

# **HOW TO OPTIMIZE YOUR RETIREMENT BUDGET**

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# INTRODUCTION

Many people fear running out of money in retirement. With the financial landscape constantly changing, this should come as no surprise. However, by creating and following a budget you can control and reduce the risk of depleting your assets sooner than expected. A budget outlines the funds you have coming in and how you plan on using those funds to cover your expected (and unexpected) expenses. This process helps define your needs and how your needs will be met.

# AGENDA

- Back to the basics: Budgeting in Retirement
- New Budgeting Approaches
  1. Personal consumption index
  2. Social Security as a part of Bond Portfolio
  3. Roth Conversions to reduce RMDs
  4. Allocate a part of portfolio for Long Term Care
- Conclusion



**68% OF OLDER ADULTS SAY  
THEIR OVERALL EXPENSES  
HAVE RISEN ABOUT 10%  
SINCE A YEAR AGO.**

Senior Citizens League



# **BACK TO THE BASICS**

Revisit your current budget



# CASH IN-FLOW

## PRE-RETIREMENT INCOME

- W-2 Income
- 1099 Income (Freelance or Consulting or Contract Work)
- Bonuses
- Commissions
- Stock compensation
- Passive income: Rental

## POST-RETIREMENT INCOME

- Social Security
- Pension
- Interest/Dividends
- Retirement Portfolio
- Passive income: Rental



# CASH OUT-FLOW

## PRE-RETIREMENT EXPENSES

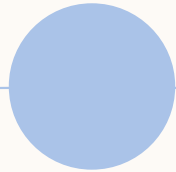
- Utilities
- Mortgage payments
- Car payments
- Credit card payments
- Child expenses (e.g., food, clothes, school, activities, insurance)
- Meals in and out

## POST-RETIREMENT EXPENSES

- Utilities
- Housing (property taxes and insurance)
- Travel expenses
- Medical expenses
- Recreational / Educational
- Meals in and out

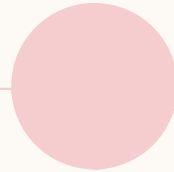


# CONTEMPORARY BUDGETING: A PRIMER



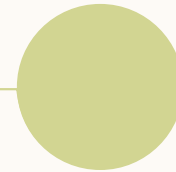
## NEEDS 50%

- These are expenses that must be met no matter what, such as: utilities, housing, healthcare, food, transportation.



## WANTS 30%

- These are things you enjoy that you spend money on by choice: subscriptions, supplies for hobbies, restaurants, vacations.



## SAVINGS 20%

- The remaining 20% of your budget should go toward the building your retirement nest egg.

# RETIREMENT BUDGETING

- **Needs 50%**
- **Housing**
- **Food**
- **Medical**
- **Transportation**
- **Wants 50%**
- **Travel**
- **Education**
- **Recreational**
- **Hobbies**
- **Passion Projects**
- **Charitable giving**

# SAMPLE BUDGET: \$5000

- **Needs 50% - \$2500**
- **Housing – \$1100\***
- **Food - \$500**
- **Medical (O/P) – \$50**
- **Auto Insurance - \$100**
- **Transportation - \$250**
- **Taxes - \$500**
- **Wants 50% - \$2500**
- **Travel - \$1000**
- **Education - \$50**
- **Recreational - \$350**
- **Entertainment - \$350**
- **Grandkids - \$250**
- **Charitable Giving - \$500**

\*Assumes mortgage is paid off

# HOW TO SET YOUR BUDGET

1. List your expected income
2. List your expected expenses
3. Consider variable expenses
4. Factor in lifestyle changes
5. Set up a spending plan you can track (and edit)
6. Execute the plan

