



FUNDAMENTAL
WEALTH



HARBOURFRONT
WEALTH MANAGEMENT

THE RETIREMENT INCOME BLUEPRINT:

A STEP-BY-STEP GUIDE



Your complete guide to creating
a sustainable retirement income



Your Complete Guide to Creating a Sustainable Retirement Income

Do you know how much your retirement will cost? Have you considered how you will pay for it?
Do you know how to generate the income you will need?

For many current and future retirees, these can be stressful questions which are often put off and left unanswered for too long.

Fundamental Wealth manages money for hundreds of Canada's affluent and successful people. We help our clients with many things, but one of the most important is helping them answer the aforementioned questions and meet their retirement goals.

We've written this guide in an effort to help you answer these fundamental retirement questions for yourself.

Why have we provided this guide at our own expense? We've found that educating and empowering retirees is good for our business, whether the individual becomes a client or not.

For some, our outstanding client service is an attractive reason to become a client. Others simply want to take our insights and use them on their own. Whichever group you fall into, we sincerely hope this guide helps you reach your retirement goals.



What Are Your Retirement Goals?

What is your plan for retirement? Enjoy the golf course? Travel? Spend time with the grand children? Keep on working, but purely for fun?

In our experience, there is an immense diversity in how our clients want to spend their retirement. But from a financial perspective, we've found most people are aiming to achieve one (or often more) of the following four goals. And before you focus on anything else, it is imperative you figure out what your goals are for retirement.

Avoid running out of money?

For many this is their number one goal - and their number one retirement fear. Being forced to turn to your children - or go back to work - during retirement is a source of anxiety for many current and future retirees. Many folks think the key to achieving this goal is very low-volatility investments (e.g. Guaranteed Investment Certificates or GICs), but we will discuss this is not always the case.

Maintain or improve lifestyle?

Most people have worked hard for their retirement and want to enjoy it. As such, a common goal for many clients is to maintain - or better yet, improve - their lifestyle during retirement. The key here is to maintain or grow purchasing power over time - this requires income growth to offset the malicious impact of inflation.

Increase wealth?

Some folks are easily and able to enjoy the retirement lifestyle of their choosing with no fear of running out of money. For those fortunate individuals and families, the goal is often to grow their wealth over the long term - typically for legacy, whether that's children, grandchildren or charity. Unsurprisingly, most people with this goal take a growth-orientated approach to their investments.

Spend every cent?

This isn't a typical goal among our clients, but there are some people who think success is spending all of their money before they die. But this is often a risky proposition - there is no way to know exactly how long your retirement will last, and people who attempt this may find themselves out of money sooner than they think.

Before you focus on anything else, figure out which of these goals are the most important to you. You can't figure out how to get there if you don't know where you are going!



How Much Will Retirement Cost?

Once you've figured out what your goals are for retirement, you can start to calculate how much your retirement will cost. Four factors to consider are: non-discretionary spending, discretionary spending, inflation and your investment time horizon (e.g. Life expectancy).

Non-Discretionary Spending

This is spending you don't have a lot of control over. There may be some wiggle room, but for the most part you can't avoid these costs.

- **Living Expenses:** Day-to-day, how much does it cost to maintain your lifestyle? You'll want to consider everything from groceries, to gas to the heating bill. If you aren't planning on relocating in retirement, you likely have a good idea of what these expenses already look like.
- **Debt:** This can be credit card debt, your mortgage or car loans. Anything you owe needs to be accounted for when mapping out your expenses because you'll have to continue to pay down the principal and make periodic interest payments.
- **Taxes:** While taxes are often lower for retirees as they shift from working full-time, the government still wants its cut. You'll want to keep money set aside to settle your tax bill and the end of the year or calculate the approximate tax withholding to remit monthly.

Discretionary Spending

Once you get past the basic living expenses, you have to account for discretionary spending. Discretionary spending is subject to your personal situation. You may view cable TV as discretionary, but golf as a required, non-discretionary expense. This is just an example, but the takeaway is if you have a hobby or other expense you can't imagine living without, you'll need to include it in your non-discretionary expenses. Below are some examples of common discretionary line items in a retiree's budgets.

