Ep. 221: Fixed Annuities, Wealth Transfers, & the Gig Economy - Transcript

Tom Mullooly: Welcome to the Mullooly Asset Management podcast. I'm your host, Tom Mullooly. I'm sitting here with Brendan Mullooly, and this is episode number 221. It kind of reminds me of that scene from Mr. Mom he's starting to work at home and he walks into the dining room with a chainsaw and Martin Mull asks him, "So, you going to rewire the place? You going to do 220?" He's like, "Yeah, 220, 221, whatever it takes." Okay, that's my joke for the week.

Brendan: I remember watching that growing up with you.

Tom Mullooly: We did a video this week about annuities and it's a popular topic for a lot of clients-

Brendan: Ken Fisher hates them.

Tom Mullooly: Ken Fisher does hate annuities. We are not in the hate column but we're in the severe dislike column.

Brendan: Yeah, I think it depends what kind. I think deferred annuities are oversold and most people don't need them because they have other place that they can put money tax deferred first before getting to there. So, especially seeing a deferred annuity in an IRA-

Tom Mullooly: I don't understand the meaning of that.

Brendan: Not great but there are many types of annuities, which is what you covered in the video. There are deferred annuities, there are immediate annuities, there are fixed annuities, there are variable annuities and so, there was an article in the Journal last week about fixed annuities. The headline was, "Why Annuities May Be Safer Than You Think." They were talking about fixed annuities in this article, just to be very clear.

Tom Mullooly: So, it's rare to see immediate annuities. It's a little less rare to see fixed annuities only because the rates have been so low and we covered this in the video. You may be locked into an annuity for eight, nine, 10 years. Your fixed rate may be fixed for a year or two or three. After that, it's going to fluctuate. It's really dependent on what's happening with interest rates at the time but it led to a bigger discussion that we couldn't get into the video where we talked about people spending time worrying about the credit worthiness of the insurance company behind it. You know, people getting worried about is my insurance company going to default? Problems like that.

Brendan: Yeah. So, the article in the Journal dug into that aspect of it. So, they were terming safer in the sense that the journalists who wrote this and backed it up with some information is pretty certain that in most cases, these insurance companies are going to be able to fulfill the obligations that they make to people, whether it be through insurance contracts or annuities. No guarantees but pretty reliable as far as things go like that. So, if people are doing a little bit of hand wringing over whether or not the companies going to be solvent enough to pay them, probably not worth getting worked up over in most cases.

Tom Mullooly: We did happen to have a situation in New Jersey, about 25 years ago, Mutual Benefit, pretty big insurance company here in New Jersey, which did have financial problems and the state insurance board did have to intervene. Everyone got paid. Now, the problem was, maybe your monthly checks, there could have been a large gap. The problem that we also run into is that when people hear that their insurance carrier or annuity provider is on the ropes, what do people ask for?

Brendan: They all want their money back at one time, which is not going to happen.

Tom Mullooly: It's just not possible because remember, the insurance company feels that they can get a better return by investing your money. They're just guaranteeing that they're going to pay you a monthly check if you're annuitized or whatever the minimal rate of return is, they're now taking that money and they're doing real estate projects, hedge funds, all types of venture capital things. So, they're taking all kinds of risks with that money but they're going to stand by to guarantee. So, the problem is that when people hear that an insurance company is on the ropes, they want all their money back and it's just not liquid, it's just not available-

Brendan: In many cases, that also wasn't what they were promised. So, for ask for it back is unreasonable.

Tom Mullooly: It is.

Brendan: In a lump sum. You were promised a monthly check. There is no lump sum anymore. You annuitized.

Tom Mullooly: Right.

Brendan: That's how it works.

Tom Mullooly: So, these scare tactics, we talk about some of the things that people get worried about when it comes to the future you.

Brendan: It's really easy to get hung up on all these things to be worried about. Nothing is guaranteed in terms of pay outs. There are just degrees of it and so, insurance companies are far to the spectrum of nearly guaranteed and the government is towards that end of the spectrum too. When we're talking about something like social security that everybody pays into more or less and everybody, I think, will collect on one day if you're paying dollars into it but apparently that is not the belief to the majority because within this Wall Street Journal article was a link to some Gallup poll data and in this poll from 2015 data, 51 percent of non-retired Americans think that social security will not pay them a benefit when they retire.

