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PENSION POVERTY AHEAD – *Pensions are Underfunded and No Longer Risk Free*

MACRO INSIGHTS

Gordon T Long
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PENSION POVERTY AHEAD

SIMPLY TOO FEW CONTRIBUTORS versus BENEFICIARIES

The post WWII "Baby Boomers" are now retiring. This massive surge has worked its way through the economy reflecting surging homeownership, consumerism, and investments and now is entering the stage of medical and healthcare services, drugs, elder care etc. The later are heavily weighted as entitlements.
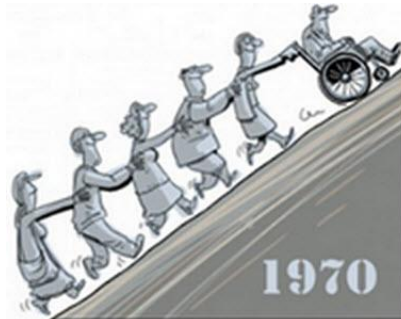
During this same period of social evolution we witnessed the advent of the "birth control pill" which reduced family sizes and the growth of the labor force (less immigration and two spouses working).
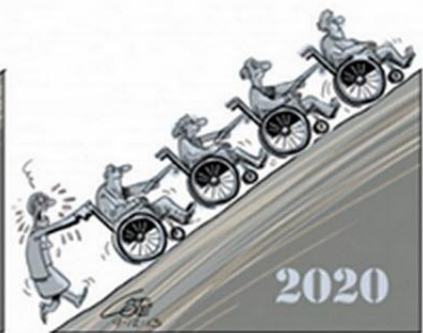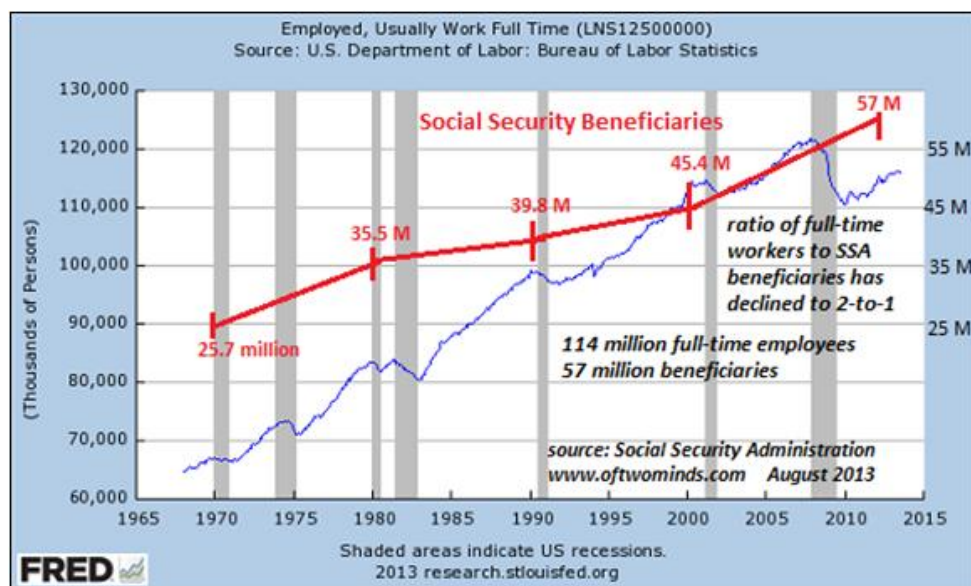
The Social Security Beneficiaries

Couple this with people living longer and "family supporting" jobs becoming more difficult to find (and hold) has resulted in huge pressures on entitlement promises for retirement.

1970   1990

2012   2020

Additionally, more and more people quality for social entitlements for medical, disability or other reasons. We now have too many people dependent on too few workers.

Too many people dependent on too few workers

Employed, Usually Work Full Time (LNS12500000)
Source: U.S. Department of Labor: Bureau of Labor Statistics

Social Security Beneficiaries

57 M

45.4 M

39.8 M

35.5 M

25.7 million

ratio of full-time workers to SSA beneficiaries has declined to 2-to-1

114 million full-time employees
57 million beneficiaries

source: Social Security Administration
www.oftwominds.com   August 2013

Shaded areas indicate US recessions.
2013 research.stlouisfed.org

FRED

(Thousands of Persons)

Current Public Policy Denial

As obvious as this problem is few developed nations have done anything to prepare for this inevitability.