- **Travel:** Many people look forward to travelling in retirement. This could include visiting the grandkids or more elaborate trips overseas. If you've been thinking about a dream trip for years, now could be an ideal time to budget for one.
- **Hobbies:** Retirement is a great time to rekindle old hobbies or pick up new ones. Ready to finally get your fly casting down or finish researching your family history? Hobbies almost always incur some costs, even if many are small.
- **Luxuries:** This is somewhat subject to your budget and definition of luxury. But whether you enjoy fine wines or simply having a coffee out every morning, you'll need to factor in non-essential purchases into your expenses.
- **Children and Grandchildren:** For many, this last category includes aspects of all the others. Your family could require travel, luxury purchases and be your favorite hobby all at once. If you need a generous budget to make children and grandchildren a focus in your retirement, you'll need to think about how much cash flow you'll need to support it.



Inflation

Inflation is insidious. It decreases purchasing power over time and erodes real savings and investment returns. Many investors fail to realise how much impact inflation can have. Since 1925, inflation has averaged 3% a year.* If that average inflation continues in the future, a person who currently requires \$50,000 to cover annual living expenses would need approximately \$90,000 in 20 years and about \$120,000 in 30 years just to maintain the same purchasing power.

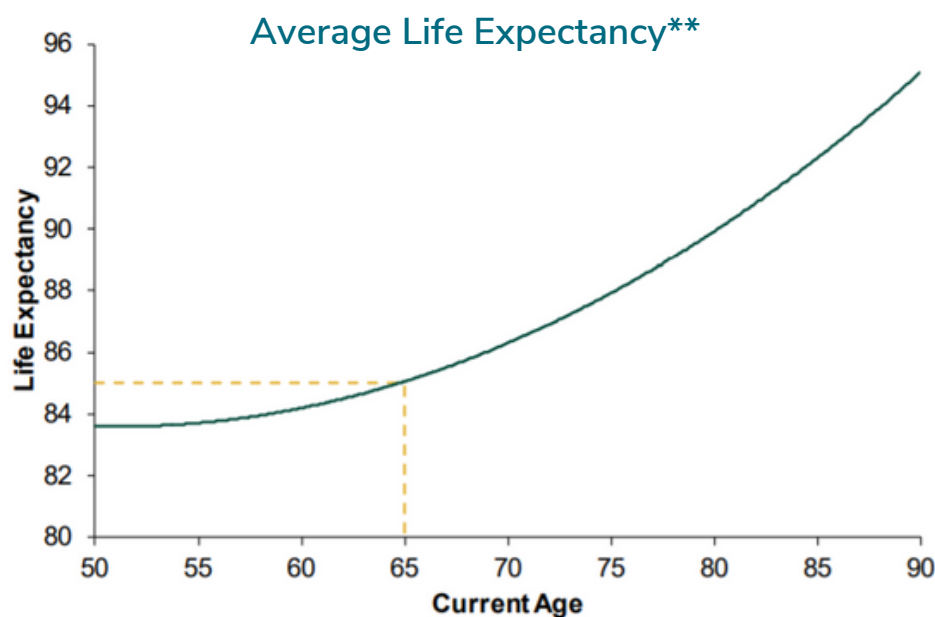
The following table shows total life expectancies for Canadians, based on current age. We believe these projections likely underestimate how long people will actually live given ongoing medical advancements.

Don't forget these are projections of average life expectancy - planning for the average is not sufficient because about half of people in each bracket are expected to live even longer. Factors such as current health and heredity can also cause individual life expectancies to vary widely.

Time Horizon

Your investment time horizon is a major determinant of your total retirement cost and is likely one of the most overlooked factors among today's retirees - fact is, most folks are living longer than they think they will. Investment time horizon can be your life expectancy, the life expectancy of a younger spouse, or a longer or shorter time horizon depending on your investment objectives.

The bottom line? Your investment time horizon may be much longer than you realize. Prepare to live a long time and make sure you have enough money to maintain your lifestyle.



Your goals, expense needs and time horizon all factor into how you should approach generating income in retirement. Next, let's examine some techniques you can consider for getting the cash flow you need.

*Source: FactSet, as of 03/12/2017/ Based on Canadian Consumer Price Index from 1925-2016

**Source: Statistics Canada, Demographic Division, Life tables.(Revised as of 25/09/2013)



How Will You Pay for Retirement?

