Effective Decumulation - How do we switch from being a saver to a spender

CPF Board 00:07
Hey and welcome to Let's Talk CPF, a podcast where we bring conversations on CPF to your ears. Brought to you by the CPF Board, this podcast will answer common questions, offer tips, and feature interviews with industry experts on CPF and financial planning. Thanks for listening, and let's get straight into today's episode.

Yu Zhen 00:33
Hello, I'm Yu Zhen from CPF Board, and today we are delving deeper into retirement adequacy and planning for it, specifically for decumulation. We all know we have to save and plan to secure financial security for our retirement. This is known as the accumulation phase, where not only do we work, we also make our money work harder to beat inflation and harness the power of compounding. But when we retire, we need to move our focus from accumulating wealth to starting to draw down from our retirement funds. This is the decumulation phase, and we're excited to have Lorna Tan from DBS join us today to share her expertise on effective decumulation. Lorna is a seasoned financial educator and is currently Head of Financial Planning Literacy at DBS bank. Beyond her day job at the bank, she also educates young adults at the NUS business school as an adjunct professor on personal finance and is a best selling author of four books on financial literacy. Hello, Lorna!

Lorna 01:31
Hello Yu Zhen, I'm happy to be here today and excited to talk about retirement planning. Decumulation is not merely about spending wisely, but also converting assets into income streams. As you may know, our life expectancies are increasing. So lifelong income streams are an extremely important part of retirement planning.

Yu Zhen 01:52
Can you elaborate more on what you mean by lifetime income streams and how can we obtain it?

Lorna 01:57
Effective the accumulation goes beyond receiving monthly payouts from the CPF LIFE annuity scheme. It also includes converting our assets into income streams, some of which would be lifelong. Doing so helps to mitigate against longevity and inflation risks and ensures that I do not outlive my nest egg. As I got closer to retirement, I started building multiple income streams. They include annuity payouts, regular coupon payouts from bonds, dividends from REITs and unit trusts, payouts from income funds, rental income and other investments.

Yu Zhen 02:34
But to convert to income streams, we should first go back to the fundamentals of retirement and financial planning, which to me means planning early for my retirement, being a disciplined saver, and constantly

upskilling with financial knowledge. We should also understand what we want our retirement lifestyle to look like and how much money we need to support this. Do you have any tips on this, Lorna?

Lorna 02:56
I did begin planning in this manner. I started by imagining what my retirement lifestyle will be. I was in my 30s back then. So it was difficult to visualise and project accurately into the future. I found that what made it easier was to plan based on three retirement lifestyles of basic, moderate and luxurious. Back then I used an Excel spreadsheet and quantified the needs and wants and expenses for each lifestyle on the left side of the spreadsheet and review them every year. On the right side of the spreadsheet, I worked out the details of my financial resources such as income savings, CPF, insurance, investments, and others that can be used to meet the expenses.

Yu Zhen 03:39
And for those of us who don't want to use Excel, you can also check out the CPF planner, where you can input retirement goals and from there, it will tell you how much more you need in your CPF to achieve your retirement goals. You can find it on our CPF website.

Lorna 03:53
Yeah, there weren't any digital financial tools back then.

Yu Zhen 03:57
So being in CPF board right retirement planning has always been at the forefront of my mind. But for everyone else, I can imagine how it is very easy to get swept up with live with encounters that steer you away from your goals. So how do you keep yourself on track?

Lorna 04:12
Financial Security has always been a top priority for me. During my younger days, I focused on accumulating as much wealth as I can, based on my financial circumstances, risk profile and time horizon. That was my accumulation phase. As I reached my 50s, I built guaranteed and non-guaranteed income flows to fund my future expenses and managed my liabilities so that the housing loan would have been paid up by the time I reach my 50s. Doing so offers greater clarity on how much I require for my retirement.

Yu Zhen 04:44
I have heard some say that they don't know how much they need when they are older. How do you even quantify your expenses?

Lorna 04:50
I mentioned earlier that I worked out the needs and wants and the likely expenses for three retirement lifestyles, and it is prudent to review this regularly. I realised that as you get older and as circumstances change some wants become needs. For example, we had to stay home during the height of the COVID outbreak, and I started watching Netflix for entertainment. Since then, Netflix went from a want to a need.