Tom Mullooly: I'm going to say this again real slow. 51 percent of people today, 2015, all right? So, a couple of years ago, but half of the people out there who are still working feel that social security won't pay them anything.

Brendan: Right. So, look to your left and look to your right and one of those people thinks they're not getting any money from social security and I think that it's easy to have this belief because a lot of people are distrustful of the government for whatever reason and I'm not going to go off on that tangent but it's easy to collectively gang up with friends and family and rip on the government. It's a national pass time. So, they're the ones backing this but in terms of who guarantees things, if I'm getting a guarantee from the U.S. government, I think that's pretty good and I think most of the world agrees with that sentiment because the dollar is by and large the reserve currency of the world. When bad stuff happens, people buy treasury bonds. So, we're talking about the spectrum of what's guaranteed and what's not. Obviously nothing is guaranteed but the U.S. government may be as far to the end of the guaranteed spectrum as you can go without being guaranteed. Do you agree with that?

Tom Mullooly: I totally agree. Like you said, it's all a matter of degrees of risk and safety. So, nothing in life is guaranteed but this is about as good as it can get. What I thought was really interesting was in that same Gallup article, you found some other numbers that I'd like you to share.

Brendan: Yeah, this poll has existed since 1989 and so, I was looking at that information too. So, in 1989, the same exact poll percentage of non-retired Americans who think they won't collect on social security. The first reading in 1989 was 47 percent and so, the 2015 one was 51 percent but it's not as if this is a new phenomenon where people have now become distrustful of social security or the government. This reading has fluctuated between 42 percent and 60 percent for 30 years now.

Tom Mullooly: So, basically, each generation, the generation that's receiving, if you were part of this poll in 1989, you might be receiving social security right now.

Brendan: Sure.

Tom Mullooly: But you didn't believe back in 1989 or '90-

Brendan: The numbers reflect that too. So, they break it down even and 50 plus, the percentages are very low in terms of who thinks they won't get it because I guess you're like close to the finish line, you can see the light at the end of the tunnel so to speak but ages 18 through 50, 63 percent think that they're not getting anything. I think that maybe this also speaks to the idea that people are so desperate to take social security right away at 62 even though they're getting a reduced benefit because they're so distrustful of the government and they feel like if they don't do it now, next year they could take it away from them because look, if half of the population believes they're not getting anything, I think that may be feeding into what we see and-

Tom Mullooly: Sure, take it now.

Brendan: 70 percent of people are taking social security before full retirement age for them. Sometimes people need the money. Sometimes people don't need the money but they're just so distrustful of the government that they take it anyway.

Tom Mullooly: Right.

Brendan: And look, that's a personal decision and a lot of factors feed into that. So, I'm not saying everybody that takes it early is wrong. That's not what I'm getting at but if the main reason you're taking it early is because you don't trust the government, I'm not sure that is a rational decision and look, you're the one who has to be able to sleep at night with your choices. So, if that is what makes you sleep, then good for you but I need to tell you as an outsider looking in, that may not be rational.

Tom Mullooly: Right.

Tom Mullooly: So, when we talk about social security and retirement, that also leads to another topic we were kicking around here in the office. Another story that we both saw on CNBC where 30 trillion dollars is about to change hands in the United States.

Brendan: So, I think the reason articles like this get written are because 30 trillion is an impressive number and that'll get some clicks because that's a lot of money that's going to be changing hands. So, you shared some thoughts on articles of this nature about wealth transfer. Do you want to share about that?

Tom Mullooly: I have heard this. Just change the front number on this headline. I have heard this line for 32 years.

Brendan: Yeah. So, people are going to inherit money and the number changes because-

Tom Mullooly: Of inflation.

Brendan: Your assets inflate and grow overtime but-

Tom Mullooly: Right.

Brendan: We had a client in here the other day who said something about money and-

Tom Mullooly: So, this was a class act.

Brendan: Yeah, this was really good.

Tom Mullooly: He said, "I'm not an Egyptian pharaoh and I can't take it with me."

Brendan: Right. So, it just speaks to this idea that wealth is going to be passed on and that's basically how things work. You save money your entire life and then you spend it down and if you don't have things to spend it on, then you're going to pass it on to somebody, whether it be a spouse or children or a charity or whatever.

