# Mad as H, E, double Q!

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That's what my mom used to say, "Mad as H, E, double Q."  I couldn't sleep last night thinking about the October 2001 **Reader's Digest** article on **"Your Dream Retirement.  How to Make It Happen."**

To illustrate the problem with the method in the article, I first entered 90% of a $48,000 current wage as a retirement goal of $43,200. Then I entered $19,200 social security (including spouse) and a $24,000 pension.  Their worksheet result says I would not need any savings at all no matter how far I am from retirement because my social security plus pension equaled my retirement goal.  **Well, it is "Your Dream Retirement," but it certainly won't "Make It Happen."**

First suppose that I was ready to retire right away.  Sure, in the first year my social security and pension would equal my retirement goal.  But what about the following years when inflation would eat away at my fixed pension?  This idiotic program assumes that all pensions have COLAs.  In fact, very few pensions have COLAs with the major exceptions being military retirement and government executives.  A rough approximation of a fixed pension's value is about 2/3 of a COLA pension at best.

Then suppose that I was twenty years from retirement.  That pension will be worth only about half what my employer shows in the report because of intervening inflation.  That means that the fixed pension contribution will be only 1/2 x 2/3 = 1/3 of the value used in the Reader's Digest worksheet!  Pity the person who would rely on this.

It's really a lot worse than this, because anyone who is counting on a fixed pension and is twenty years or so from retiring has an even bigger problem.  Unless he or she remains at that company, that pension is not going to be worth very much.  Pensions build value quickly as you near retirement because the determinants, years of service multiplied by recent working wage, set the value.  If you leave long before retirement age, the years of service is low as is the recent working wage.  A low value times a low value is a very low value.  The value has no chance to grow after you left the job, do you are doubly cursed and the pension fund proceeds can be used by the employer to bolster earnings instead of compensating you.

To pour salt into the wound, their analysis is based on a 3% real growth for a retiree's portfolio.  Using simulations going back to 1926, a portfolio of 50% stock and representative costs would have substantially less than a 50% chance to get 3% real return due to reverse-dollar-cost-averaging. (See p. 254 of J. K. Lasser's Your Winning Retirement Plan.)  When are planners going to learn that you can't use the conventional definition of returns based on the growth of $1?  Retirees regularly take money out of savings which gives them lower effective returns which is just the opposite of making regular deposits.

Further, few retirees would maintain that high a stock allocation, especially late in life, and all would want higher than 50% success rates, not lower.  After looking at thousands of historical cases, I believe that retirees are well advised to assume near zero real return even if the future is as good as the past--and it might not be! (Just think of all those who retired around 1960 or the many that were hoodwinked into investing in Japan's stock market.)

The source of this method is the American Education Savings Council at www.asec.org.  Contrary to their stated objectives and implication with their name, I don't think they are doing much to educate America about savings when they put out this kind of material.  It's not much harder to get the math right.