Political leaders in America, from Clinton to George Bush raised the seriousness of the issue but nothing has been done to prepare financially or physically for this new era.

Insufficient Nursing homes are being built, affordable assisted living facilities are not meeting the demand, and entitlement payouts are not rising to meet inflation pressures.
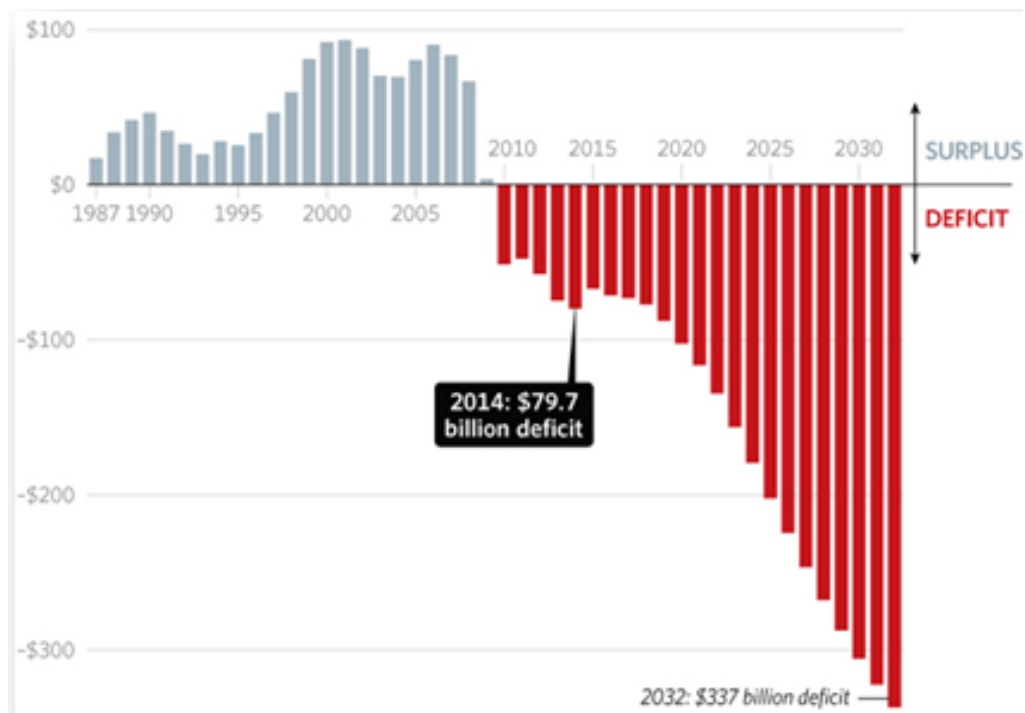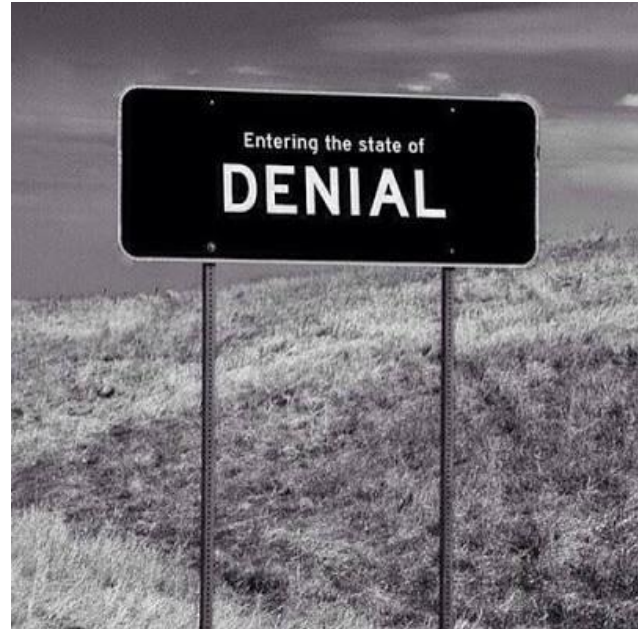
It leaves both the public and government with what amounts to an 'impossible" problem.