Yu Zhen 05:16

For me too, traveling has become some sort of a need. I cannot imagine not traveling at least once a year. So how do you ensure there's enough savings to last for as long as the person lives?

Lorna 05:26
To ensure that I have enough to last my lifetime, I have to work out my must have income floor. This is the minimum monthly income or my must have amount to fund my needs. They should ideally be funded via more stable income flows, such as CPF LIFE payouts, annuity or retirement income insurance payouts and bond coupons regardless of the state of the economy and whether the market is up or down. I also realised that the older I get the more risk averse I become. Although I have the capacity and capability to take a more investment risk, the need to do so reduces over the years as more wealth is accumulated. This lower risk profile is reflected in a higher must have income floor. It will definitely cover all of my needs and some of my wants too.

Yu Zhen 06:19
I see that you mentioned that your must have income floor became higher as you adjusted your aspirations, and as you move to some wants to needs. So do we need to regularly review our retirement plans as we progress in life?

Lorna 06:31
Yes, and with inflation, our must have income floor will definitely change as well. So we need to stress test our financial planning. To achieve my desired higher must have income floor, I have accumulated sufficient financial resources to invest in safer products. This is reflected in a higher concentration in fixed income products in my portfolio as I got older. By planning for retirement early and reviewing it every year, I'm able to better allocate my savings into suitable investments to close the gaps.

Yu Zhen 07:05
Would you mind sharing your strategies for obtaining income in retirement?

Lorna 07:09
I have been focusing on building multiple income streams and they sit in these four pots. They are the decumulation, preservation, growth and legacy. For the decumulation pot, I will be drawing down my investments in this pot till they are depleted. They include payouts from CPF LIFE, supplementary retirement scheme withdrawals and insurance policies. In the preservation pot, the income flows will come from dividends, cash payouts, yields and rental income while keeping the capital some or principal amount intact. The investments include bonds, blue chip shares, REITs, income funds and real estate. The growth pot will comprise long term investments for more variable ones, as I'm looking forward to potentially higher returns in the future. Finally, the legacy pot will include assets for distribution to loved ones when I'm no longer around.

Yu Zhen 08:07
Having multiple income flows such as investment, rental income are definitely something to work towards. What about for members who may not have the extra income to start with?

Lorna 08:19

For those who have limited financial resources and limited capacity to take investment risks. The worst case scenario is to lose the little that they have. I believe the safest and most viable approach is to rely on CPF to build their nest egg. I would encourage them to understand how to maximise CPF schemes, such as the Matched Retirement Savings Scheme, and the new Majulah Package Earn & Save Bonus. Also, do contribute to CPF special account and retirement account through the CPF Retirement Sum Topping-Up Scheme to leverage the risk free interest rates and reap the benefits of compounding over time. Use tools like the DBS Your CPF feature to project their CPF payouts in the future against the estimated retirement sums of their age cohort. Other tools include CPF planner, and the CPF LIFE estimator to determine which CPF LIFE plan is suitable. Besides maximising the CPF schemes, they can consider investing surplus cash savings in suitable insurance plans and a diversified portfolio of investments that are aligned with the objectives risk profile and time horizon.

Yu Zhen 09:32
In addition to CPF and other financial products. I personally also think that it is important that we have cash on hand so that we are always ready for unexpected expenses. I will set aside about six times of monthly expenses for this and we'll continue to do so even when I'm retired.

Lorna 09:49
Yes, like you said it's good to ensure liquidity at all times. When I'm retired, I would have about three to six months worth of expenses in cash plus a pot of cash alternatives of another six months of expenses that can be turned into cash within a short period of time. Liquid assets include Singapore Savings Bonds, fixed deposits and balances in higher interest yielding bank accounts and cash management accounts.

Yu Zhen 10:15
After setting aside funds for retirement, I find it quite difficult to do a whole 180 degrees to move into spending mode. So how do you deal with it?

Lorna 10:23
I started by understanding my own money personality and acknowledging that I am a saver, and that I have an ingrained habit of deferring gratification and making sacrifices for the future. For example, whenever I buy something, I have an inner voice that will ask, is this a need or a want? This is still happening for me today. So it's difficult for me to transit from a saving to a spending mode automatically, just because I have the means to do so now, I have to keep reminding myself that this is the future that I have been working so hard for, and I can afford to relax and spend more than my usual. So I believe if you have done your homework, simulated your income flows under different scenarios, for example, a higher inflation rate and a longer lifespan, and if the math shows that you are financially comfortable, then consider enjoying the fruits of your labour now.

