

# Right Road.

**The vast majority of retirement plan projections are overly optimistic because they're based on incorrect or outdated assumptions. By Jim Otar**

**As financial planners,** our goal is to provide clients with realistic retirement projections. However, my research shows that current models with straight-line growth do not achieve this goal. Adding some randomness to the model, such as the Monte Carlo simulation, is a step in the right direction, but it's still far short of what historic evidence suggests.

Retirement planning software helps us to prepare a projection of asset values into future years. In doing so, we input several assumptions, such as investing a certain amount periodically, retiring at a certain age, withdrawing a certain amount of income from this portfolio after retirement, and so on. Similar retirement calculators are available from financial institutions. For the do-it-yourselfers, there are plenty of Web sites that offer such calculators as well.

These calculators produce a report outlining a financial plan, including a graph showing projected asset growth over time. Typically, it may look similar to the graph shown in Figure 1. Note: For this article, I made the following assumptions: 1) the initial withdrawal rate is 6% during the first year of retirement; 2) the withdrawal amount is adjusted each year for inflation. The average inflation between 1900 and 1999 was 3.5%, and that is what I used in this projection; and 3) the portfolio grows at 8% each year. I am assuming a conservative asset mix of 60% fixed-income and 40% equities. The portfolio is re-balanced each year.

*First in a Three-Part Series*