The US and most developed nations have simply waited and procrastinated too long.
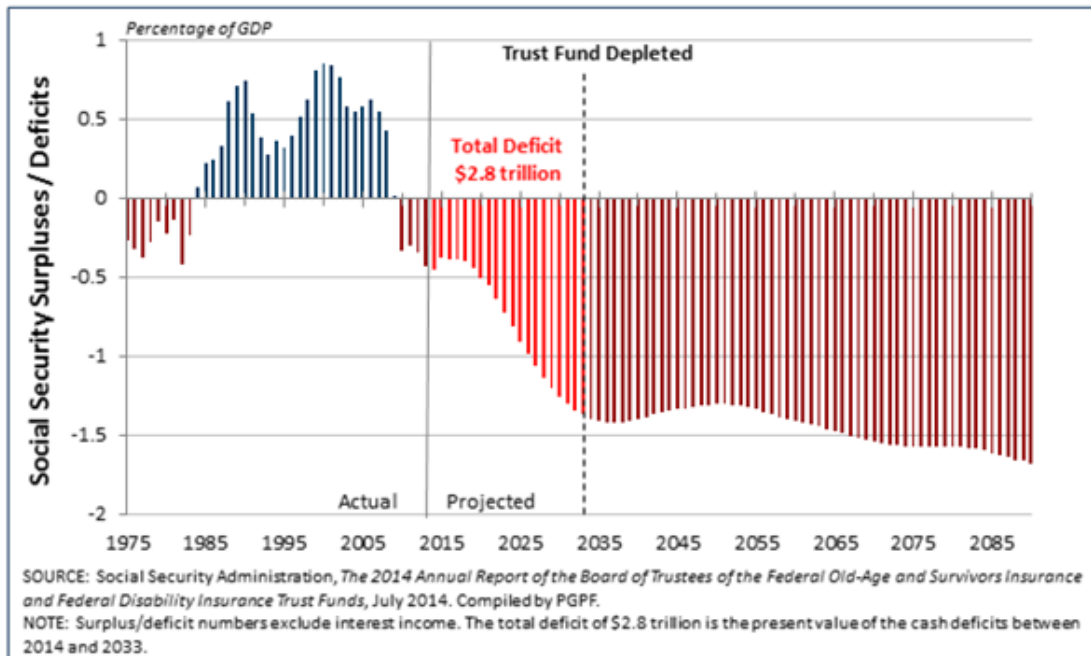
The Social Security Deficit

Social Security Deficit – Near Term

The entitlement deficits are massive ….

Social Security Deficit – Longer Term

…. and expected to get even worse.

SOURCE: Social Security Administration, *The 2014 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 2014. Compiled by PGPF.

NOTE: Surplus/deficit numbers exclude interest income. The total deficit of $2.8 trillion is the present value of the cash deficits between 2014 and 2033.

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Three Stools of Retirement has lost two of Its Legs!
The three legs of retirement have always been considered by planners to be:

1. An Employer Pension,
2. US Social Security,
3. Personal Savings

Two major developments have additionally occurred to compound an already monumental problem:

In the case of the US there has been a seismic shift from Defined Benefits to Contributory Benefits. The result of this has been the loss of a pension because 401K's in America for Contributory Pensions now averages 18,400. An amount that is currently enough to retire (at the poverty level) for LESS than a year.

With ZIRP (Zero Interest Rate Policy) currently delivering nearly no interest on a retirees life's savings many retirees are having to use capital to live on versus income from their savings. According to Swiss Re nearly half trillion dollars has been taken from savers and retirees since ZIRP and QE programs were initiated.

The combination of these two factors has quite literally pulled the stool out from under the retiring "baby boomer" generation.

Many had hoped to solve this problem by selling their homes which was the predominate area of growth in their wealth over the last few decades. Unfortunately, the realization has now come that the cost to live anywhere else has grown dramatically as has mounting property taxes on a home that they may have paid off with through prudent savings.