Once you have a sense of how much your retirement will cost, you can start figuring out how you're going to pay for it. We suggest you calculate all of the income you generate without relying on your investments. The most common categories of non-investment income are listed below:

Non-Investment income

- **Salary:** Will you work at all in retirement? If, so, you'll need to estimate how much salary you can expect. For our purpose, don't count money you make from a business investment partnership; just consider direct financial transfer from your employer to you.
- **Pension:** If your employer offers a pension, you should determine how much you can expect to receive on a regular basis. Note, RRSPs and TFSAs are not pension plans. Rather, they are types of accounts that hold funds you've invested over the years and will be able to control in retirement.
- **Canada Pension Plan:** If you've started collecting from CPP, you're familiar with how much to expect. If you haven't yet, you'll want to determine the age you want to start receiving benefits and how much you should expect monthly. The Government of Canada's website* has a free calculator you can use to estimate your future benefit.
- **Business and Real Estate:** If you maintain an interest in a business or investment property, this could produce non-investment income. When calculating how much to expect, consider these sources of income are more susceptible to market conditions than guaranteed pensions.

If you are interested in learning more about optimizing CPP and other government benefits, check this book → [Maximizing Government Pension Plans and Create a Sustainable Retirement Income.](#)



*<https://www.canada.ca/en/services/benefits/publicpensions/cpp/retirement-income-calculator.html>



Determine What You Need from Your Portfolio

Now that you've determined what your expenses are likely to be and how much non-investment income to expect, the worksheet below can help you put it all together.

INCOME

Non-Investment Income

Salary	\$	
Pension	\$	
Canada Pension Plan	\$	
Business & Real estate	\$	
Other	\$	
TOTAL INCOME	\$	

EXPENSES

Non-Discretionary Spending

Basic Living	\$	
Mortgage	\$	
Credit Card / Loans	\$	
Taxes	\$	
Insurance	\$	
Non-Discretionary Subtotal	\$	

Discretionary Spending

Travel	\$	
Hobbies	\$	
Luxuries	\$	
Gifts to Family/Charity	\$	
Others	\$	
Discretionary Spending Subtotal	\$	

TOTAL EXPENSES: (Add both subtotals)	\$	
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NET SAVINGS

(Subtract Total Expenses from Total Income)	\$	
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Using Your Investments to Pay for Your Retirement

The difference between your total income and your total expenses is your net savings. If this number is negative (as it is for many affluent retirees), you'll need to more cash flow from your investment portfolio to ensure you're able to cover all of your expenses.

The remainder of this guide primarily focus on generating cash flow from your portfolio to bridge this gap. But before we get into specific strategies, we discuss some important principles of retirement investing.

Income vs. Cash Flow

It may seem minor, but there is a key difference between income and cash flow. Income is money received and cash flow is money withdrawn. For example, dividends and bond coupons payments are considered income. These are two completely acceptable sources of funds. But if you rely on them solely, you could be selling yourself short. On the other hand, selling a security and withdrawing the proceeds also generates cash flow. When you sell a security, the difference between what you put in and what you take out is considered a capital gain (or loss).

Note, cash flow withdrawn from your portfolio isn't a bad thing - and can be very important component of your overall retirement strategy

Consider: If you have a portfolio of \$1,000,000 growing at 10% a year, and you realise \$100,000 in annual gains, this really isn't any different than a portfolio growing at 5% a year that pays \$50,000 in dividends. The total return (i.e. capital gains + dividends) is the same on a pre-tax basis; and, depending on your situation, selling a security and paying tax on capital gains may be more tax-efficient than dividend income!

Bottom line: When it comes to paying for your retirement, you should really only be concerned about the total return of your portfolio and after-tax cash flow - not whether it comes from selling securities or regular income.

Before you can generate income though, you'll need to decide what assets will make up your portfolio.





Asset Allocation

Asset allocation is the single greatest determinant of portfolio returns and the likelihood of being able to afford the retirement you want. At its core, asset allocation is what you decide to invest in.