# START TRACKING



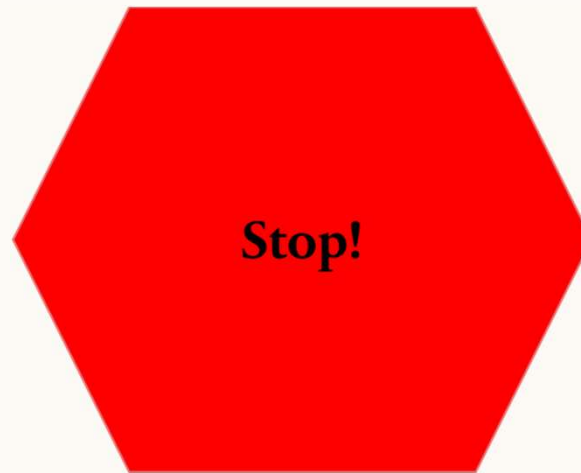


# **EMERGENCY SAVINGS?**

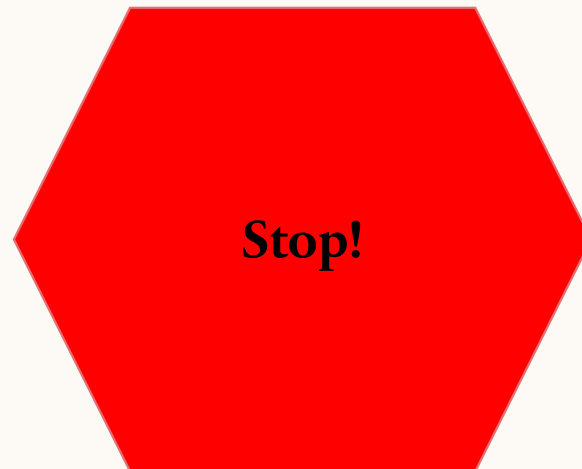


**Stop!**

# **FLOOR SET?**



# **DISTRIBUTION RATE?**







# **1. PERSONAL CONSUMPTION INDEX**

Determine your personal inflation rate

# DO YOU KNOW IF YOUR MONEY IS KEEPING UP?

**CPI Inflation Calculator**

\$

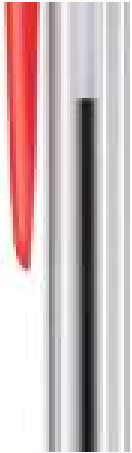
in

has the same buying power as

in

Avg 3.57% per year

# THE POWER OF \$1 IN 2000



**98 CENTS**

Ball Point Pen



**98 CENTS**

2 liter Soda



**33 CENTS X 3**

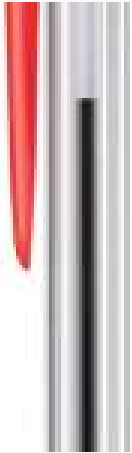
3 stamps



**99 CENTS**

A loaf

# THE POWER OF \$1 IN 2024



**\$4.72**

Ball Point Pen



**\$2.68**

2 liter Soda



**68 CENTS X 3**

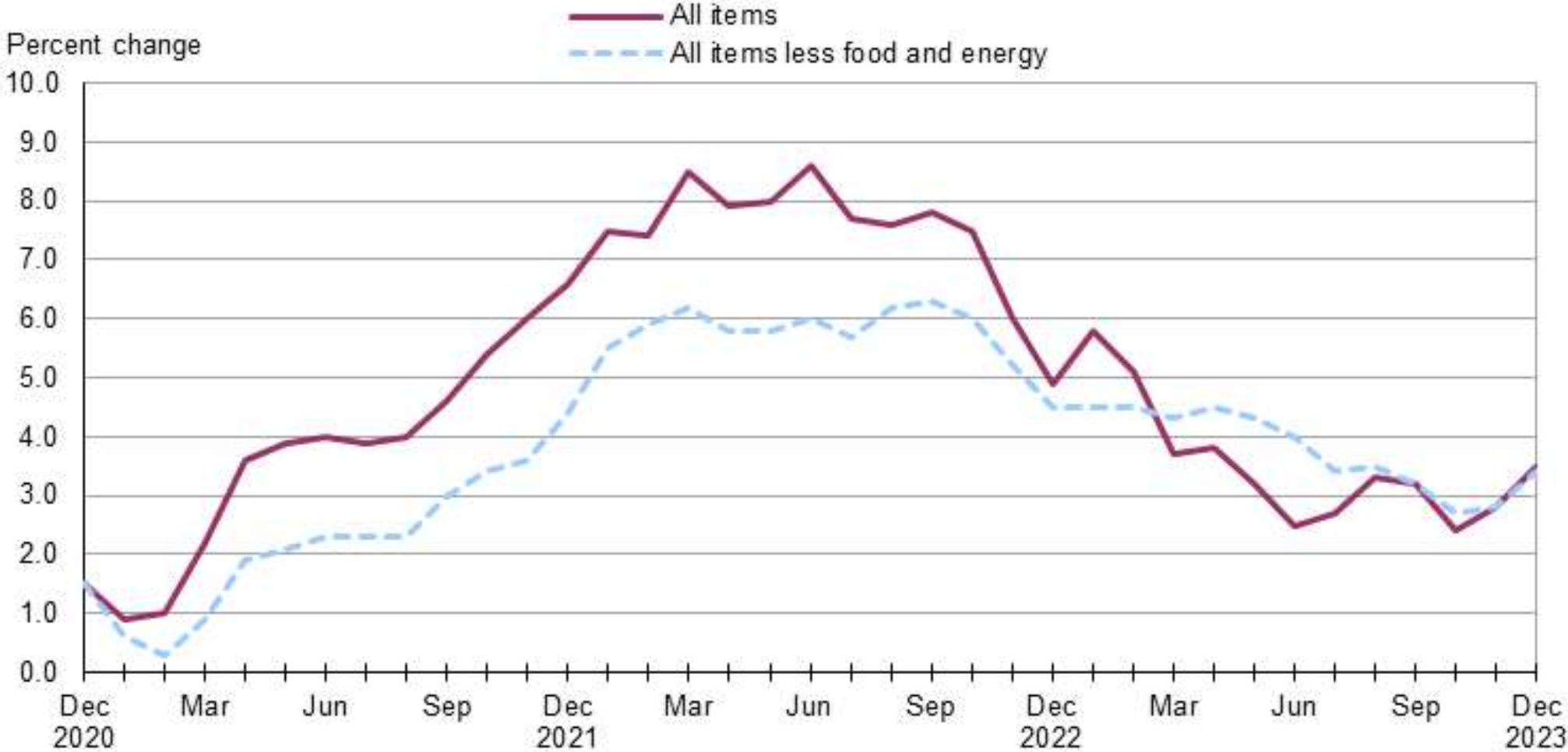
3 stamps



**\$3**

A loaf

**Chart 1. Over-the-year percent change in CPI-U, Los Angeles-Long Beach-Anaheim, CA, December 2020–December 2023**



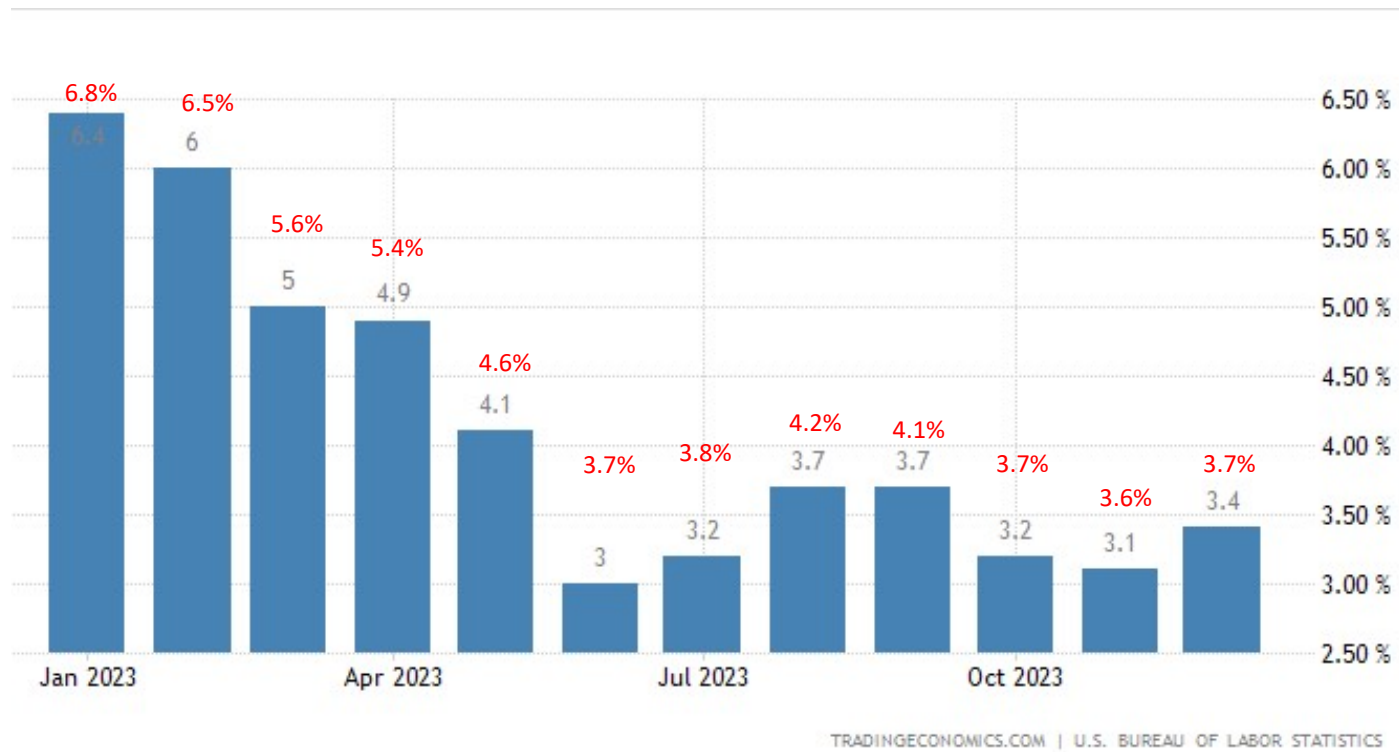
Source: U.S. Bureau of Labor Statistics.

## Consumer Price Index for Americans age 62+

3.7%

Month	All items	Food and beverages	Housing	Apparel	Transportation	Medical care	Recreation (1)	Education and communication (1)	Other goods and services