Household Retirement Accounts
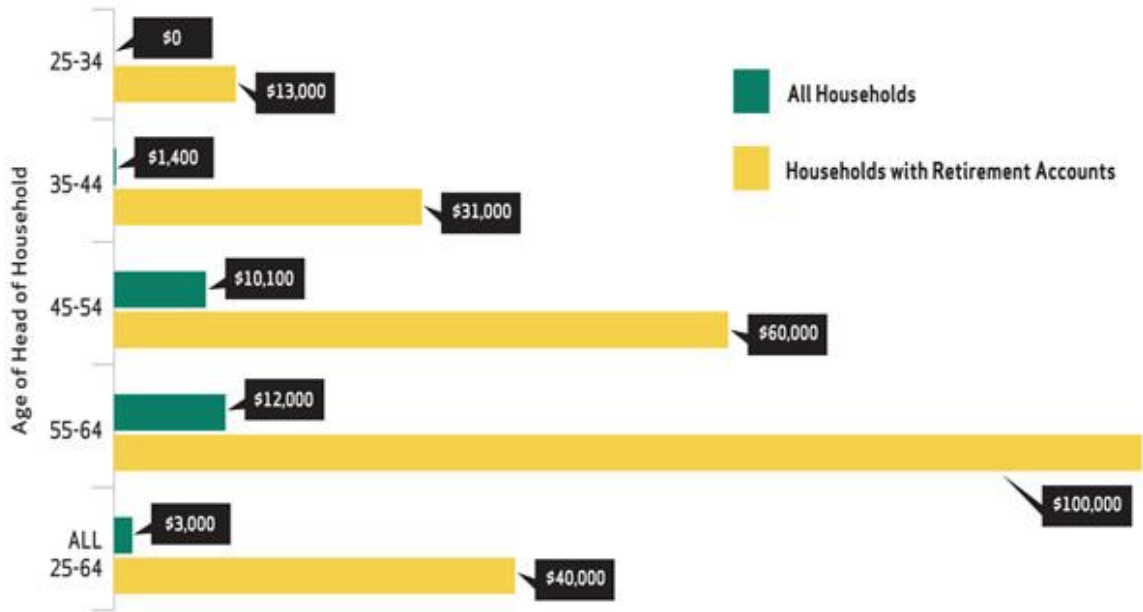
But it gets worse!

PBGC's Safety Net Exposure

US Public and Private employers have not been paying into the existing pension funds. This has resulted in approximately $4.7T in unfunded State and Local Public Pensions, Close to $3T at the Federal Public Pension level and another $3T in the private sector. There is a looming $10T pension problem which additionally needs to be addressed.

Insurance to protect against pension failure is also insufficient to cover potential needs.

Figure 5. PBGC's Safety Net is Effective for Current Plans, Less so for Future Plans
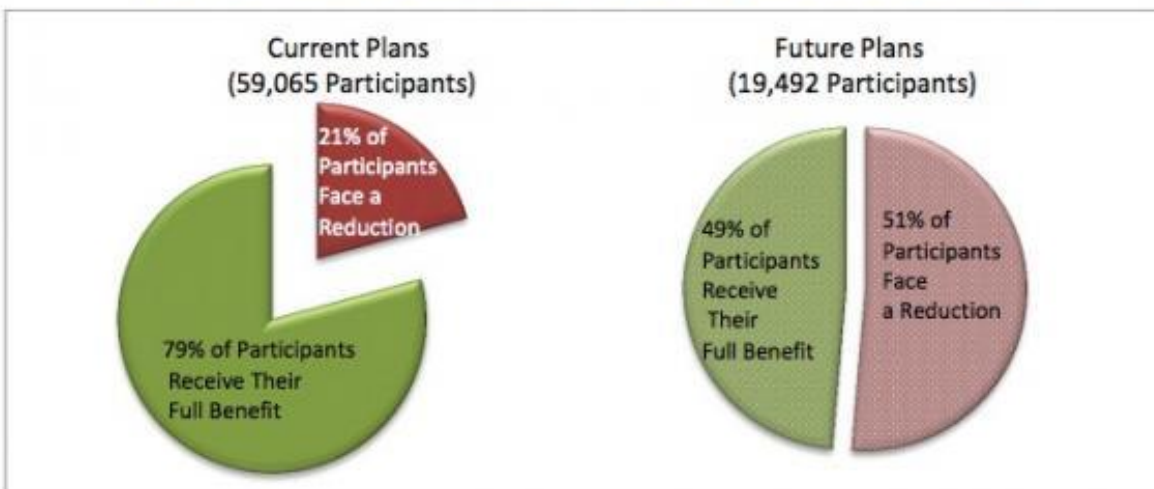
Let's consider that basic issues at hand. I will use a set of slides which I used with Charles Hugh Smith in a recent Macro Analytics discussion. We attempted through the slides to understand the issues in more detail.