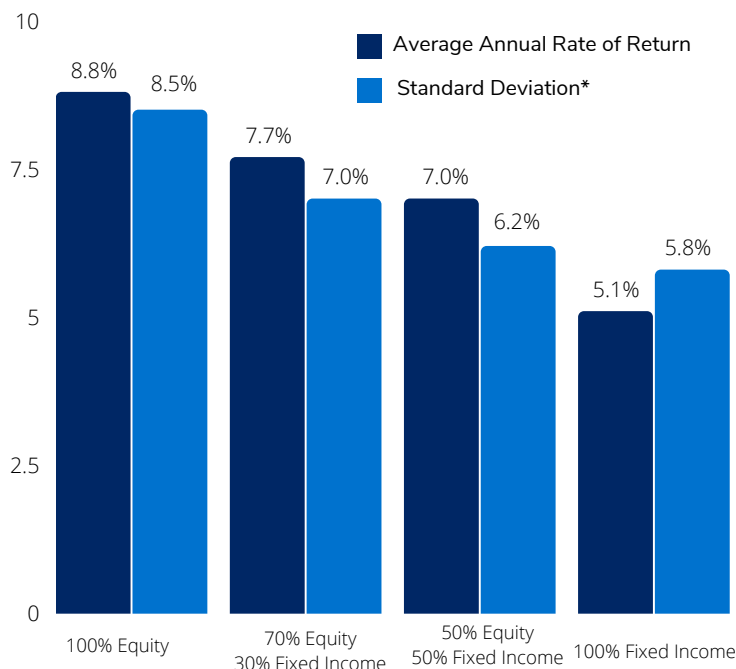
For most, this will mean Equity (i.e. Stocks, ETFs), Fixed Income (i.e. Bonds, GICs) and in some cases, cash.

When many people hear their asset allocation could determine if they run out of money or live comfortably, they instinctively want to "play it safe." Fair enough, but most people actually get it backwards.

There is a common misperception that bonds are safer than stocks. This originates in stocks' higher short-term volatility. So retirees looking to avoid volatility - "playing it safe" - Sometimes opt for bonds but end up neglecting their return needs. As you can see in the following chart, as you include more fixed income in your portfolio you get less volatility (standard deviation), but also lower returns over a short five-year period.

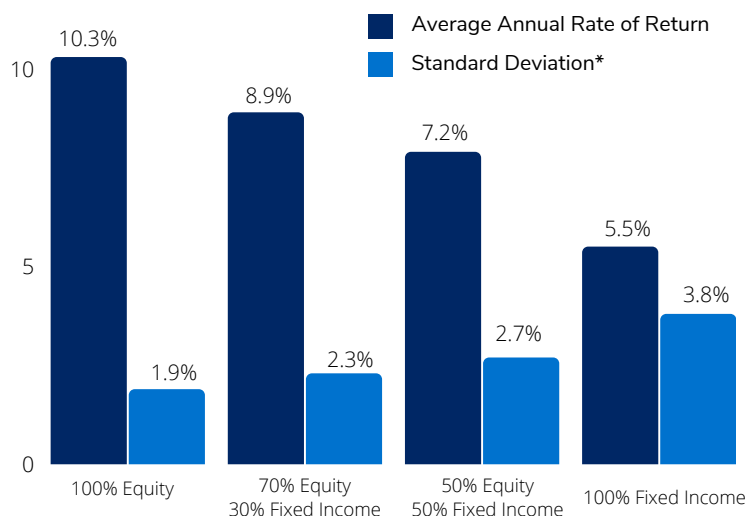
Stocks actually have lower volatility (Standard deviation) than bonds over longer time periods. This means if you have a longer time horizon and/or higher return needs, stocks may make up a larger percentage of your asset allocation than you previously considered. This is especially true when you factor in withdrawals over the course of your retirement.

5-year rolling periods



Opting for a drastically lower return isn't an option for many retirees and it's unlikely your time horizon is only five years. When we consider a more plausible time horizon, say 30 years, a different pattern emerges.

30-year rolling periods



*Standard Deviation represents the degree of fluctuation in the historical returns. The risk measure is applied to 5 and 30 year annualised returns in the above charts.

Source Data: Global Financial Data as of 11/01/2016. 5 and 30 year rolling returns from 1925 to 2015. Equity return based on world return index and converted to CAD. Fixed Income returns based on Global total return government bond index and is converted to CAD.



If you're taking \$50,000 out of a \$1,000,000 portfolio every year in withdrawals, you're more likely to deplete it if your rate of return is too low. You'd need a 5% total rate of return every year just to keep your balance the same and that's before you factor in inflation. If you're worried about having "safe" investments, consider the greatest danger lies in running out of money because of a low rate of return over the lifetime of your investments.

Next, we'll address a problem equally as serious as return that are too low: taking withdrawals that are too high.

Risk of High Withdrawals

A common - but incorrect - assumption is that since equities have historically delivered a roughly 10% annualised average return over the long term,* it must be safe to withdraw 10% without drawing down the principal.

