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The Sound Investor Series #34

Boomers Better Save More

By Ed Hynes, CFA
January 25, 2006

"What will attract the most money this year: Stocks, Bonds or Cash?" This week Barron's presented that question to a small group of professionals and I was pleased to be included. My answer was "Stocks, driven by the growing realization of baby boomers that owing stocks is the only chance they have for a decent retirement."

I do not want to sound flippant so let me elaborate. First, I was glad Barron's asked which asset category would attract the most money, not, which would have the best performance. In the long-term I am confident stocks will outperform bonds and cash; but short-term, who knows!

Second, I hope Baby Boomers, including myself, will do more to prepare for retirement, but I am not holding my breath. We need to:

- Halt our spending spree
- Save substantial amounts of money
- Invest in long-term investments such as stocks

A few lucky Baby Boomers still work for companies or government agencies with excellent pension plans and the financial strength to fulfill their promises. Saving for these Boomers will probably make an already good retirement, even better.

The majority of Boomers do not have excellent pension plans, if they have one at all. For them their savings will be a critical source of income during retirement. Somewhat surprisingly, these Boomers are not paying attention and have saved relatively little.

A number of explanations may account for why Boomers are ignoring the problem. One may be that they are using their parents as reference points. This may be a mistake. Our parents grew up, worked and retired in a very different world. To start, a gut wrenching Depression shaped their lives and everyone learned the importance of saving. Then WW II forced them to work together as a team. Is Boomers' disinterest in saving a subconscious rebellion against their parents' admonishments to save?

From these experiences, our parents and grandparents created what I call the "Golden Age of Retirement." They created the social security safety net. This wasn't needed when America was agrarian and people lived on farms. Have you ever heard of a farmer who retired and moved to the beach?

Our parents also shaped the tax code to encourage the establishment of employee and union pensions. While they had good intentions, the public and private systems they created are now being overwhelmed. The basic problem is that the system allowed our "leaders" in the business, labor and political worlds to make promises no one had to keep until many years in the future. The future is now and the cupboards are almost bare.

Perversely, I think Boomers are not paying attention because everything is going pretty well. We don't hear of people desperate due to poor retirement planning - yet. In addition, Boomers are a cocky lot and have never experienced a situation where their own hard work, would not make a difference. A Depression, where everyone is hurt regardless of ability, is almost beyond their comprehension.

How much money will Boomers need to live comfortably during retirement? The answer depends in large part on how long they live, which is obviously unknown. Nevertheless, here is something to remember, if a couple is healthy at 65, one of them will probably live into their 90s. To give them a reasonable chance of outliving their savings, investments must be appropriate and funds spent very slowly. Experts calculate retirees invested "correctly" can only spend 4.5% of their savings in the first year of retirement. If they then increase this first year amount only for inflation, there is good probability their saving will last into their 90s.

Hum…that means if a Boomer retires with a million dollars in the bank, he can withdraw $45,000, pre-tax, in the first year. My guess is that most investors who have saved a million dollars spend a lot more than $45,000 a year!

Are you starting to get sweaty palms yet? In 25 years, my guess is that we are going to have three classes of retirees. The first will be living off their pensions and be mostly government employees (teachers, police and transit workers) as most private plans are curtailed or eliminated.

The second group is reading this with sweaty palms. They realize the scope of the problem and will continue to save the best they can. Retirement will be good, but not great.

The last group is the problem. They do not have sweaty palms because they are not paying attention. If they even glanced at this article's headline, they quickly turned the page. This group appears to be using their parents for role models without putting in the hard work of saving and avoiding debt.

Sadly, I don't know who these people think will take care of them.

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