WHY ARE PROMISED PUBLIC PENSIONS & BENEFITS UNSUSTAINABLE?

1- Demographics & 2- Low Yield ZIRP Economics

Macro Analytics June 20th, 2015

The Coming Era of PENSION POVERTY

Why are the pensions and benefits promised to public employees unsustainable?

1. **DEMOGRAPHICS:** Back in the day, there were 10 workers for every retiree. That slipped to 5 to 1, and it is now around 2 to 1: only two full-time workers for every retiree.

2. **LOW YIELD ZIRP ECONOMIES:** Pension funds were based on a minimum annual investment return of 7% or more. Returns of 3% or less mean the promised pensions cannot be paid out of investment earnings—they must be paid by higher taxes.

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3-Investment Risk

Macro Analytics June 20th, 2015

The Coming Era of PENSION POVERTY

Why are the pensions and benefits promised to public employees unsustainable?

3. RISK: Increased risk of pension fund investments. Pension managers have compensated for low yields by shifting more of the fund's capital into high-risk investments such as junk bonds as a way of capturing higher yields.

This strategy has paid off in a 'risk-on' environment but has the potential to yield catastrophic losses in a "risk-off" downturn.

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4-Politics

MACRO ANALYTICS

Why are the pensions and benefits promised to public employees unsustainable?

4. POLITICS: Many public unions have exploited the system by buying political favors. Many retire at 55 and game the pension plans to retire with 90% pay based on their last year of service, which includes huge overtime pay; questionable disability claims that make their pensions tax-free, etc.

This has changed the public employee pension plans from models of modest payouts to cash cows in which employees rake in $250,000 payouts upon retirement, are hired back as consultants (double dipping) and a host of other abuses.

5-Disposable Income

MACRO ANALYTICS

Why are the pensions and benefits promised to public employees unsustainable?

5. DISPOSABLE INCOMES: Voters squeezed by stagnant incomes and steep increases in healthcare and educations costs cannot afford to pay higher local government property taxes without crimping their consumption.

Forcing voters to pay for public pensions with sharply higher taxes (all levels) will trigger a self-reinforcing recession as consumption declines -> lower consumption/sales taxes, lowering local government revenues despite higher taxes.

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WHY IS THE SOCIAL SECURITY SYSTEM AT RISK?

1-PAYGO and Demographics

Macro Analytics June 20th, 2015

The Coming Era of PENSION POVERTY

Why is the Social Security System at risk?

1. **PAYGO:** Social Security is "pay as you go"—the Trust Fund is a fiction, IOUs that are empty promises, not tradable securities. The deficits in Social Security must be paid with higher taxes or by selling Treasury bonds, i.e. increasing Federal debt.

2. **DEMOGRAPHICS:** there are only 2 full-time workers for every Social Security/Medicare recipient.

2- Existing Deficits

Macro Analytics June 20th, 2015

The Coming Era of PENSION POVERTY

Why is the Social Security System at risk?

3. EXISTING DEFICITS: Social Security is already running deficits:

Social Security Ran $47.8B Deficit in FY 2012; Disabled Workers Hit New Record in December: 8,827,795
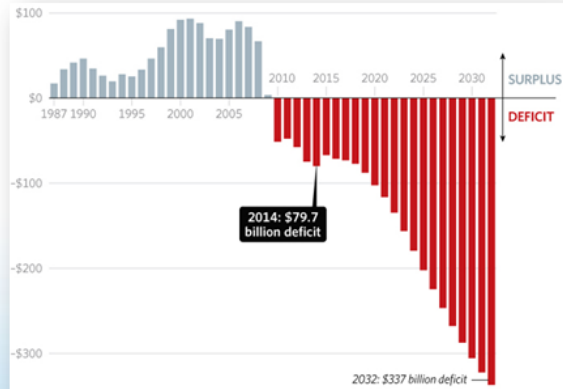
http://cnsnews.com/news/article/social-security-ran-478b-deficit-fy-2012-disabled-workers-hit-new-record-december

3- Non-Retirees

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Why is the Social Security System at risk?