December 2022	322.838	322.352	327.600	122.450	270.857	572.331	149.927	119.905	468.747
January 2023	325.520	324.686	330.768	125.362	273.123	573.873	151.220	120.417	472.092
February 2023	327.499	326.139	332.944	129.569	275.121	572.689	153.048	120.688	476.354
March 2023	328.457	326.202	333.901	130.376	277.584	571.722	153.878	120.633	478.698
April 2023	329.868	326.867	334.785	128.834	282.907	571.696	154.419	120.561	483.798
May 2023	330.663	327.414	335.706	128.642	284.187	572.610	154.559	120.303	486.111
June 2023	331.791	327.575	337.554	127.821	285.683	573.329	154.454	119.924	487.240
July 2023	332.545	328.530	338.703	126.365	286.371	573.526	154.592	120.022	486.862
August 2023	334.032	329.073	339.847	128.258	290.501	575.448	154.294	120.100	489.019
September 2023	335.069	329.633	341.692	130.072	289.486	576.104	154.741	120.181	491.336
October 2023	335.102	330.614	342.088	130.356	287.132	576.698	154.692	119.998	494.279
November 2023	334.876	329.970	343.074	126.310	284.129	578.671	154.014	119.540	495.522
December 2023	334.758	330.126	343.991	123.374	280.128	580.395	154.586	119.676	494.331

