Case Study: Connie and Ziggy's Retirement Nightmare*

The following real world example may help to clarify the reasons why individuals need a better retirement solution than what is commonly used today.

Connie and Ziggy, a married couple well into their retirements by 2008, were not ready for the global financial collapse that engulfed them back then. In an effort to be wise with their finances, they'd created a retirement plan many years before. They'd sought retirement planning advice from competent investment professionals who followed standard industry best practices. It was based on asset allocation theory modeled with statistical simulations. While this was a current best practice for individual investment advice, and blessed by the firms' compliance departments, they were unaware of a risk reduction approach followed by corporate pension plans since before 2008 known as Liability Driven Investing (or LDI).

Their plan included Ziggy selling his optical business but continuing to work there part time. He could walk to work from their condo, a home which held tremendous sentimental value for them. Both agreed that aging in place was their top priority in retirement (Note: This seems a common goal for retirees in America; a 2018 AARP survey found 76 percent of those ages 50 and older said they preferred to remain in their current residence as they age.)

The global financial collapse of 2008 created a crisis that grew by the day as a threat to their dream. Like many Americans, they were exposed to several pitfalls in common retail financial planning strategies. To begin with, the common use of risk tolerance questionnaires to determine asset allocations turned their retirement security into a stressful nightmare.

This couple did not understand how much their investments were designed to fluctuate. They knew their portfolio could vacillate, but did not fully comprehend they were susceptible to big declines at any point in time. ***Their advisors' computer simulations modeled average annual losses within a likely range of "plus x and minus y percent" two thirds of the time. Less understood was the potential for losses of y percent "or more" one sixth of the time. The Global Financial Collapse that began in 2008 was the "or more" part of that bargain.***

Former Wharton professor David Babbel describes the problem of retirees counting on retirement income from projections based on statistics as like playing Russian roulette with live ammunition: "[the risk of running out of money in retirement using systematic withdrawal] may only be 15%... [but] that is roughly equivalent to the 16.7% odds of losing in a game of Russian roulette... and few people are prone to participate in such games!"

Panicked by such a market decline, Connie and Ziggie tried to find a better solution from a different company. But without realizing it they were essentially put right back in the same portfolio. They again received the standard recommendation – using statistics to create a diversified portfolio without regard to matching assets with expenses – and their ability to cover their essential needs like housing was still in question. Their must-haves were lumped in with more discretionary things like entertainment, and averaged into risk tolerance scores that exposed their entire budget to fluctuations in stock and bond markets.

Connie and Ziggy didn't know how this was risky for them because they were not offered a sensible alternative. The outcome was terrifying.

Looking back, Connie believes it is impossible to pinpoint what came first: the onset of Ziggy's failing memory or the financial collapse. However, she knows the bear market was clearly a contributor to the exponential increase in his overall stress levels. Causes and effects for dementia and Alzheimer's typically highlight psychological factors that include anxiety and depression. Ziggy began a daily obsession of watching price declines of their mutual funds in the paper. He lost sleep and grew more and more forgetful. This unfortunately compounded the overall situation as it also impacted his part time employment, which in turn contributed to further progression of his memory loss.

Connie still remembers her husband's biggest concern was that their brokerage account would run out of money. He had crunched their spending numbers enough to know what would happen if he died first and the investment account failed: Connie would lose one of their two Social Security checks and would struggle financially to remain in the condo alone. Whether this outcome was probable or not based on their advisor's statistics-driven simulations was irrelevant. To Ziggy it simply felt like Connie's safety was at risk.

The condo was their most important must-have expense item. The idea of losing it felt like an existential threat. The need for a fail-safe funding strategy was never discussed. Their financial plan put them in an unmatched position, they did not know how to solve it, and hearing the words "just change your spending" didn't fix it.

In 2009, their financial advisor recommended switching to a fee-based discretionary account diversified with low cost ETFs. This was still a mix of risk exposures and many of the values continued to decline. Signs appeared that Ziggy's forgetfulness was progressing rapidly. Their financial adviser lost patience while trying to keep him calm, insisting he look at the return of the whole portfolio instead of individual funds. This was an exercise in futility. Ziggy's diminished capacity kept him from appreciating the logic of a diversified mix of risky assets.

They next tried moving their account to a discount brokerage, where they were guided to invest in a professionally managed active mutual fund program. This approach was nearly identical to that of their prior firm. Unfortunately, many of these new funds fared poorly as well. To add to their despair, Ziggy lost his job. The new owner of the business told Connie Ziggy couldn't continue interfacing with customers given his memory loss. It was like a rogue wave to their financial plan. Sadly, the disease progressed quickly, leading to a nursing home, physical decline from things such as urinary tract infections and, tragically, hastened his death a year later.

Connie's physical health deteriorated during this time too, as the stress of watching her beloved suffer and slip away combined with the pressure of assuming sole decision making responsibility for their financial security and was too much to bear. It was all new to her, and scary. She wishes there could have been a different way they could have budgeted for retirement, and that they done so well in advance.

What if they had prioritized their retirement expenses into three buckets based on what was most important to them? The approach of segmenting and funding different expenses with more economic precision would have eased Connie and Ziggy's overall stress and does not require rocket science. If implemented from the start, it may have helped Ziggy live longer.

The following table illustrates the concept:

Example of Categorizing Expenses in a Hypothetical LDI-Like Framework

Expense Item	Most Important	Discretionary	Optional	Funding Match
Food	*			***Social Security**
Shelter costs: HOA, Taxes, Maintenance	*			***Annuity W/COLA *Reverse Mortgage**
Health Insurance	*			***Medicare *Social Security *LT Care Insurance**
Income Taxes	*			***Social Security**
Liquidity	*			***Savings *Reverse Mortgage**
Transportation		*		***Social Security**
Inheritances			*	***Home Equity *Investments *Life Insurance**
Travel/Entertainment			*	***Investments**
Clothing Other Optional Items			*	***Investments**

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