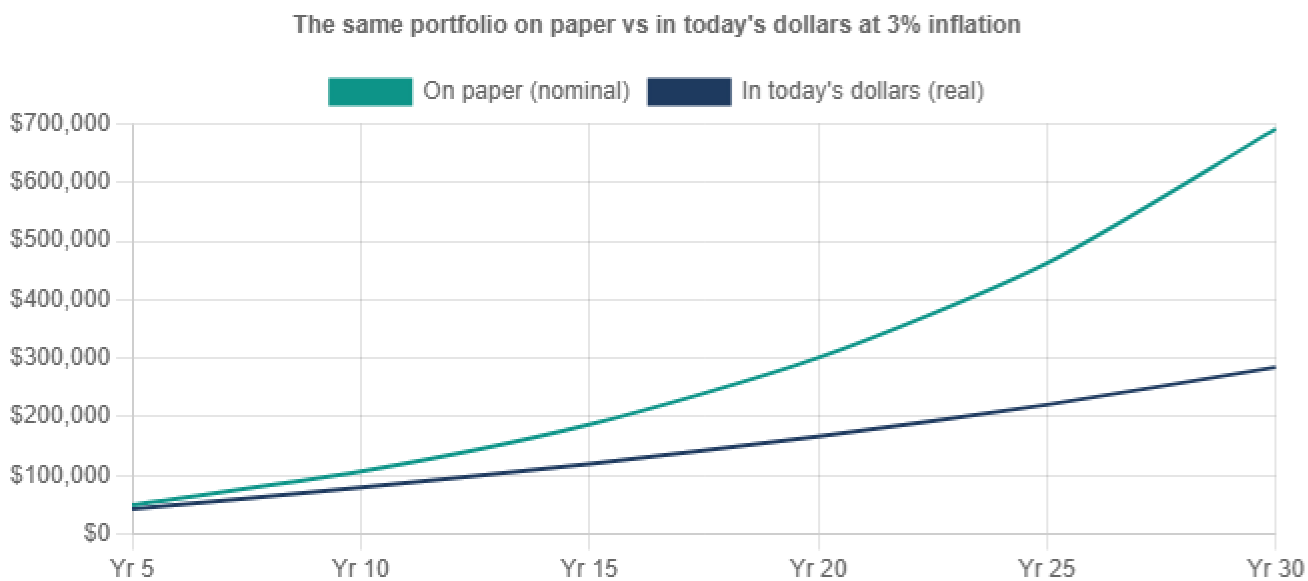
What Inflation Quietly Takes

> A portfolio can look like it grew enormously while its real buying power grew far less. This shows the gap between the number on paper and what it can actually buy.

A projection that shows your money growing to a huge number is telling the truth and hiding something at the same time. The number is right, but each of those future dollars buys less than a dollar does today. This shows both lines at once.



Year	On paper	In today's dollars
5	$49,973	$43,107
10	$106,639	$79,349
15	$186,971	$120,009
20	$300,851	$166,574
25	$462,290	$220,792
30	$691,150	$284,745

Reading the chart

The upper line is the balance on paper, growing a 10,000 dollar start plus 500 dollars a month at 7 percent. The lower line is that same balance restated in today's dollars at 3 percent inflation. After 30 years the paper figure is about 691,000 dollars, but its real buying power is closer to 285,000 dollars.

The two lines start together and drift apart, because inflation compounds against you the same way returns compound for you. The gap between them is what inflation quietly took.

Why plan in real dollars

A retirement target that looks comfortable in future dollars can fall short once you translate it into what it will actually buy. Planning in today's dollars keeps the goal honest and avoids a nasty surprise decades out.

Raise the nominal return on the control and the paper line jumps, but the real line moves less, because part of any return is just keeping pace with inflation. A useful rule of thumb is that your real return is roughly your nominal return minus inflation.

Key takeaway. Growth on paper is not growth in buying power. Judge a long-run plan by its value in today's dollars, not the headline balance.

Assumptions

- A 10,000 dollar start plus 500 dollars a month grows at the nominal return you set, over 30 years.
- Real value discounts the balance at 3 percent annual inflation to show buying power in today's dollars.

Sources

- U.S. Bureau of Labor Statistics, Consumer Price Index