

Physician's Financial News

Worst Case Scenario

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The Seven-Year Dwindraft

Flat. That describes our Gross Domestic Product (GDP), which was 0.6% for the past two quarters. Since it isn't falling, we don't meet one of the common definitions of recession: two quarters of declining GDP. What we do encounter, though, is a lot of worry. This is reflected by declining spending on both durable and non-durable goods.



Retirees or near retirees or those whose job is not secure have to take notice. Their income is not protected unless they make or made it so. Their common question is, "How much money should be put away for protection from a dwindraft?" In other words, does the cushion need to be thick and ample like an expensive oversized sofa or, can it be thin and puny like a futon?

The answer, "It depends." Usually downturns in the stock market last two years, so theoretically a 24-month cushion would be enough. But, as always, just like getting to know another person means she/he isn't always what we think, the history of the stock market can reveal another face when we get to know it better.

A longer decline than two years that was relatively recent was between 1974 and the early 1980s. Then, anyone who was retired or retiring or lost a job could have suffered a considerable hit in their investment portfolio. This is not only because of the large drop in the market in 1974-1975. It is also because it recouped so slowly. Whereas the usual downturn takes two years to recover, this decline turned into a sloth. It didn't come back until the early 1980s, about seven years.

This means that if you were relying on investment income rather than salary during those years, you would have had to dip into your investments while they were dropping in value or barely climbing upward. Later, it would have been almost impossible to recoup the lost monies, especially for the older investor. This would mean a smaller income from investments in the future. This scenario, should it be repeated in this downturn, means that people without substantial padding in their portfolio that depend on its income might suffer.

What to do if someone in the above category is anxious about the worst case scenario, a significant drop for a prolonged period (like the seven year fiasco following 1974-75)? A plushy cushion could be needed. The whole idea is to sleep comfortably at night and that is what a previous post, [Buy or Not](#), also addresses.