long-term care costs, and another for discretionary spending and gifting.

There is, of course, no one right way to plan for and manage expenses in retirement. It truly is more art than science. All I want you to remember is it takes a plan. Getting started is, I promise, the hardest part. If budgeting doesn't come easily to you, please get some help from a professional you trust, preferably a CERTIFIED FINANCIAL PLANNER™ practitioner who has met experience and educational criteria and is subject to a strict code of conduct and practice standards.

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