# CPI (All Urban) vs R-CPI-E (Ages 62+)



\*R-CPI-E is represented by the red percentages



Expense Type	Category	Amount spent (August 2023)	Amount spent (August 2024)	% of total amount	12-month inflation rate
Home	Rent	\$0	\$0	0%	0.0%
Home	Mortgage and property taxes	\$0	\$0	0%	0.0%
Home	Electricity/heating	\$0	\$0	0%	0.0%
Home	Water and trash service	\$0	\$0	0%	0.0%
Home	Telephone service	\$0	\$0	0%	0.0%
Home	Internet service	\$0	\$0	0%	0.0%
Home	Home furnishings and supplies	\$0	\$0	0%	0.0%
Essentials	Groceries	\$0	\$0	0%	0.0%
Essentials	Clothing	\$0	\$0	0%	0.0%
Essentials	Personal care (haircuts, bath products, cosmetics, etc.)	\$0	\$0	0%	0.0%
Auto/transportation	Gasoline	\$0	\$0	0%	0.0%
Auto/transportation	Auto maintenance/repair	\$0	\$0	0%	0.0%
Auto/transportation	Auto insurance	\$0	\$0	0%	0.0%
Auto/transportation	Registration/license fees	\$0	\$0	0%	0.0%
Auto/transportation	Parking/tolls	\$0	\$0	0%	0.0%
Auto/transportation	Cab fare/mass transit	\$0	\$0	0%	0.0%
Travel	Airfare	\$0	\$0	0%	0.0%
Travel	Hotels/other lodging	\$0	\$0	0%	0.0%
Travel	Car rental	\$0	\$0	0%	0.0%
Medical	Drugs and medical equipment	\$0	\$0	0%	0.0%
Medical	Medical services	\$0	\$0	0%	0.0%
Medical	Health insurance	\$0	\$0	0%	0.0%
Education/child care	School tuition, activity fees, etc.	\$0	\$0	0%	0.0%
Education/child care	Day care/nanny	\$0	\$0	0%	0.0%
Recreation/leisure	Dining out/takeout	\$0	\$0	0%	0.0%
Recreation/leisure	Recreation goods (electronics, pets, sporting goods, toys, etc.)	\$0	\$0	0%	0.0%
Recreation/leisure	Recreation activities (streaming services, pet services, movies, concerts, sporting events, etc.)	\$0	\$0	0%	0.0%
Other	Legal and financial services	\$0	\$0	0%	0.0%
<b>TOTAL:</b>		<b>\$0</b>	<b>\$0</b>	<b>Total 12-month Personal Inflation Rate:</b>	<b>0.0%</b>





## **2. SOCIAL SECURITY AS A PART OF BOND PORTFOLIO**

Re-Evaluate your income portfolio



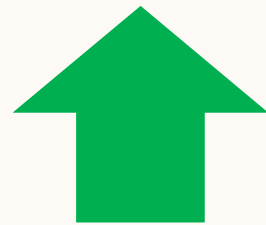
# WHAT ROLE DO BONDS HAVE IN YOUR PORTFOLIO?

1. Reduces volatility in your portfolio (diversification)
2. A bond issuer's promise to pay bondholders a fixed rate of interest
3. Generates predictable income and bolster a higher total return
4. Government Bonds are considered to have little to no default risk
5. Corporate Bonds add an element of risk leading to a higher yield
6. Duration of the bond controls the yield guaranteed

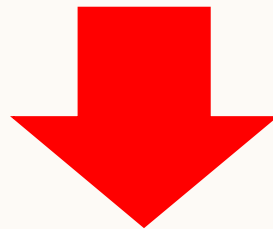


# WHAT ABOUT SOCIAL SECURITY?

- Produces income like a bond
- Income is adjusted for inflation like a treasury inflation protected bond
- It is a government issued income vehicle like a government bond
- The late John Bogle, the founder of Vanguard, was allegedly a fan of using Social Security benefits as a bond in one's portfolio.