Tom Mullooly: I secretly think that there's some of us, Tim included, who believe that he's going to be King Tut and he's going to be buried with lots of jewels and gold.

Brendan: Yeah, nobody's getting buried with a casket stuffed full of dollar bills but whatever.

Tom Mullooly: You could talk about Tim because he's not on this podcast but yeah, it's a theme that I have heard throughout my entire career and it yes, it's going to happen eventually but we're got some other things that are clogging up the pipeline too that we don't always talk about. One of the things we're starting to hear more and more from clients, survivors, kids of elderly parents now is not that they want to sound greedy but it's like, "Holy moly, this nursing home care is 12000 dollars a month. That's about 150 grand a year. First mom went through it, now dad's going through it and there's not going to be a nickel left for them."

Unfortunately, that's going to be the answer for a lot of folks as they get older. People are living longer, health care becomes more and more expensive and it is just a virtual drain on all of your assets until you get down to the medicate level.

Brendan: Yeah and look, if passing on something to the next generation is really important to you, there are other ways to approach it aside from liquid assets that you draw down on expenses towards the end like a nursing home or care or things like that. If it was really a priority, you can use things like trusts-

Tom Mullooly: Sure.

Brendan: You can obviously write things into your will. You can have insurance policies that pay off. That's not money you have, it's a policy that's going to pay off when you die. So, if that's important to you, there are other ways to do it if you have other expenses to cover in your later years.

Tom Mullooly: So, I'm not picking on CNBC today but I saw another headline that said, "More than a third of small businesses can't fill open jobs, a record." Which I scratched my head because I think if they interviewed a lot of small business owners, that number would be closer to a half.

Brendan: Yeah. It's always going to be an issue with any kind of poll. Who did they ask?

Tom Mullooly: Again, this is another theme that I've heard for a long time throughout my career but it pops up at different points. The last time I heard people talk like this where we can't find good, qualified people, whatever that means.

Brendan: Right. That was going to be my nit-pick. That's incredibly wishy washy and subject to the whims of whoever you're asking and what if they're standards are unrealistic and they want to pay somebody nothing and have them be uber qualified?

Tom Mullooly: Yeah, I want a PhD to come in here and work for 15 dollars an hour. It's just not realistic.

Brendan: Right.

Tom Mullooly: The line that I was going to draw was the last time that this was showing up in the headlines was 2006 and '7, right before a lot of people were suddenly available.

Brendan: And that's exactly how things work. The economy is cyclical and so, yeah, when we get to three percent, four percent unemployment, very low ratings, the only place it can really go is up eventually and when three or four percent of people are the only people with no jobs right now then yeah, the pool is diminished and maybe you can't find the exact worker that you want.

Tom Mullooly: Okay. So, another headline that we saw was, "Five ways to make the gig economy work for you," and they talk about five ways they give for people working in the gig economy could pretty much be said for people working in any kind of job. It didn't seem to me that they were really specific to just people who were working short term gigs.

Brendan: The stuff that they said did apply to these people because so, look, they have uneven cash flows, maybe they get a bunch of projects at once or a lot of work at once and then there's a lull. So, in terms of planning, they should definitely be trying to map out what they're going to do in the lean times, so to speak. So, a budget, an emergency fund may be larger than the average person is sensible but at the same time, there's a part of me I would recommend to somebody who may not have steady income that they should have a health emergency fund and so by standards, that would mean six months instead of three or you could argue more than that but when somebody has uneven income like that, do they even have the ability to sock away six to 12 months of expenses when they have bills to pay now an different money isn't coming in steadily, how are they? I'm not sure how they get to that point where they have the emergency fund that they need and then what happens if they do build it and then they need it? What's the plan to get it refilled?

So, there's a lot to think about there and quite frankly, I'm sure they have a lot more on their plate like finding work. If somebody is doing something on a gig basis and they haven't had work in a couple weeks, they're more worried about finding a job than filling their emergency fund to back up. That's the last thing I'm thinking of.

Tom Mullooly: That is the last thing on their list. So, I know that when I started Mullooly Asset Management, I wanted to make sure that I had enough of a reserve, enough of a cushion to start a business at zero and work its way up and you know what? I didn't have nearly as much as I really anticipated. I should have had double what I had set aside. It wasn't even close but eventually, you get to a point where it's like, "Look, I can work for another year or two and continue to stock pile assets." Who knows what career path I would have taken in the next 12 or 18 months but it was time to make the change and so, at some point, you just got to pull the rip cord and say, "We're jumping off the plane."

