Ep. 223 - Transcript

Tom Mullooly: Welcome to the Mullooly Asset Management podcast. This is episode number 223. I am one of the co-hosts, Tom Mullooly. My other co-host is here, Brendan Mullooly.

Brendan M.: Hello. Ready for action.

Tom Mullooly: What we typically do is run through some of the headlines of the day, things that people are talking about on Twitter or that we're seeing in the financial news that we think are worth sharing, and we try and keep it fast-moving. Brendan, what's caught your eye this week?

Brendan M.: I saw a Tweet that Bob Seawright shared, and it had a link to a post that was titled The Most Googled Financial Questions By State. I looked at it already, but I wanted to see if you could guess what some of these top ones are. These are the top things people are googling about finance.

Tom Mullooly: By state.

Brendan M.: By state, but they rank them. Some states had the same one, so see if you can get one of the top 10, let's say.

Tom Mullooly: All right, so this is going to be like Family Feud. Survey says ...

Brendan M.: Yeah, exactly.

Tom Mullooly: Okay. All right. Mortgage rates.

Brendan M.: All right. We've got mortgage calculator, interest rates, so close, close on that. That was a good guess.

Tom Mullooly: Okay. How about what's a home equity loan?

Brendan M.: No. No home equity loan. I'm surveying the top 10. It may be outside of the top 10, but not in there.

Tom Mullooly: Okay. How about what is an APR, annual percentage rate?

Brendan M.: No. All right. I'm going to run through some of the top 10, but they do-

Tom Mullooly: You're saying I'm flubbing?

Brendan M.: Okay, so they also have this cool little map, and I'll make sure that we link to this is in the show notes, but they have a map that does each state's one, and there are so many that are foreclosure, which is a bummer. A lot of student loans, so different ... and so some of the ways they phrase it are different, but how do student loans work? is one of them or-

Tom Mullooly: I was going to bring up credit cards.

Brendan M.: Right. Credit cards are in there too, pay day loans, unfortunately.

Tom Mullooly: Oh, my goodness. That's awful.

Brendan M.: New Jersey's top phrase that was googled is debt consolidation.

Tom Mullooly: Yikes. Yikes.

Brendan M.: These are all not great, but just to show you what people are looking for. A lot of these, I think, may be counterintuitive to people who follow the markets and are more focused on investments, but all of these are more like personal finance. Budget planner is on there. People want help with, really, the building blocks of finance. I think that that is a signal to people like us who work with individuals. It's easy to overlook these simple things, but this is really the stuff that people need help with.

Tom Mullooly: Okay, so this is going to sound like it's a little off-topic but, my first year of college, one of the electives that I was offered to take was a course called Music and the Movies. Every class, you sat there, and you watched a movie. One of them was The Godfather. One of them was The French Connection. I mean this is the kind of thing that ... We send our kids to college, spend a lot of money. They learn about the music in movies. Why don't they teach them how to budget? Why don't they teach them how to pay bills on time, how to open a checking account? What's a mortgage? What's a home equity? How do you save money for retirement? How do you handle your student loan? Why don't they have courses on that?

Brendan M.: Not sure. I think some of those things you have to want to be interested in, though. I'm not sure if you put a course out there that covers those ... I'm not sure that that-

Tom Mullooly: Music and the Movies is really-

Brendan M.: It sounds sexy. You know?

Tom Mullooly: Yeah.

Brendan M.: I'm not sure people sign up for that course. Some of those things are things that you kind of just get forced to learn about, and the best way to learn about them is by doing them. How to live on what you make, that's when you learn how to budget, right? Not-

Tom Mullooly: How to live within your means, yeah.

Brendan M.: Not when ... I don't know. I guess you do that, to an extent, at college, but the budget consists of what? Pizza and beer.

Tom Mullooly: Pizza and beer, gas for the car. Yeah.

Brendan M.: I mean so, on a smaller scale, maybe you build up to that, but ...

Tom Mullooly: This is a course they could teach while people were online to sign up for Music and the Movies. Now I say online. We used to actually have to wait to sign up ... get on a line to sign up for classes. Now you just submit it, I guess.