Nothing could be further from the truth. Though markets may annualize about 10% over time, returns vary greatly from year to year.

Miscalculating withdrawals during market downturns can substantially decrease the probability of maintaining your principal. For example, if your portfolio is down 20% and you take a 10% distribution, you will need about a 39% gain just to get back to the initial value.

This risk is heightened in the first few years of your retirement. Low early returns accompanied by high withdrawals can have a permanent impact on your probability of retirement success. This further speaks to the importance of asset allocation and diversification.

When you consider how devastating years of too-high withdrawals could be, it's clear how important it is to properly manage your cash-flow expectations and discretionary spending.

Difficult Decisions

As you can see, investing requires trade-offs, like more short-term volatility higher long term returns. Another trade-off you may have to consider is between different discretionary spending.

Sometimes you may have multiple expenses important to you on a personal level, such as paying for a grandchild's university education or taking a dream trip with your spouse. However, in order to meet your investing goals you'll need to be clear about what's affordable. It's not advisable to risk depleting your portfolio for non-essential spending. This isn't to say helping with university or a vacation are off the table; rather, they just need to be realistically budgeted in the context of your overall goals, cash-flow needs and return expectations. Maybe you can do both or only one, or possibly neither.

It's also helpful to be clear with yourself and other family members how much you can spend beforehand. Once the spending becomes counted on, emotions come into play and you could end up with a bigger bill than you're comfortable with.

Any time you're taking more than 5% off your portfolio, you're greatly increasing the risk of depleting your assets.

Now it's time to consider what investments you'll use to generate income.

*Source: Global Financial Data; As of 23/01/2015. Based on 9.7% annualised S&P/TSX 500 Index total returns from 1933 - 2016



Investment Income Sources

Registered Accounts

Most all Canadians have utilized one or more of these accounts during their lives. These include Registered Retirement Savings Plans (RRSP), Tax-Free Savings Accounts (TFSA), Locked-In Retirement Accounts (LIRA) and Registered Retirement Income Fund (RRIF) to name a few.

These accounts can hold many different kinds of underlying investments including stocks, bonds, mutual funds, ETFs, GICs and more. The investment you choose to hold inside of your registered plan will vary depending on your time horizon, willingness to accept risk and desired asset allocation.

When it comes time to generate an income from these accounts, it is crucial to integrate the expected taxation into your retirement income plan. All of these accounts - excluding the TFSA - are taxable as income when money is withdrawn. Be mindful of your marginal tax rate as a higher income may bump you into a higher tax bracket and have a negative impact on your government benefits (think OAS recovery tax).

2% interest and you are in the 50% marginal tax rate, your after tax rate of return will be 1%. If we factor in inflation you are left with a loss in purchasing power of -2%.

- **Dividend Income:** When you are a shareholder of a publicly traded company by owning stock, you may be entitled to a dividend. For some retirees, dividends provide a stable source of retirement income without needing to withdraw from the principal. Dividends are tax preferred stable income source for many retirees.
- **Capital Gain:** When you sell an asset within a non-registered account you may trigger a capital gain. Capital gains are subject to a 50% inclusion rate. This means half of the gain is taxable. In simple terms, if you are in the 40% marginal tax bracket, your effective tax rate on your gain is 20%. If you happen to sell your investment at a loss, you will be able to deduct this "capital loss" against capital gains.

Non-Registered Accounts

This type of investment account is subject to tax as income is earned. Unlike registered accounts, there is no contribution or withdrawal restrictions however, there are three different ways your underlying investments may be taxed.

- **Interest Income:** This source of income is the least tax efficient of the three. Interest income from things like High Interest Savings Accounts, Bonds and GICs is taxable income. To put this in other terms, if your GIC is earning



Tax Planning Strategies

There are a multitude of tax planning strategies we employ when creating a retirement income plan for clients. Here are a few of the most common:

- **Tax loss harvesting:** This is when you purposefully trigger capital gains and offset tax by triggering capital losses. There is a superficial loss rule you need to be aware of while orchestrated this strategy. However, if done correctly, tax loss harvesting can help to minimize your tax bill.
- **Asset allocation optimization:** Take a close look at your Registered and Non-registered accounts. Take note of the asset allocation within each of the accounts. You may benefit by holding more tax efficient investments (Capital Gains) within your non-registered accounts and tax inefficient (Interest income) in your registered plans. Small changes in your allocations could have significant impact on the taxation of your retirement accounts.
- **Efficient use of the TFSA:** Often overlooked by retirees is the true power of the Tax-Free Saving Account. The name suggests it is just another “savings account”, but the reality is the TFSA can be used to hold most traditional investments, including stocks, mutual funds and ETFs. The TFSA may be your greatest ally in reducing tax in retirement!
- **Year end de-registration:** Near the end of the year, review your estimated taxable income and marginal tax rates. If you are close to the next marginal tax rate, it may make sense to to withdrawal extra funds, pay tax, and reinvest the proceeds. Why do you ask? For some it may make sense to pay a lower tax rate today so they can increase liquidity and reduce the impact of a near 50% estate tax.





How Can Fundamental Wealth Help?

We have designed this three step process to give you (and us) a framework for making an educated and informed decision about working together. For people who are potentially a good fit for our firm, there is no cost or obligation for this process as we want you to know exactly how we can help you before you pay us a single dollar in fees or trust us with a penny of your nest egg.

1

SCHEDULE 20-MIN CALL

A 20-minute phone call will give us both a chance to make sure your situation matches our expertise. After all, you wouldn't see a Cardiologist if you needed foot surgery!

[Schedule Your Call](#)

2

TEAM MEETING

Like a doctor, it's important to diagnose before we prescribe.

The next step is meeting with our team (in our office or via Zoom). During this one-hour meeting, our team will get crystal clear on your financial goals, needs, and concerns.

3

REVIEW ASSESSMENT

With your Retirement Assessment complete, we will have a second meeting (in person or virtually via Zoom) to review our findings and recommendations.

In plain English, we will explain exactly what you can do to improve your retirement plan, lower taxes, optimize your investments and improve your estate.

SLEEP ON IT!

We are looking for long-term client relationships, not a quick transaction. It's important that you take as much time as needed to make a decision. If you decide that we aren't a good fit, we will happily help you find another professional with the right expertise. There is never a hard-sell or pressure to say "yes."



From the moment you become a client, we put you first.

We are dedicated to helping investors like you reach their long-term financial goals and live comfortably in retirement. As CERTIFIED FINANCIAL PLANNER® professionals, we adhere to Standards of Professional Responsibility, including a Code of Ethics and Rules of Conduct all CFP® professionals must follow.

Fees Aligned With Your Interests

We provide fee - based solutions to our clients. This approach unbundles your cost of investing and advisory fee to increase transparency and reduce conflicts of interest. We find that it helps our clients get a clear understanding of the value of the financial advice we provide.

A Tailored Approach

Some financial advisors only sole focus is on your investments. While this is a crucial component to your financial future, we find that most clients benefit from our in-depth approach that factors in all aspects of their lives.

Unparalleled Service

Your dedicated team is here to serve you, not sell you. We are well versed in your financial goals and will help you stay on track with your financial plan. We will make sure you understand your investment portfolio and why. We also offer an Advanced Financial Planning Approach that draws in leading tax, legal and investment specialists to give you a clear picture of your your families financial future. We believe strongly this approach is unlike anything you have ever experienced.

Investment Experience

Our investment approach is centred around one common goal: providing investment solutions focused on maximizing risk-adjusted returns over the long term, so our clients can confidently pursue their goals and a more secure financial future for their families.

Our overarching investment philosophy:

- Pension style investing utilizing alternative investments.
- Low-cost passive ETF solutions.
- A disciplined selection and monitoring process.
- Sustainable investing principles that emphasize the long term.



Value you can count on

We are passionate about our client experience. When you meet with us, our mission is to show you that the value of advice that you receive will outweigh what you pay in fees. In a 2021 study completed by Russell Investments, it was shown that working a comprehensive financial planner can provide 3.95%* in total value to the client relationship.

A	<u>Active</u> rebalancing of investment portfolios	0.04%	
+		+	
B	<u>Behavioral</u> coaching	2.00%	
+		+	
C	<u>Customized</u> client experience & planning	0.63%	= 3.95% total 2021 value of an advisor
+		+	
P	<u>Product</u> alignment	0.62%	
+		+	
T	<u>Tax-efficient</u> planning & investing	0.66%	

Source: Value of Advisor 2021 Canada, May 2021. <https://russellinvestments.com/us/resources/financial-professionals/value-of-advisor>



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