



ACI Advisors Corner

What to Do When the Markets Crater

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Gobs have been written about the worldwide economic crisis, the equity markets, the viability of stable value funds, whether or not target date maturity funds will steer the baby boomers and others through to retirement, et. al. In a talk a few days ago to a group of CEO's I remarked that if they hadn't opened up their 401(k) statements recently, it may be best not to do so unless they were on anti-depressants!

Sarcastic—yes; but what do we learn from this and how do we pass this knowledge to our clients and their employees in a way that is truly valuable? If done properly, can we forestall our clients from making a hasty and ill-considered removal of their advisor and/or third party administrator? I say yes.

But what is that **valuable knowledge**? Here is my take.

1. To pull a percent from political rhetoric, I would wager that more than 95% of adult Americans have never put pen to paper or much less key stroke to Excel spreadsheet to calculate weekly, monthly and annual scheduling of income, expenses and savings. In short, we didn't plan to fail, we have failed to plan.
2. Maybe it's obvious, but we have gotten to this point financially as a nation by saving in negative amounts. A key part of emerging from this will be to reverse the negative savings rate into a positive rate. We do that by making better choices, participant by participant, to pare our spending and take the resulting savings and squirrel it away for retirement.
3. The longer we postpone the change in behavior the bigger the change in our life styles will ultimately be required. In other words small incremental changes will ultimately prevent shocking venue changes.
4. The private retirement system is going to be legislatively challenged in the next session of Congress. Rep. George Miller from the Bay Area held hearings on the failure of the 401(k) system. Early testimony has one economist, Teresa Ghilarducci, offering a bizarre "Saving Retirement in the Face of America's Credit Crises: Short Term and Long Term Solutions" on October 7, 2008 suggesting that the 401(k) system be gutted by requiring a **5%** employee deferral for all employees and government contribution of \$600 every year (unclear if the deferral is pre tax or post tax) and both employee deferral and government contribution would be invested in government bonds earning **3% plus the inflation rate**—administered by the government. Further, participants in a 401(k) type plan could trade their entire account balances ("perhaps valued at mid-august prices") for a guaranteed monthly pension when they begin taking Social Security. The traded money would also be earned the 3% plus the inflation rate.

The average inflation rate in the US from 1997 through 2007 was 2.57%; while year to date through September 2008 it is 4.59%--a 78% increase over

the average of the prior eleven year period. The question is what can we expect will happen to the inflation rate after we print a couple of trillion dollars of bailout and stimulus package monies over the next 18 months? Some economists think that we may be heading towards deflation; others feel that it will soar. Either way a guaranteed return is hard to compete with (3% plus say 5% current inflation = **8%**) and since this program would be mandated by law competing is not an option under Ms. Ghilarducci's proposal.

The 401(k) plan participant who would be covered in this government program may be disinclined to defer into the 401(k) plan. A blatant statement by Ms. Ghilarducci in her report suggests that this program "...ends the fruitless discussions with brokers and financial sales agents, who are also desperate for more fees and are often wrong about markets". She is out to get the financial industry out of the 401(k) business. Not surprisingly, this proposal is getting some attention in the press and may have some legs in Congress.

5. So the **valuable knowledge** is to share your knowledge by helping employers to foster savings through contributing more to their 401(k) plans in terms of matching or profit sharing contributions (and possibly by adding Cash Balance defined benefit plans) and providing education and enthusiasm for personal budgeting processes and savings to eligible plan participants. This goes beyond automatic contribution arrangements—to the success of the plan measured by a percentage increase in those deferring and a percentage increase in the average deferral rate.

Perhaps future 401(k) plan designs may need to have provisions that prevent savings leakage that comes with withdrawals for hardships and loans. To prevent a government intrusion into the 401(k) system, it appears to be in our best interest to think outside of the current box and take appropriate action.

I was asked to give a talk recently titled "Tricking out your 401(k) plan". What we are discussing here isn't about tricking out or indeed tricking anyone or anything at all. It is about providing value by going to the core of the economic problem.

Good Luck and let us know if you would like to collaborate on any matters.

For those that have an interest here in telling your Congress Representative here is the URL http://www.house.gov/house/MemberWWW_by_State.shtml