Brendan M.: Back when I was in college, we did it ... it was online. They'd assign you a time based on your last name, or your number of credits, or something along those lines and-

Tom Mullooly: That's when you want to change your last name to Able or something like that.

Brendan M.: I thought that was good and just ... I mean it kind of shed some light on what people are really worried about in this country. I mean it was cool to see, state by state, what people are looking for.

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Tom Mullooly: Let's just stay with this for a second because one of the articles that you and I both talked about this week was in The Wall Street Journal. The pension hole for US cities and states is now the size of Japan's entire economy. What?

Brendan M.: Yeah. These pensions are underfunded, which is ... This was an interesting way to put it that grabs your attention. It shows you the extent of what some of these pensions are working with. I mean we both read the posts. I mean what are some of the solutions that are out there, and why haven't they been tried yet?

Tom Mullooly: They're unpopular. It's kind of like they used to talk about, "Hey, if you're going to discuss Social Security, it's like the third rail of politics." It's the same thing. It's raising taxes. It's cutting costs, cutting services, and then also, maybe in the future, cutting benefits. That's ...

Brendan M.: Those are exactly ... so which of the three or a combination of those three are going to be okay with people?

Tom Mullooly: None. Zero.

Brendan M.: If you do a combination of the three, you're probably just going to piss of everybody, so maybe ... I don't know. I also read, maybe it was in this same post or a different one, about, similarly, the issues with pensions where they were talking about ... No, it was this one. They were talking about one town specifically, and it was the police and fire pension and how they agreed to get 55% of whatever the benefits were. It's more or less like if you own stock or bonds from a company that's going bankrupt. You're willing to accept pennies on the dollar because you're afraid you might get nothing. In this instance, they accepted 55% of whatever their benefits they were promised, and now the financial situation has improved, but they already took the deal, so ... and they're not getting raise ... they're not going to raise the benefits back up now.

Tom Mullooly: No. Of course their financials are going to improve because they took the deal. That is the reason why their finances improved. It's going to be a mess. It's funny. I mean sometimes our conversations kind of go off the rails a little bit around here at the office, but I suggested to the guys that they read up on the French Revolution this week because if they start cutting pension benefits, that is what our world could look like. I mean you don't want to be a fear mongerer, but if you've worked your entire career, and you've basically banked on the idea that you're going to have this guaranteed income stream in retirement, and now it's not there or it's severely reduced, people are going to do freaky things that are not good behavior.

Brendan M.: The problem, I think, is for a lot of people in this situation where maybe they're not retired yet or approaching it. Maybe they're in their 30s or 40s working a job where they're paying into a system like this despite knowing that there are issues. Oftentimes, they don't really have a choice, so the pension ... If you're in the union at work, which also doesn't seem to be a choice very often, you're paying your dues into this pension over time and, in many cases, these are public servants that aren't really making a ton of money, so not only are things like taxes and whatever they have to pay for their healthcare coming off the top, but their pension are coming off too, so-

Tom Mullooly: They've got these retirement costs, yeah.

Brendan M.: Look, everybody can make the ability to save if they really want to, but these people may not be as able to save above and beyond the pension as we imagine, because the solution here is like, "Okay, so if the pension isn't going to be there, I know I have to do a better job saving on my own, and if the pension is there, then great. I'm just better off." Sometimes these people don't make enough money to do something like that and live their life and support their families off of their income. It's tough.

Tom Mullooly: On a somewhat related note, when the Social Security program was implemented in 1935, there was something like 14 workers for every retired person. Now it's almost one to one.

Brendan M.: Right. Demographics are changing here.

Tom Mullooly: Yeah.

Brendan M.: One of the things that I thought was not very cool about this was the way ... One person they interviewed presented it this way. These people who have been paying into pensions have been paying in their side of the bargain basically forever, and the other side of the bargain is what these different municipalities or states are supposed to be contributing to the thing too, the pension fund, and they're not, and that's ... I think that's a problem because ...

Tom Mullooly: It's a huge problem.

Brendan M.: One of the things they said was that, during the '90s, they said that they market growth in conjunction with the participants' contributions was enough and that they didn't need to send in extra money because things were going so well, and so they did things like that or, conversely, they did something similar where they just said, "Market returns are great, so we're going to promise these insane benefits to people." Then, obviously, mean reversion kicks in like we all know it does, and we experience a decade of below-average returns with two market crashes and, oh, guess what? Now we can't fund the pension anymore. Maybe we shouldn't have done that?

