Retirement Finance Simulation Model

# Client: John and Jill Smith

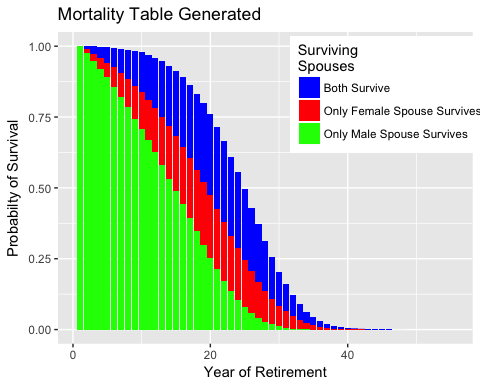
Sat Dec 9 13:27:38 2017

Assumptions for the simulations are as follows:

* Run 10,000 scenarios.
* Demographic data
  + Husband's current age is 65.
  + Wife's current age is 67.
* Social Security data
  + Husband has the highest Social Security benefit is TRUE.
  + Expected Social Security benefit for lower earner is $ 17,580.
  + Expected SS benefit for higher earner is $ 36,444.
* Portfolio parameters
  + Initial portfolio balance before annuity purchase is $ 3,940,000.
  + Equity allocations randomized from 0% to 100%.
* Market and inflation parameters
  + Annual average rate of inflation is 2%.
  + Inflation rate annual standard deviation is 1%.
  + Risk-free real return rate is 1%.
  + Equity risk premium is 4.25%.
  + Standard deviation of annual market returns is 12%.
* Annuity parameters
  + Age of annuitant when payments will begin is 66.
  + Quote for annual payment before any deaths is $ 9,600.
  + Annuity is inflation-protected is FALSE.
  + Husband owns Annuity is TRUE.
  + Percent of benefit that goes to survivor is 50%.
  + SPIA payout rate is 5.36%. $ Annuity allocation as percent of initial portfolio randomized from 0% to 40%.
* Spending parameters
  + Expected spending year one of retirement randomized from $ 216,000 to $ 240,000.
  + Percent expense decline after death of first spouse is 63%.
  + Expenses typically decline 0% annually throughout retirement.
* HECM Line of Credit
  + Home apprecation rate is 0% annually.
  + Initial HECM Line of Credit available is $ 0
  + Initial Reverse Mortgage Balance is $ 0
  + Home Market Value (no real annual growth assumed) is $ 1,200,000
  + Mean long term return for 1-yr Libor= 2% with standard deviation= 1%
  + HECM line of credit's maximum lifetime interest rate cap 10.34%
  + HECM line of credit's margin added to Libor Index for variable rate loan 3%
  + HECM line of credit's Monthly Insurance Premium percentage 1.25%

# The following charts show the parameters for this simulation.

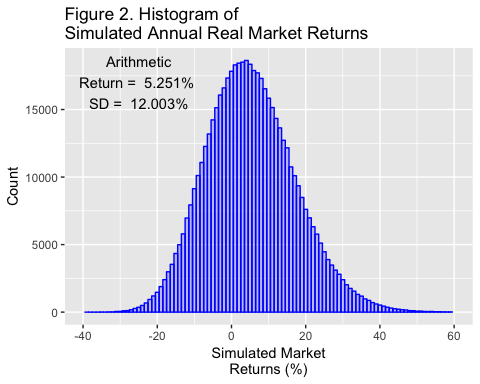
Life expectancies for husband and wife are plotted below.



## .Primitive("return")

The following annual market returns were simulated.

## Warning: Removed 56 rows containing non-finite values (stat\_bin).

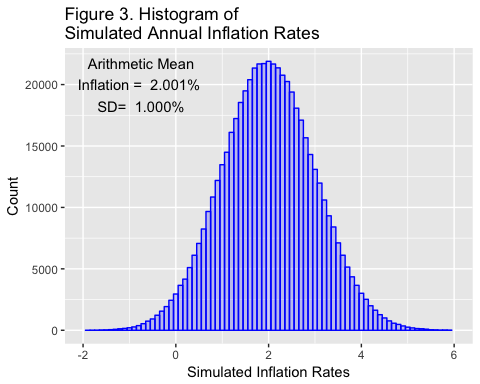


Arithmetic Mean of Simulated Annual Returns = 5.251%.

Standard Deviation of Simulated Annual Returns = 12.003%.

The following simulated annual inflation rate were simulated:

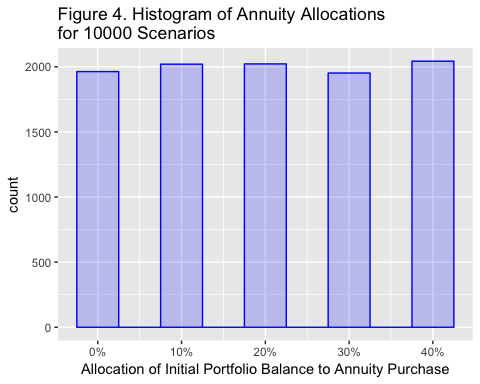
## Warning: Removed 36 rows containing non-finite values (stat\_bin).