Yes



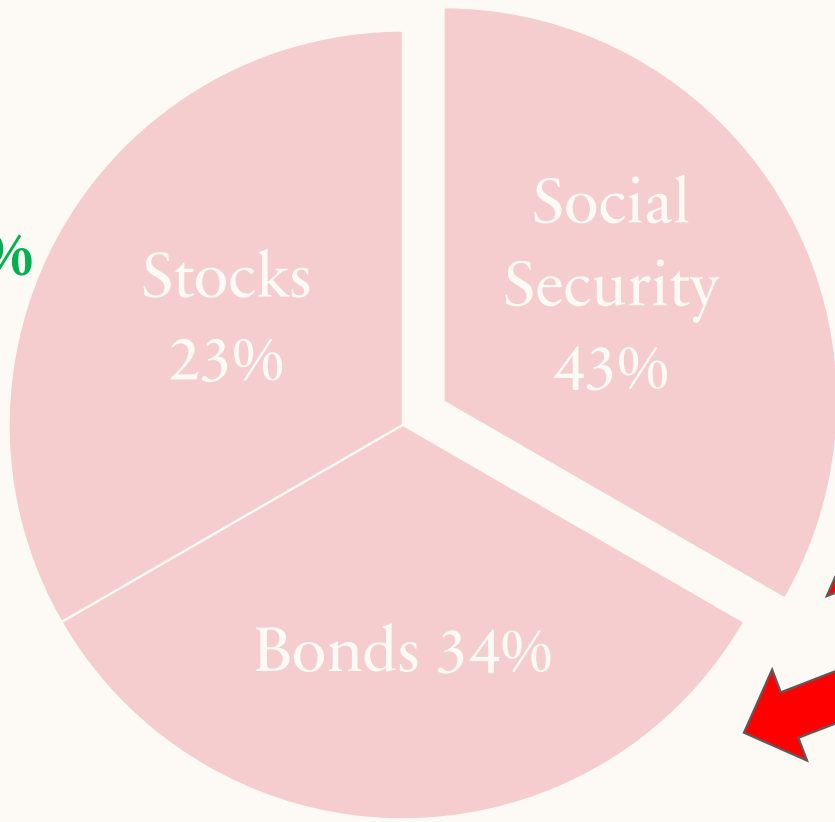
No

# HOW WOULD THAT WORK?

- Start with a conservative yield from a bond, say 4% per year and reverse engineer the payment to get the hypothetical balance. In other words, if you are receiving \$2,500 for Social Security, divide  $\$2,500 \times 12 / 4\% = \$750,000$  bond.
- If you have 40% Stock worth \$400K /60% Bond Portfolio worth \$600K, adding \$750K to the Bond would bring the total Bond portfolio to \$1.35 MM.
- The new allocation would be 23% Stocks /77% Bonds

★ **Planner's Side Note:** Start by asking how much income you need to generate from your portfolio (include income that is also generated by dividends). If the combination of bonds and social security generates enough income for you to satisfy your monthly, quarterly, and annual financial obligations, then you can increase your stock (equity ETF or MF) exposure to max out up to the original allocation of 40/60.

  
**Increase by 17%**



  
**77% of Safety**

# 25% STOCKS AND 75% BONDS

	Average Annual Return	Best Year	Worst Year	Best average annual return over 3 years	Worst average annual return over 3 years
Portfolio A	4.3%	7.8%	-2.0%	6.8%	1.7%
Portfolio B	5.2%	10.0%	-3.2%	8.3%	3.4%
Portfolio C	6.1%	14.1%	-11.7%	9.9%	1.2%
<a href="#">Portfolio D</a>	6.5%	16.2%	-15.9%	11.7%	0.1%
Portfolio E	7.0%	18.6%	-20.1%	13.5%	-0.9%
Portfolio F	7.9%	25.5%	-28.6%	17.1%	-3.1%
Portfolio G	8.8%	32.4%	-37.0%	20.7%	-5.2%

# 55% STOCKS AND 45% BONDS

	Average Annual Return	Best Year	Worst Year	Best average annual return over 3 years	Worst average annual return over 3 years
Portfolio A	4.3%	7.8%	-2.0%	6.8%	1.7%
Portfolio B	5.2%	10.0%	-3.2%	8.3%	3.4%
Portfolio C	6.1%	14.1%	-11.7%	9.9%	1.2%
<a href="#">Portfolio D</a>	6.5%	16.2%	-15.9%	11.7%	0.1%
Portfolio E	7.0%	18.6%	-20.1%	13.5%	-0.9%
Portfolio F	7.9%	25.5%	-28.6%	17.1%	-3.1%
Portfolio G	8.8%	32.4%	-37.0%	20.7%	-5.2%



# ALLOCATION MATTERS

Percentage Allocation			Rate of Return		Rate of Return
Cash	10%	X	0.01%	EQUALS	0.01%
Stocks	40%	X	7.00%	EQUALS	2.80%
Bonds	50%	X	4.00%	EQUALS	1.60%
				Gross	4.40%

# REAL (AFTER-TAX) RETURN

Portfolio Real Return		
	4.40%	
Minus	0.05%	Fees
	4.35%	
Minus	0.87%	Taxes
	3.48%	
Minus	3.40%	Inflation
Equals	<b>0.08%</b>	



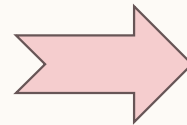
# **3. ROTH CONVERSIONS TO REDUCE RMDS**

Assume Higher tax rates

# PERSONAL INCOME TAX RATES

## BEFORE TCJA

- 10%
- 15%
- 25%
- 28%
- 33%
- 35%
- 39.6%



## AFTER TCJA

- 10%
- 12%
- 22%
- 24%
- 32%
- 35%
- 37%

# REVIEWING YOUR PERSONAL CASHFLOW

Cash Inflows				Cash Outflows				
<u>Income Inflows</u>	<u>Planned Distribution</u>	<u>Other Inflows</u>	<u>Total Inflows</u>	<u>Expenses</u>	<u>Goals</u>	<u>Tax Payment</u>	<u>Planned Saving</u>	<u>Total Outflows</u>
\$60,000	\$0	\$36,000	\$96,000	\$48,000	\$10,000	\$10,000	\$0	\$68,000