Tom Mullooly: You just described exactly what occurred in the state of New Jersey from 1992 or 3 through the end of that decade. We were told, "Hey, the market's generating enough returns." I mean New Jersey used to be AAA-rated state. Now we're borderline junk. Then we went through this decade where we had negative returns, flat returns, still no contributions going in. Now it's just we've kicked the can so far down the road. We've gone 25 years without putting money into retirement benefits for state employees.

Brendan M.: That's not by the fault ... A lot of people will look at situations like this and point the finger at the employees who have ... they're the ones who have been paying into this. It's not as if they stopped their contributions here. They did their part. I don't know what the solution is. Like we discussed, three options, none of them seem great. They are going to be unpopular but, at some point, we're going to come to a crossroad, and the decision's going to have to be made.

Tom Mullooly: Come to Jesus meeting. That's kind of the way it's going to go.

Brendan M.: Similarly to these kind of issues from these pension funds, I saw another post from The Wall Street Journal over the last week that was called The Market Isn't Going to Save You From Saving Too Little. It's just like, wow, is this the same problem individuals and institutions are having?

Tom Mullooly: It has to be. We've done videos and blog posts about this topic as well, is that you can't expect that the market's going to give you double-digit returns forever into the future and that's going to, basically, bail you out of not saving enough money. Can you imagine? I mean we have similar themes here in the office where we talk about, "Hey, you know, right now we're getting a little extra gravy," you know what I mean? in terms of things happening with the business, but we shouldn't be living on the gravy. We should be living on the mashed potatoes. You know what I mean? We should be doing things, the block and tackling stuff that gets done every day. People should be saving money systematically, whether it's a small amount, large amount, doesn't matter. They should be saving something for the rainy day because it's going to happen.

Brendan M.: Yeah. I mean and I think doing the work to figure out small amount, large amount, the dollar total I'm not sure is the right way to frame it. I think you want to take a person's income and get to that percentage that is a healthy percentage. Yeah, the dollar total is going to be very different for everybody out there, and that's fine, as long as you're saving a healthy percentage of your income, then you're doing your part to make sure that you aren't under-saving and then trying to hit home runs in the market, because we all know that, inevitably ... We don't know when mean reversion is going to occur, but periods of high returns are followed by periods of low returns. We just discussed the '90s and then the 2000s.

Over the long term, you're going to have several of these cycles over your investing lifetime if you're in the market for 30, 40, 50 years, like many people will be, and that's fine. I think, over time, it averages out, but if you're not saving enough in the beginning, and you're shortening the playing field to one or two decades, the ability to earn high average returns over a lifetime, it just gets tougher and tougher the more you close that window up. You might get lucky, but you might not, and I don't really think that that's something you want to leave up to chance.

Tom Mullooly: No. You're going to be in charge of your own future if you can put these basic concepts to work like paying yourself first, not spending more than you're bringing in. Those two things are really the building blocks of everything.

Brendan M.: It's classic Buffett, though, like simple not easy. Right? It's so easy to talk about these concepts, but to actually follow through with them is not. There are so many different things that feed into it that can stop you from doing those. It's really easy to let your lifestyle get out of control. It's really easy to make emotional mistakes with your investments, but yeah.

Tom Mullooly: I just realized that my Escalade is double parked, and I left it running. I'm burning all that gas. I'm kidding. These are the kind of things that we see on a daily basis, some poor decisions.

Along those lines, and again, I don't want to make this sound like a soap box, but another article from The Wall Street Journal where it said young people don't want construction jobs. That's a problem, of course, for the housing market, but it's also a problem because folks aren't learning some basic skills, how to swing a hammer. I think that's actually kind of important. We have a couple of new homeowners here in the office, and I told them, "Hey, in your first house, that's where you make all the mistakes." This is how you learn how to tear things down, and put up a wall, and patch things. Your first home is where you can make all the mistakes, and it's not going to cost you a fortune in terms of, "Oh, I should have done this or I should have done that, and now I can't sell my half-a-million-dollar home."

