Rediscovering Budgeting

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When millions of Americans leave work, they also leave behind the comforts of a paycheck. Suddenly, in retirement, they are exposed to a chore that they last experienced in their 20s and 30s—managing a budget that might feel tight. Chances are, it was not a pleasant experience back then, and they are not looking forward to it now.

The concept of budgeting has a limiting feel to it, with a dash of guilt mixed in. You are supposed to limit your expenditures below a threshold that may be set by outside influences (the press, so-called ‘experts’) and in extreme cases, you are told that your future financial success depends on giving up coffee in the morning or the now-famous frivolity: avocado toast.

In the past, there was the added hassle of tracking where your money went, but today there are a variety of tools that will do this for you, linking to your bank and credit card accounts and putting each expenditure into its proper category. Yes, you have to tweak the categories to customize them, but after that, you have the numbers part of it pretty much tamed.

The most recent approach to budgeting takes some of the guilt and much of the limit out of the process. You might ave heard of the 50/30/20 framework, which is as simple as it sounds. The first 50% is allocated to your needs—that is, your basic expenditures like food, housing, transportation etc. The next 30% is allocated to 'wants'—things like dining out, travel, buying gifts. Under this formula, the last 20% is allocated to savings and debt repayment—but of course retirees are generally not repaying their student loan debts and probably haven't racked up unpaid credit card debt. Nevertheless, that 20% can become a kind of safety net for various unplanned expenditures, like car repairs and potential healthcare expenses.

But retirees aren't getting a regular paycheck, which means they have to calculate how much to apply that budget to. There are a variety of ways to calculate how much sustainable income can be derived from a retirement portfolio, some of them quite sophisticated, and all of them dependent on future assumptions that may or may not come true. One way to start is to tote up all the basic living expenses, and lock those down. Take Social Security, pension or other stable income, and allocate that to the 'needs' bucket, and see how much of the needs are still uncovered. Those extra dollars become the amount that the retired couple would have to take out of the retirement portfolio simply to avoid sleeping under a bridge.

That's the 50% parts of the equation. Three-fifths of that amount would be, under the structure, available for spending on, well, anything the retiree wants. Does that size monthly expenditure feel comfortable, based on the total portfolio amount and time frame between now and the end of retirement? Is that a safe paycheck to take out of a portfolio that may be gradually depleted? This is a subjective decision, and of course, some of that 30% will be set aside for larger items, like a foreign vacation; it won't all be spent in the same month.

There are no hard and fast answers to this question but framing it this way might help a retiree get back into the budgeting game with an organized way of making spending decisions. They might be surprised to find that, unlike when they were in their 20s and 30s, budgeting can be uncomplicated and less painful.

Sources:

https://www.nerdwallet.com/article/finance/how-to-budget

https://www.nerdwallet.com/article/finance/budget-worksheet

If you have any questions about this article or want to discuss your family finances, investment portfolio, or financial planning advice, please call on me anytime at my number (215) 325-1595 or you can click here to schedule a meeting.

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