

Money

You Might Be Overestimating How Much Money You Need to Save for Retirement

By: [Martha C. White](#)

Editor: [Kaitlin Mulhere](#)

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People stress a lot about saving enough money to live comfortably in retirement. New research finds that, in spite of our anxieties, many of us are doing better than we think.

A November **survey** of 500 employees of private-sector companies conducted on behalf of Principal Financial Group shows that roughly two-thirds of respondents overestimated how much money they would need to accrue before retirement, many by a significant amount. Principal found that 56% of respondents believe they need at least 30 years' worth of income saved before they can retire comfortably.

This is about three times higher than what experts generally recommend, but Sri Reddy, senior vice president of retirement and income solutions at Principal Financial Group, says he's not surprised that people make this incorrect assumption.

People who think they need 30 years' worth of income probably believe that they need to have enough saved up to cover every year's worth of living expenses after they retire, he says. In reality, if people save 10 times their annual salary, that plus Social Security will bring them to between 75% and 80% of their pre-retirement income – provided they know how much they can safely withdraw every year to balance the need for immediate cash with the need to continue saving for years to come.

And unfortunately, Principal's survey finds that's another figure people tend to miscalculate. More than half of respondents believe they can withdraw 10% of their retirement savings annually while remaining financially stable over the long term. That's more than double the 4% many advisers say you should aim for. At a 4% withdrawal rate, enough of your retirement principal will remain invested to generate returns for decades into the future.

Principal finds that most people manage to save about 8% of their income annually. Reddy says that's a little low – although not by much. "Try to get to at least 10%," he says, including both your contributions as well as your employer match.

Peter Gallagher, managing director of Unified Retirement Planning Group, says that people who want to save more but don't know how much should focus on contributing as much as they can. Most people probably won't max out their contributions – for workers 50 and younger, the 2025 limit for 401(k) savings is \$23,500, and the IRA limit is \$7,000.

If those limits seem high based on what you're earning, don't get discouraged. In fact, Reddy says that's actually a big risk – that people become intimidated by the amount they think they have to save up and not even trying. "Saving anything is better than saving nothing," he says.

He adds that there are ways for people to increase their savings rate over time without feeling deprived. “As you get raises in the future, consider earmarking half of that for savings. It’s hard to miss money you’re not used to getting,” he says.

And, as it turns out, you actually can save too much for retirement. The issue isn’t the dollar amount so much as where you’re saving it, Nicole Garner Scott, a financial advisor with Northwestern Mutual, previously **told Money**.

Traditional retirement accounts have preferential tax treatment that helps you get the most out of your 401(k) or IRA contributions by deferring taxes on that money until you take withdrawals in retirement. The drawback is you generally can’t tap into that money until you’re at least 59 ½ years old, which means if you save too much, you could face an expensive liquidity crisis.

If you need to access your money before you’re nearly 60, you’ll get hit with an early-withdrawal penalty plus have to pay income tax on the money. While you can borrow against a 401(k), you don’t have that option with an IRA. What’s more, if you lose your job, you have to pay back anything you borrowed from your 401(k) within a short time frame, often 90 days.

The other problem with saving too much for retirement in pre-tax instruments like traditional 401(k)s and IRAs is it can lead to unexpectedly big tax bills once you get into your 70s and beyond – and potentially for your heirs, as well, Gallagher says.

Gallagher says that many people who spend their lives scrimping and saving don’t realize they’ve reached a point in retirement where they can actually enjoy the fruits of their labor. “It’s usually a shock at first,” he says. “They feel like they don’t have enough.”

Because of recent changes ushered by the SECURE Act 2.0, people who inherit IRAs from a parent have just 10 years to pull that money out after the parent's death. For an adult child who inherits a \$1 million IRA, this means having to essentially tack an extra \$100,000 onto their taxable income every year for a decade.

"That's a huge thing," Gallagher says.