It's unfortunate because I think some of these folks overlook these construction jobs, and they can actually lead to pretty well-paid careers. I'm pretty certain, in the last podcast or the one before this, we talked about a client that I had who was a plumber, and every two years he would lose his new hire because he would go out and get his master plumber license, and he'd go into competition against his boss.

Brendan M.: I think this is a societal problem, though, because there was one line in this article that really grabbed me, and it was this idea that if your child does not go to college, that you've failed them. It's not only the kids that don't want these jobs. It's because their parents made them not want these jobs because they think that they have to go to college, or the kid feels like a failure, and the parent thinks that they failed their kids or that their kid is a failure when, realistically, none of that is true.

Like you said, you can have a great career, be a business owner, make a ton of money doing jobs that don't require college. It's getting talked about more and more now, but it's going to be this shift of mindset that has to happen because, again, it's one of these things that's super easy to talk about like, "Oh, yeah these ... The people out there, they should just go to trade school and learn how to do these crafts," but who is that? It wasn't me. It wasn't-

Tom Mullooly: It wasn't me, either.

Brendan M.: Right?

Tom Mullooly: Yeah.

Brendan M.: We can sit here on a podcast and talk about it, but until people truly believe it that it's a viable career path, maybe these shortages continue. I don't think they should, but it's tough.

A good post from Christine Benz at Morningstar, and she talked about what you should do with your home equity in retirement. I thought this was interesting. An often overlooked part of somebody's assets, I think, is the value of their home.

Tom Mullooly: Not to branch too far away from the subject, but I think the order in which you start your deaccumulation phase is something that people don't really give a lot of thought to. We just met with a client yesterday, and we kind of had to reprogram this person in terms of thinking like, "Hey, maybe living off Social Security first isn't going to be the right answer. Here's another potential outcome to think about." The gist of the article, if I'm understanding it, was that a lot of people will spend down their liquid assets, and now they've reached older age, if you want to call it that, and they're cash poor, house rich.

Brendan M.: No, that's absolutely it, and some really good stats from the article, just to speak to that point, 66% of people aged 65 to 69, 66% of their net worth is in their house, and this number climbs as people get older. For people between ages 70 and 74, 70% of their net worth is in their house, and for people over age 75, it's 76%. It kind of speaks to your point of the idea that people are more willing to draw down things like investment accounts, draw on things like Social Security before they consider the house.

I understand that from the perspective that the house is primarily a place where you live, but some of the things that Christine posts in this article that I thought were, again, worth considering as part of your deaccumulation strategy in retirement would be to sell the house, downsize or rent, so move into a smaller place, net the difference, and you can use some of that money to live on in addition to your already liquid savings. You could rent at a lower cost and, again, take the money that you get from the sale of your house and live off of that in conjunction with retirement savings that you have.

A reverse mortgage, for some people, might be worth exploring if they want to stay in their home, not downsize, but would like to use some of the equity that's in there, or what a lot of people do, the third option she talked about was that you stay in the home, and you use that as, basically, estate planning tool, so it's the home is the asset that's going to go to the heirs, and you're going to live off of the IRAs, and investment accounts, and whatever else you have. You're going to drain all of those but leave the house to your kids or whoever.

Tom Mullooly: Right, so a lot of things to think about. It's not as cut and dried as you may think, so we encourage our listeners, when they've got questions about topics like this, that they really need to sit down with a financial planner and ask.

One of the articles that we found that didn't really make the cut this week was in CBS MarketWatch. It said don't be afraid to ask dumb questions about money.

Brendan M.: No dumb questions.

Tom Mullooly: There are none.

Brendan M.: I hate that because it's cliché to respond how I just responded, but I think that it's true. If it's something that you don't understand that you want to know, just ask, I mean

Tom Mullooly: Yeah. They interviewed this financial planner out in Colorado Springs, and she said, "One of the most common things I hear from clients is, 'I feel like should understand this better, and I'm embarrassed to show you this.'" We hear this all the time. There's no such thing as a dumb question. Reach out to a planner or reach out to us. We would be happy to talk to you about whatever kind of questions you have.

Thanks very much for listening to podcast episode 223. We will catch up with you again on the next episode.