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Parkinson's Law and Retirement Spending

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Last week, my son's Boy Scout Troop went on a weekend campout. The campout was on an island in Sebastian, Florida. The campsite was primitive and the boys could only bring what they could carry on their backs!



It was a great lesson on bringing only what you need and what is important.

I was watching the boys on the campout as an assistant scout master (sitting on my portable chair) and I thought about Cyril Northcote Parkinson; about how his law applies to preparing for a primitive backpack trip and how your investments can last the rest of your life.

Over the last 20 years, I have probably prepared over a 1,000 financial plans. All of the software and spreadsheets will show you the following.

If you retire with \$1,000,000 invested and you are spending more than \$50,000 a year, there is a good chance you will run out of money. Or put another way, if you are spending more than 5% per year of your savings..., even if you are investing the money... inflation and/or the cost of living deplete all of your savings.



Imagine retiring with \$500,000 invested. This money could be in your 401(k) or your IRA. While you were working you earned on average 6% per year. Yes, you were working so you felt comfortable taking risk on your investments. Now at retirement you might not feel the same level of comfort.

Let's say you are taking out or need \$25,000 per year to cover your expenses. This amount is pretax and after any other income streams (such as social security or pension income). That \$25,000 will increase each year because of the cost of living (*imagine how much health care will be in 10 years!*)

At some point, the \$25,000 will grow larger than the increase on the investments and you will have to dip into savings. Maybe it will not happen for 10 years, maybe 15, but it will happen. As you start to dip, it becomes a compounding effect and the amount of savings will decrease rapidly. Until there is nothing left!

Run the numbers yourself and you will almost always see a cross over point. The three main exceptions are if you have enough income from other sources during retirement, or you have enough savings, or you reduce your expenses.

There is a proverb known as Parkinson's Law. This statement was made by Cyril Northcote Parkinson, in 1955, and states "Work expands to fill the time available for its completion."

Another way of looking at this proverb is that the demand for something expands to match its supply. Or the more you have of something, the more of it we consume. This is true for anything: food, time, and toothpaste. Imagine you have a new tube of toothpaste, how much do you use, a lot!



As you get to the end of the tube, how much do you use? Well it will last you a really long time because you squeeze it as much as possible. How much can you possible get out of it? Well it definitely could last a long time.

I have found that Parkinson's Law also applies to retirement savings. It usually happens when you are down to half of the amount you had when you retired.

For example, let's say you had the \$500,000 saved when you retired. Now, because you are spending more than you are earning (perhaps because of inflation), your \$500,000 over time, will dwindle.

All of the retirement programs and spreadsheets will show it reduced to zero. Here is the big secret: This is not the case, as the money hits that magic half way mark, you remember having the full amount.

You tighten your belt and make the money last. Imagine your money is the tube of toothpaste and you are squeezing and squeezing it to make it last. The amount of money you spend as you get older will reduce because of your fear of running out of money.

How can you use this rule toward your advantage? There are 7 financial ways that this rule can make your life easier and never run out of money. In my next article I will cover these 7 ways.

The boys on the island had a lot of fun. Some forgot their sunscreen, bug spray, and some did not bring enough food. We ended up sharing both the food and also the life lessons.

Remember, plan today... protect tomorrow.

Until Next Time,

Peter Blatt

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