 \* Arithmetic Mean of Simulated Inflation Rates = 2.001%.

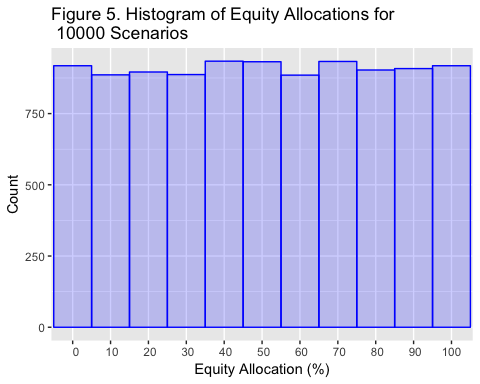
* Standard Deviation of Simulated Annual Inflation Rates = 1%.

The graphs that follow are intended to show the range of inputs used by the simulation model (for example, the range of spending tested) and the distributions of the input parameters (for example, life expectancy follows a Gompertz distribution, while spending parameters are randomized with a uniform distribution.)

The following chart shows the number of scenarios simulated at each level of annuity allocation. The *x*-axis shows the range of annuity allocations simulated.



The following chart shows the number of scenarios simulated at each level of equity allocation. The *x*-axis shows the range of equity allocations simulated.



# Results of Simulations

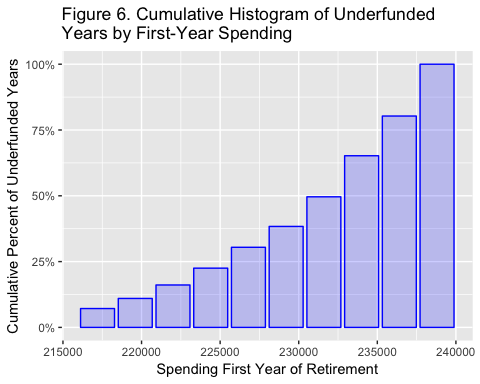
* Statistics For Underfunded Scenarios
* 391 scenarios with unmet spending or 3.91%
* Number of years with unmet spending 2041
* Mean years with unmet spending when spending not met 5
* Depleted portfolios 3.91 %
* Scenarios depleting HECM Line of Credit 0 or 0%

The previous charts showed the distribution and ranges of key randomized inputs to the simulation model including spending, equity allocation, annuity allocation and stochastic life expectancies. The following charts provide a summary of the simulation model's output for those scenarios and years that were underfunded in the simulation.

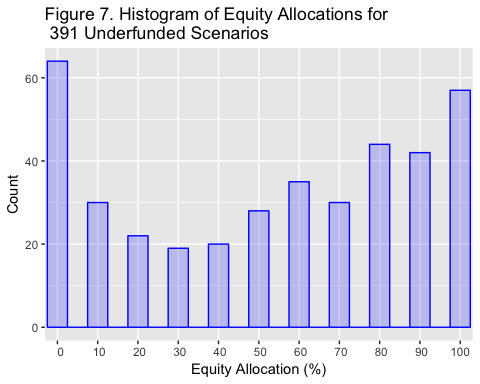
Following is a histogram showing spending amounts (and the range of spending along the *x*- axis) for the first year of each retirement scenario.

This histogram shows the cumulative ratio of underfunded simulated years by the amount of spending for the first year of retirement. The right-most column, for example, shows that 100% of 391 unfunded years had spending in the first year of retirement of $ 240,000 or less. The column to its left shows that about 80% of all 391 unfunded years had spending in the first year of retirement of $ 237,600 or less.

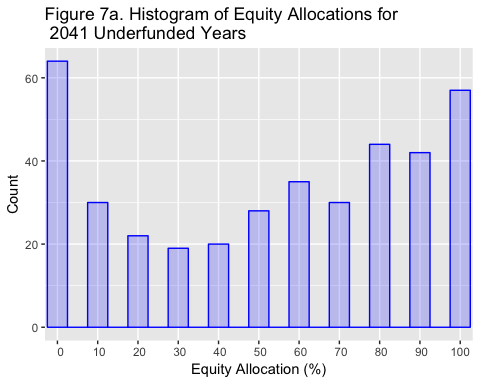
About half of the 391 underfunded years in this simulation could have been funded by spending less than $ 232,800 from the beginning of retirement.



Following is a histogram showing the equity allocation for underfunded scenarios (an underfunded scenario had at least one underfunded year).



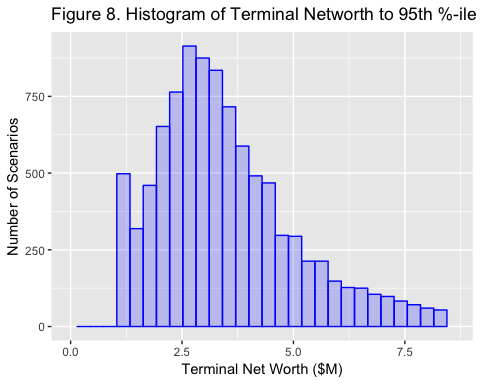
Following is a histogram showing the equity allocation for all underfunded *years*.