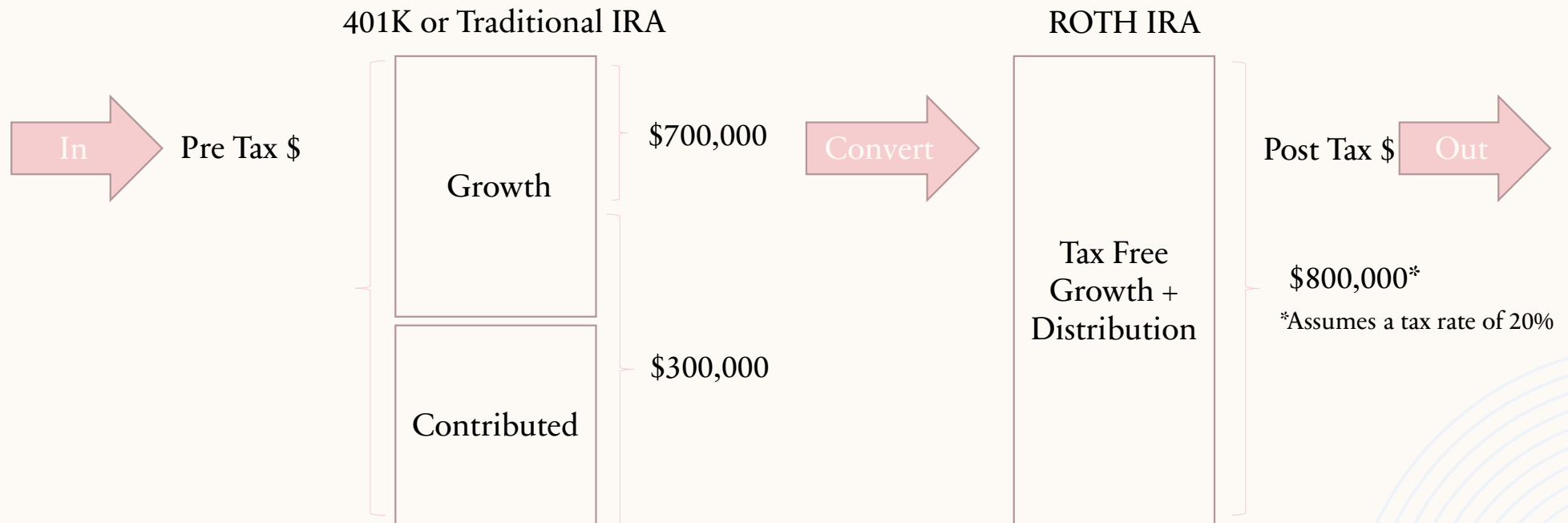
# REVIEWING YOUR PERSONAL CASHFLOW

Cash Inflows				Cash Outflows				
<u>Income Inflows</u>	<u>Planned Distribution</u>	<u>Other Inflows</u>	Total Inflows	<u>Expenses</u>	Goals	<u>Tax Payment</u>	Planned Saving	Total Outflows
\$60,000	\$40,000	\$36,000	\$136,000	\$48,000	\$10,000	\$18,000	\$0	\$76,000

# ROTH CONVERSIONS

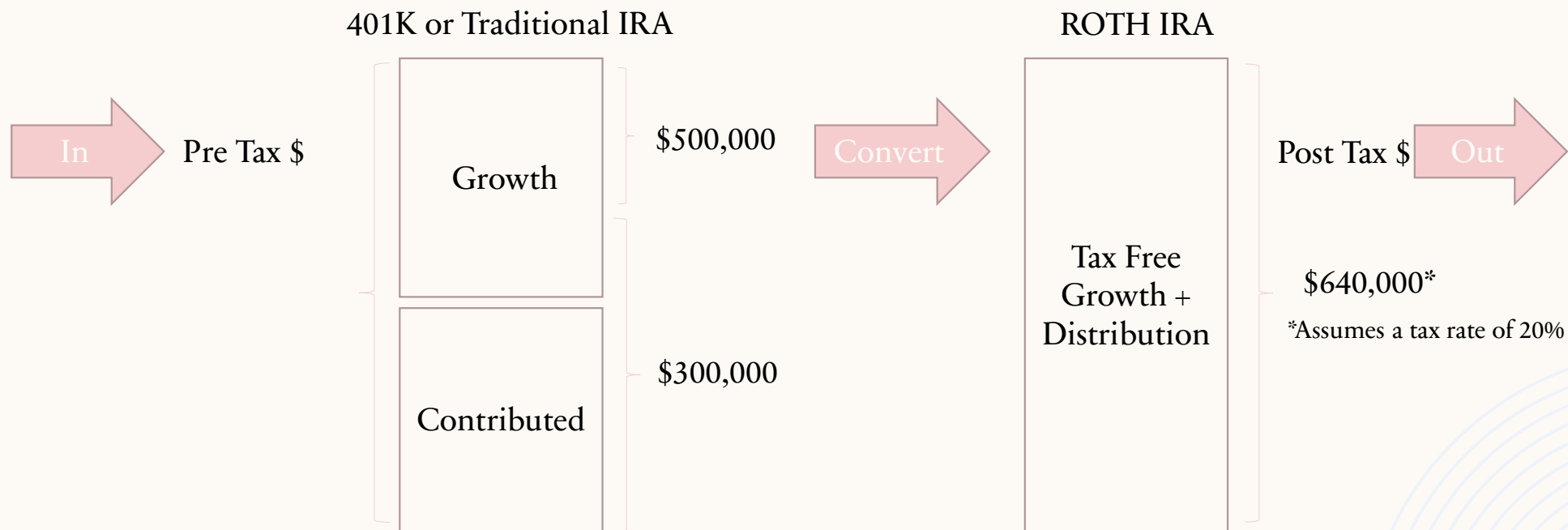
- **What is it?** It involves moving assets from your tax deferred account like an IRA or 401K plan into a ROTH IRA so that you can continue growing your money tax deferred but more importantly to take tax free distributions
- **Who is it for?** Anyone who has enough income (outside of retirement accounts) to satisfy monthly obligations and believes tax rates will rise in the future and do not want to worry about forced retirement distributions at a higher tax rate (**Caveat:** Not for those who need the distributions from retirement accounts as soon as they retire)
- **Why should I consider it?** If you believe that tax rates will be higher in the future, then it may be prudent to look for ways to reduce annual taxable income
- **When:** It is best if you can start performing the conversion early in retirement so that you have more options to evenly spread out your conversions over time. Or you can stagger your conversions for certain events like a down market or a year when your income is lower than usual