Yu Zhen 11:18
So when is a good time to start enjoying the fruits of labour? So for CPF, our payout start age is between 65 and 70. Is there an ideal age to start drawing down? Or should we only do so when we stopped working completely?

Lorna 11:32

I realised that to get the most out of life, the three basics that we need to have health, time and money. But for most people, these three seldom come together. When we are younger, most of us will have good health, more free time, but less money. At 65, we may have more money than 45. But our ability to do physical activities is diminished even if we are in great health. This is why I have redefined when my golden years are. They would include a good mix of health and wealth and be the period of maximum potential enjoyment. So these will be the years when I should be spending on what I value or bring happiness instead of delaying gratification and hoarding assets.

Yu Zhen 12:19
Thinking of retirement age in terms of the three basics is actually quite a fresh take. I've never thought of it this way. Most of the people I know work as long as they are able to which I understand because work is kind of like an anchor in their life. So it's nice that you have defined retirement like this.

Lorna 12:35
I believe that retirement age is not any single absolute number age we should aim towards. Rather this means that for those who have planned well, they ought to start spending their wealth instead of waiting till the CPF payout start age. Drawing down from your financial resources in your redefined golden years doesn't mean that you need to stop working. I like to think of it as easing into retirement in phases whenever we are financially ready, even before the official retirement age by starting to spend more than usual.

Yu Zhen 13:09
Spending more than usual even before retiring seems like quite an unconventional take.

Lorna 13:15
You can do this in a controlled manner. For instance, make a conscious effort to spend X amount each month or year of the spent budget that you have set aside for this stage of financial freedom. Personally, it doesn't mean having to spend on myself all the time, because I still stick to a simple lifestyle. But my spend can be in terms of better self care, creating memories by giving more treats to loved ones and friends and donating to charity.

Yu Zhen 13:43
Before we go, can we hear from you how your retirement plans have changed as you move through life? I personally believe that our financial or retirement planning journey is an iterative process. And being agile is important as we respond quickly to market and policy changes, but also reviewing plans with respect to personal needs as we move through life from new relationships and have different priorities. So Lorna, how have your retirement plans change over the years?

Lorna 14:11
One significant milestone in the last five years was turning 55 and having a CPF retirement account. I've been planning for retirement or financial freedom since my 30s. So when I turned 55, and as I moved nearer to my retirement, it is exciting to put into place a system of multiple income flows to fund my golden years with the foundation made up of CPF income flows. I have been topping up my CPF retirement account to the prevailing enhanced retirement sum each year after turning 55. This will mean higher

monthly CPF LIFE payouts of about $2,300 when I turn 65. I still have a healthy balance in my special account that attracts at least 4% interest per annum. My plan is to use it like an ATM. I will withdraw just the interest component every year, leaving the principal amount in the special account. During the last five years, I paid up my housing loan and car loan so I became debt free. All this time, I continue to stay invested in equities for potentially higher capital appreciation in the future.

Yu Zhen 15:21
What about health care and legacy planning?

Lorna 15:24
I'm glad you asked this. As part of retirement planning, long term care and legacy planning are important focus areas. I'm enrolled in CareShield Life, and I've also reviewed my will, CPF nominations and the lasting power of attorney. I encourage everyone to get started on estate planning if you have not done so. Besides the financial aspects of retirement, it's important to understand what's your life purpose, and also what you hope to accomplish during your retirement? Well, I plan to spend more time with my aging parents, travel, exercise, and learn how to cook. I've also realised that there are advantages to sticking to a more structured lifestyle and keeping to a routine. I will continue to contribute to the financial literacy space, and stay engaged with the community for mental stimulation via projects and part time work such as workshops and lecturing.

Yu Zhen 16:19
Thank you so much, Lorna for sharing these useful tips for decumulation today.

Lorna 16:24
Thank you, Yu Zhen. Happy to share!

Yu Zhen 16:26
And here are some key takeaways from this session. We can consider a multi prong approach to retire well by redefining your golden years. Empower yourself with financial knowledge, inculcate this discipline to exercise and eat well, and understand what gives you purpose in your life. And with that you have been listening to Let's Talk CPF.

CPF Board 16:48
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