4. NON-RETIREES: Social Security is supporting an increasing number of non-retirees, i.e. disabled.

Social Security Disability Insurance Benefit Payments Have Grown Dramatically Since the Program's Inception
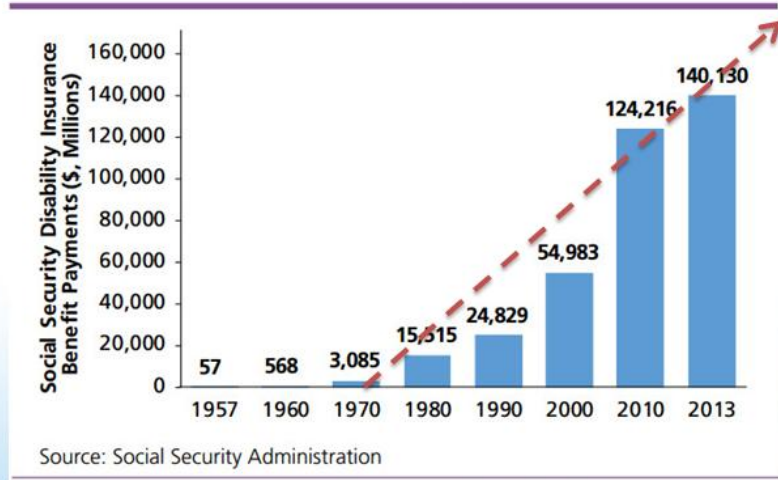
Source: Social Security Administration

4- Demographics and 5-Financial Assumptions

The Coming Era of PENSION POVERTY

Why is the Social Security System at risk?

5. DEMOGRAPHICS: the number of baby Boomers who qualify for Social Security and Medicare is set to soar -- 60+ million Boomers are entering these programs while the economy only supports 115 million full-time jobs.

6. ASSUMPTIONS: Faulty actuary assumptions. When Social Security was established, it was assumed there would always be 5 workers for every retiree, people retired at 65 and that the average age at death was mid-to-late 60s. The system was not set up for people retiring at 62 and living into their 80s.

PUBLIC WORRIES – MEDIA BEGINS TO FOCUS

Though our politicians refuse to discuss or address these issues and public media has recently began focusing on the issues because it is central to what their followers are worrying about.

Working Late 1 of 16

Retirement Realities: Why It's Getting Worse

Retirement savings are inadequate. Social Security is shrinking. Will most of us work until we drop? **Drastic Changes Could Be Necessary »**

Find the Best and Latest High-Yield CD Rates

10 Best States for Retirement

CNBC

Retirees: Prepare for Huge Health Costs »

Which Tax Bracket Do You Fall Into?

Fast Food Menu Items You Won't Recognize

Military Tech Helps You Shop for Furniture

Can Amazon-Like Reviews Work for Prescriptions?

Congressional Controversy 3 of 15

Social Security Under Threat

As funds run out, Congress is wrangling again over Social Security. **Will There Be Cuts? »**

Find the Best Savings Account Rates Now

5 Little-Known Facts About Social Security

Link Savings to Checking for Higher Yield

Pension Problems

Why Pensions Are Plummeting

Private pensions dropped another 9% last year. Many companies are now trying to buy out pensioners with lump sums. **What You Need to Know**

GET READY – ITS COMING!

Greece, Puerto Rico & Chicago

We have recently witnessed major financial problems from Greece to Puerto Rico to the City of Chicago / State of Illinois.

What they have in common is their inability to pay the short term immediate pension obligations. The money was simply not there.

In all situations the endless 'can kicking' and 'accounting trickery' came to an abrupt halt as they ran out of games they could play.

The other thing they all have in common is their inability to print more money or debase their currency. Unless money is printed for them by the EU/ECB or the US Treasury/Federal Reserve they have few option.

Expect this to become more widespread in the EU peripherals or the US equivalent, being State & Local government.

The Pension Crisis is going to be huge, protracted and will take down governments with it.

An Era of Pension Poverty lies ahead for many in the Developed Economies.

Greek pension funds ration payouts

NEW WORLD

Tsipras backs down on bailout demands

Greek prime minister vows to accept almost all the creditor conditions

- Explainer How to contain Greek contagion
- All eyes on ECB as Greece's time runs out
- Payment failure pitches IMF into uncharted territory

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