# Basic Roth Conversion Illustration

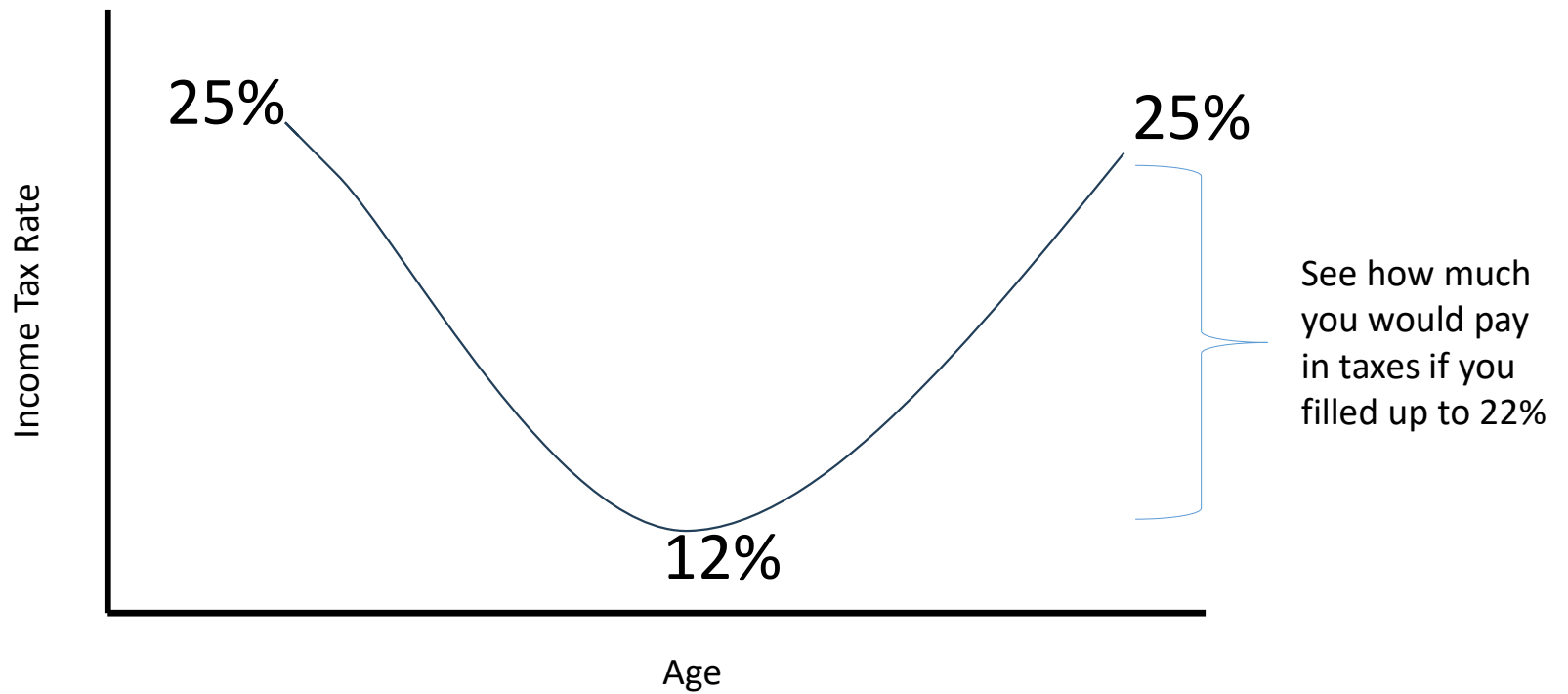




# During a Down Market (-20%)



# During an income valley



# PERSONAL INCOME TAX RATES

The key is to perform incremental conversions that distributes the tax liability over time without pushing you into the next tax bracket.

Convert enough to fill up your current tax income tax bracket and see if you can afford to pay the extra taxes.

Tax Rate	Single	Married filing jointly	Married filing separately	Head of household
10%	\$0 to \$11,600.	\$0 to \$23,200.	\$0 to \$11,600.	\$0 to \$16,550.
12%	\$11,601 to \$47,150.	\$23,201 to \$94,300.	\$11,601 to \$47,150.	\$16,551 to \$63,100.
22%	\$47,151 to \$100,525.	\$94,301 to \$201,050.	\$47,151 to \$100,525.	\$63,101 to \$100,500.
24%	\$100,526 to \$191,950.	\$201,051 to \$383,900.	\$100,526 to \$191,950.	\$100,501 to \$191,950.
32%	\$191,951 to \$243,725.	\$383,901 to \$487,450.	\$191,951 to \$243,725.	\$191,951 to \$243,700.
35%	\$243,726 to \$609,350.	\$487,451 to \$731,200.	\$243,726 to \$365,600.	\$243,701 to \$609,350.
37%	\$609,351 or more.	\$731,201 or more.	\$365,601 or more.	\$609,350 or more.