Following is a histogram of 99 %-ile terminal net worth (portfolio value plus home equity at death of the second spouse). The largest 1% of terminal net worth values are excluded because they are highly unlikely and distort the graph.

## `stat\_bin()` using `bins = 30`. Pick better value with `binwidth`.

## Warning: Removed 500 rows containing non-finite values (stat\_bin).



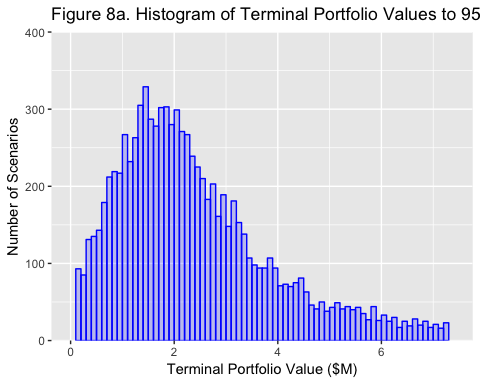
* Median Terminal Net Worth = $ 3,292,183.
* Mean Terminal Net Worth = $ 3,980,048.
* About two-thirds of Terminal Net Worth values fell between $ 1,072,589 and $ 6,887,507.
* About 95% of terminal portfolio values fell between $ 0 and $ 9,794,966.

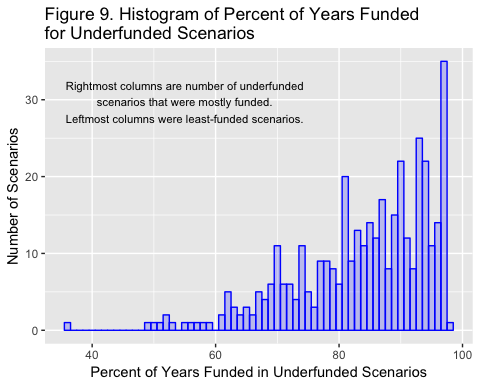
The following graph shows the percent of years that were funded for the 391 *scenarios* that were underfunded, i.e., those scenarios with less than 100% funded years. Leftmost columns show the number of scenarios that failed early in retirement. Rightmost columns show the number of scenarios that were nearly completely funded.

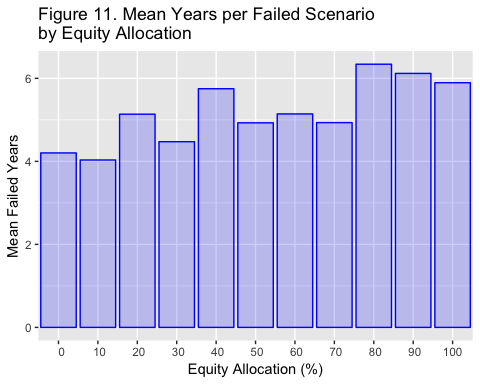
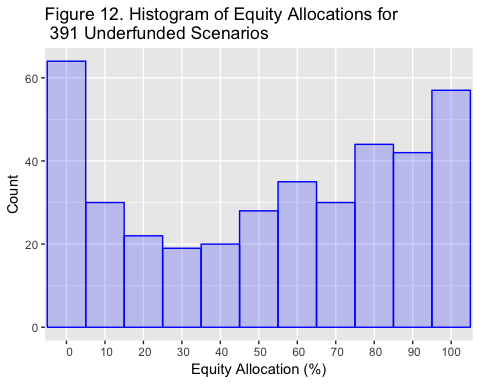
Rightmost columns may fall within the margin of error and possibly should be considered successful scenarios. In this simulation, 53 or 13.5549872% of underfunded scenarios were at least 95% funded.

## Warning: Removed 500 rows containing non-finite values (stat\_bin).

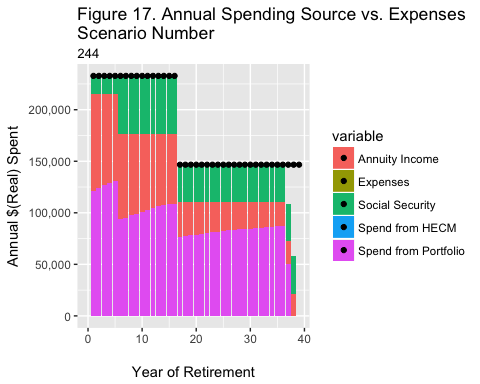
## Warning: Removed 7 rows containing missing values (geom\_bar).



 The following graph shows the number of years of retirement for which spending demand (consumption) was *not* met.

The following charts summarize a single, user-selected scenario. The black line shows consumption demanded. The colored areas indicate the source for funding that consumption. Underfunded years will show that funding sources did not achiev demanded consumption.



## Warning: Removed 30 rows containing missing values (position\_stack).

