The Top 3 Mistakes People Make When Saving for Retirement

Description

Planning for retirement is never an easy task. After all, it always seems like such a distant event. It is therefore difficult to put in place the required capital and decision-making process in order to generate a nest egg that provides a financially-free retirement.

With that in mind, here are three common mistakes that people making when seeking to build their retirement savings. Avoiding them may make it a lot simpler to retire with a comfortable income which provides the financial flexibility most people seek in older age.

Wrong assets

While saving for retirement is tough, knowing where to invest it could be even more difficult. Put simply, many people invest in the wrong assets throughout their lives, and this can hurt their returns in the long run.

During the accumulation phase of an individual's life, the vast majority of savings should be invested in a stock market, such as the FTSE 100 or S&P 500. This is because there is time for a potential downturn to recover before an individual reaches retirement age. And since retirement funds are not needed until age 65+, volatility is unlikely to be an issue, either.

However, many people choose to keep large amounts of cash savings, or invest in assets such as bonds throughout their lives. While they may offer lower risk and less volatility than stocks, ultimately they are unlikely to provide a sizeable nest egg in older age.

Inflation

Given the long-term time horizon involved in planning for retirement, it is easy to overlook the impact of inflation. In other words, what seems to be a sufficient amount on which to retire today is unlikely to be enough in 20+ years. Assuming inflation of 3% per annum, over a 20-year timeframe inflation could erode the value of an asset by as much as 80%. This means that obtaining a return which is in excess of inflation is vital to people planning for retirement, and also for those individuals who have already retired.

With stock markets such as the S&P 500 and FTSE 100 offering high-single digit returns on an annualised basis over the long run, they could help an investor's portfolio to stay ahead of inflation.

Long-term approach

While retirement savings are not accessed until an individual has retired, many investors worry about the performance of their portfolios in the short run. This can lead to poor decision-making, since it can force an investor to give up on assets that could deliver high returns in the long run.

In fact, it could be argued that falling asset prices are a good thing for individuals who are not yet retired. After all, they provide an opportunity to purchase the same asset at a lower price. And since individuals are net buyers pre-retirement, it could mean that their long-term returns are given a boost. As such, taking a long-term approach could be a sound method of overcoming paper losses and planning for a financially-successful retirement.

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