# SHOULD OR SHOULD NOT

## PROS

- Reduce or eliminate RMDs
- Tax free distributions for you
- Tax free distributions for your beneficiaries

## CONS

- Pay taxes on the deferral
- Potentially raise taxes on Social Security benefits or Medicare Part B/D premiums
- You may not have the money to pay for the conversion tax
- Plan on giving to charity through a Qualified Charitable Distribution



## **4. ALLOCATE A PART OF PORTFOLIO FOR LONG TERM CARE**

Take holistic approach to fund LTC



# **MEDICARE WILL COVER ALL HEALTHCARE COSTS**

- Anonymous

# MEDICARE PLAN PACKAGE

Part A – Hospital  
Insurance

Part B – Medical Insurance

Medi-Gap

Part C – Medicare  
Advantage

Part D – Drug Coverage

# STATISTICS

70% of adults aged 65 years and older will require long term care at some point

\*The average length of stay in long term care is 3.3 years for women and 2.2 for men

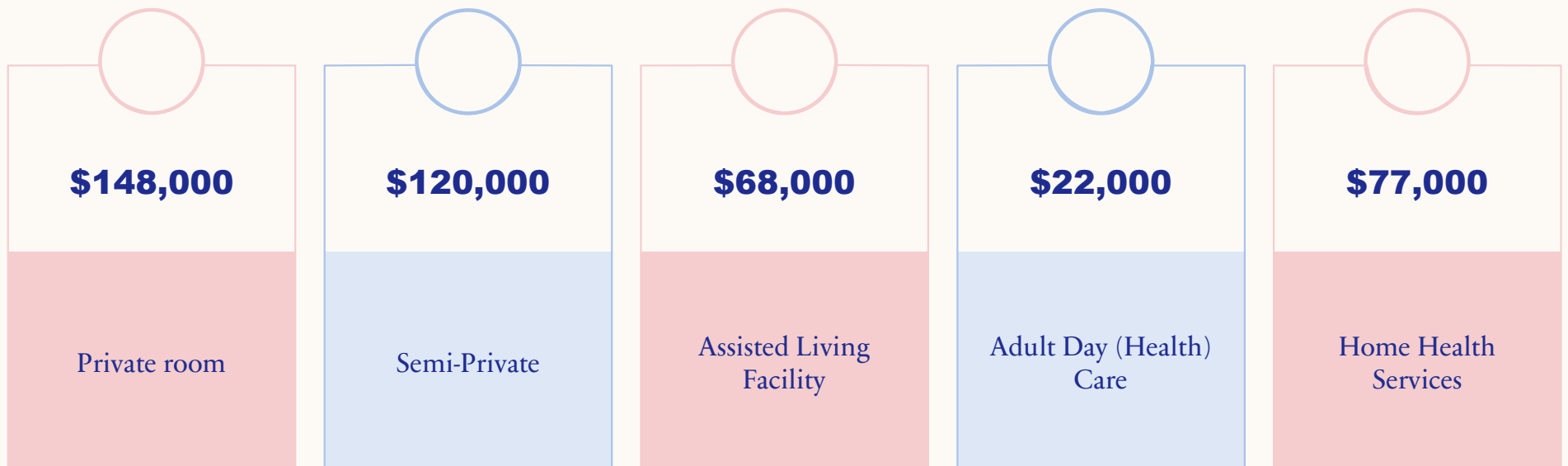
Americans spend \$475.1 billion annually on long term care

Medicaid only covers 42% of America's long term care costs

\*20% or less will require care for 5 years or longer



# ESTIMATED ANNUAL COSTS



# FUNDING OPTIONS

There are four main sources for financing long term care (outside of self-funding):



LTC Insurance Policy



Hybrid Life Insurance (LTC Rider)



Hybrid Annuities (LTC Rider)



Medi-Cal

# ALTERNATIVE OPTIONS



Downsize and use a portion of the capital gains exclusion amount



Directing RMDs into a balanced portfolio inside taxable brokerage account exclusively used for LTC



Combination w/ order of operation: (1) Self Fund (2) RMDs (3) Exclusion on capital gains after downsize (4) Medi-Cal

# LONG TERM CARE TAX

## Background:

- In 2019 Gavin Newsom approved Assembly Bill 567 establishing a committee to investigate the rising cost of long-term care
- The task force was also formed to evaluate the creation of a state funded insurance program requiring residents to pay an increased payroll tax of 0.40 to 0.60%

## Latest Update

- December of 2023, the task force has been disbanded after completing a report that presented five different LTC programs
- As of the start of 2024, there has been no bill introduced by CA legislators



**STAY TUNED!**

# SUMMARY

Optimizing retirement income and expenses require taking a holistic approach which includes applying “outside the box” methodologies. Maximizing return on savings and investments during a workers accumulation years is vital. But equally important is the decumulation process, when you spend those savings and investmetns in the form of income. And to ensure your money will last, you need to start by looking at your cashflows and being able to be flexible enough to adjust with the changing environment.

# THANK YOU

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