Brendan: Yeah, I'm sure a lot of business owners, entrepreneurs face that same decision. I think if you look at things like probability and base rates for new businesses-

Tom Mullooly: They all fail, right?

Brendan: Right. So, if you were worried about that, you wouldn't even do it but obviously, you have to have some sense of belief in yourself or maybe a little bit of a delusion for why the base rates don't apply to you and if no one was willing to take that risk, then we wouldn't have the kind of capitalism in this country that we do. So, it's good that people take that risk but at the same time, it is a risk and we only hear from the survivors.

Tom Mullooly: Yeah, I was just going to bring that up because before we turn the mic on, you brought up a really good topic about how we hear these statistics like four out of five new businesses fail in the first three years but we only hear the success stories, the people who actually toughed it out and made it. We don't hear about the 70 or 80 percent of people who wash out with the new business.

Brendan: Yeah. Everybody likes a good story and a lot of businesses that have made it do have really good stories. There's always trials and tribulations, there's struggles and there's triumphs. That's a natural story to tell.

Tom Mullooly: And it's a good story to hear.

Brendan: Yeah.

Tom Mullooly: Don't tell me about your losers, just tell me about your winners.

Brendan: Well, yeah and no one wants to hear-

Tom Mullooly: That sounds like a stock broker.

Brendan: You're not going to read in the news about the four restaurants that failed. You're going to hear about the one that's killing it on Main Street.

Tom Mullooly: Got a line around the block, yeah.

Brendan: Exactly and that's just the nature of being human but it doesn't mean that the other people don't exist. So, it's tough because we have this bias where we believe in ourselves more than we should at times, which is good and bad because it makes you do things that are risky and that maybe you don't perceive as being risky because you only hear from the winners and it lets you be blind to the actual odds your facing.

Tom Mullooly: Okay, last question for today, what's on your reading list right now and then I'll tell you what's on my kindle.

Brendan: I'm reading, right now, the Success Equation by Michael Mauboussin. That was recommended. It was actually in Thinking at Bets by Annie Duke.

Tom Mullooly: Okay.

Brendan: They cover similar topics. So, it's separating skill from luck and I had heard Michael Mauboussin on with Patrick O'Shaughnessy a year or two ago. He was one of the early podcast guests that Patrick had on. So-

Tom Mullooly: I think it was his first one. First or second-

Brendan: It was very early.

Tom Mullooly: It was very early, yeah.

Brendan: So, I've been meaning to get to this one because I enjoyed their conversation and it's good so far. I'll have more to report next time but I also finally read Thinking Fast and Slow, which was worth finally digging into. It was one of those cases where I was like, "Oh, I've read some of the papers or I've read Michael Louis, I've read the Undoing Project." So, I was like, "I probably have the gist of most of this," but it was still worth reading Kanheman, I think, separately. So, I would definitely recommend digging into that.

Tom Mullooly: So, I read Crushing It, the new Gary Vaynerchuk book. It's a very easy read. You can read it in a weekend, very easily but great stories, positive examples of what can be done if you focus and hustle and I'd encourage anybody who's in business to pick it up and read. It's such an easy read and he kept most of the potty mouth stuff out of the book. So, that's good.

Brendan: I don't mind that, I'm fine with the potty mouth stuff.

Tom Mullooly: Yeah, we know all the words. I'm also reading Astro Ball right now which is the story of the rebuild of, the tear down and the rebuild of the Houston Astro's.

Brendan: They already have a book?

Tom Mullooly: Oh yeah.

Brendan: Wow. Well, I guess that's fair because they made Baseball Maverick after the Mets went to the world series? They didn't even win it, at lease the Astro's won, right?

Tom Mullooly: Right. So, the writer for sports illustrated, who's the author of the book, his name escapes me right now, I'm sorry but Tim will put it in the show notes, they actually made a prediction in 2014 that the Houston Astros would win the world series in 2017 and it happened exactly that way. So, made for a great story in Sports Illustrated and a much better book, which just came out last week.

Brendan: Oh, cool.

Tom Mullooly: Yeah. So, well, thanks for tuning into episode or podcast episode number 221 and we will catch up with you next time.