A Talk With Nick Murray

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Editor's Note: Editor-In-Chief Evan Simonoff sat down last month with author and advisor Nick Murray to talk about the retirement income challenge. Murray will be a keynote speaker at the upcoming Financial Advisor Retirement Symposium in Las Vegas.

Q. It's widely accepted that most baby boomers have undersaved. Even among advisors' clients who are savers, there is a gap between the perception and reality of the amount of retirement income their savings can buy. Global monetary policy isn't helping. Some think we are headed for a train wreck as big or bigger than the financial crisis. Others say humans have remarkable abilities to adapt. What say you?

A. First of all, undersaving isn't a baby boomer phenomenon. It's a human phenomenon. Fifty percent of all Americans over the age of 65 are living entirely on Social Security. Undersaving (and underinsuring) are why the financial advisor was sent into the world. Second, I don't see what "global monetary policy" has to do with anything; Americans save and spend in dollars, and the dollar is far and away the most credible currency in the world, not that that's saying much. Third, some people are always predicting a train wreck to dwarf all other train wrecks; history counsels otherwise. And history has to become our investment philosophy. Our only other choice is chaos theory, and I don't know how to make investment policy out of chaos theory.

Failing to plan is planning to fail. For people in the accumulation phase of life, that means a written, date-specific, dollar-specific retirement accumulation plan, premised on long-term historical returns. Once in retirement, it has to become a retirement income plan which, at historic returns, defends and even accretes purchasing power. We financial planners know how to craft such plans, and they should always be our focus. The rest is noise.

Q. We are six years into the most unloved bull market in most Americans' lifetime. According to some measure, only one bull market since 1873 made it to seven years and that was from 1897 to 1903. Should that be a source of concern?

A. I guess if you torture the data long enough they'll confess to anything, but it really depends in part on how you define a bull market. We had one from 1946 to 1968, by my reckoning—albeit one interrupted by three relatively brief and relatively shallow (i.e. less than a 30% decline) downturns. We had another from August of 1982 to March of 2000, interrupted essentially by one day of horror in 1987 and a couple of blips in 1990 and 1998. And in the largest sense, we've had one since those guys met under the buttonwood tree; it is quite wonderfully ongoing, as how could it not be?

But beyond all that, I don't see how this line of inquiry gets us anywhere, inasmuch as the market can never be timed. Peter Lynch said it best: "Far more money has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in the corrections themselves."

Q. The biggest risk facing recent retirees in the last 15 years, according to experts, is a phenomenon defined as sequential risk, or retiring just before a bear market begins. Millions of Americans experienced this when they retired in 2000–2001 and in 2008–2009. So some like Wade Pfau and Michael Kitces have proposed standing the traditional 60% equities-40% fixed income on its head, and moving to 70% fixed income-30% equities and not rebalancing, but instead just letting the equities ride over the remainder of their lives.

A. After observing that whatever the biggest risk was over the last 15 years won't be the largest risk over the next 15 (during which we seem unlikely to have the two biggest market declines since 1929 all over again), let me acknowledge that placing 60% and 70% of one's portfolio in bonds may be a way of managing sequence-of-return risk, but so is shooting oneself in the *head. Both are fatal; one is just more sudden.*

There are any number of ways to manage sequence-of-return risk while maintaining a preponderantly equity portfolio. One is to start with two years' living expenses in a cash equivalent, so that if the market goes south early you can moderate or stop altogether your withdrawal plan and live off the side fund. Another is to work part time and/or a couple of years longer. Another is to start a planned 4.5% withdrawal program as 2% the first year, 3 the next, 4 and then 4.5. Moreover, all these tactics can and in many cases should be combined. Finally, there are the so-called "living benefit" riders of variable annuities, which may very well have a place for some portion of the portfolio.

Chuck Yeager termed ejecting from a supersonic aircraft "committing suicide to keep from getting killed." That applies equally well, it seems to me, to trying to fight off three decades of rising living costs with a 60%–70% fixed-income portfolio.

Q. You are known for having a low opinion of bonds. Given their yields, your opinion isn't the only thing about bonds that is low. But the vast majority of retirees need both an element of risk control and a source of income in their portfolios. A look at the options—high-yield bonds, real estate, high-yield munis, dividend paying stocks, MLPs, annuities and other instruments—reveals that each vehicle has its own set of issues and each has also been influenced by global monetary policy. How do you evaluate the choices embedded in this conundrum?

A. What conundrum? Nothing has provided greater risk control over the long term than equities, which are historically without principal risk over 30-year periods (unless you're mistaking volatility for loss, in which case you're already doomed). And there has never been a source of increasing income as powerful or reliable as the constantly rising dividends of the Great Companies in America and the world.

Today's retirees will average age 62, which means they were born in 1953. If they were born in February 1953, the S&P Index was at 26, and the dividend at $1.40. The relevant numbers as I write are 2,000 and $39. Again, as long as you don't mistake temporary decline (volatility) for risk/loss ... what conundrum?

Q. Debt, the demographics of aging, and large budget deficits are global problems. The IMF and the World Bank say the U.S. economy is one of the few bright spots in the world but most Americans think our economy is mediocre at best. Should we accept this as the New Normal?

A. No. We should enact pro-growth fiscal policies, including but not limited to tax reform and entitlement reform, to begin with. When, as and if we get our fiscal situation rationalized, our economy can and will grow at superior rates.

Q. In the past, you have argued that optimism is the only rational outlook for the future. That flies in the face of the current mood in America and elsewhere. Do you still believe that and why?

A. That optimism flies in the face of "the current mood" is almost reason enough to embrace it, all by itself. But I carry in my back pocket more computing power than existed on Earth when I started kindergarten in 1949, and a million times more than E. F. Hutton had when I joined that firm in 1967. I have been almost effortlessly cured half a dozen times in my life of illnesses which, had I been born 50 years earlier, would have killed me. Both these staggering improvements in the quality of life are compounding exponentially, as indeed is all information technology—and all technology is information technology.

As the developing world continues to adopt free market principles, it continues to pull tens of millions of people a year out of poverty—first to become producers and then consumers. America remains the most entrepreneurial, flexible, transparent economy in the world. We virtually own science. Nearly all (if not all) of the revolutionary global companies started since the advent of the microprocessor are ours; this country throbs with opportunity for the path-breaking technologist.

We're one of the richest countries in mineral resources, and the only one which vests the mineral rights in the landowner—just when we've perfected the synthesis of horizontal drilling and hydraulic fracturing. We may very soon be an exporter of hydrocarbons—a major boon to Americans and a source of strength for the dollar. Cheap natural gas is bringing manufacturing back home. I can go on and on like this. I've never been more optimistic in my life than I am today.

Q. If an advisor wanted to focus his or her practice on just one idea for the foreseeable future, what would it be?

A. That when an American (or an American couple) steps across the threshold of retirement, they find themselves facing two doors. Door Number One says, "The money outlives the people." And Door Number Two says, "The people outlive the money." And the newly minted retirees must pass through one door or the other. It's as stark and as simple as that. Forget debt, the demographics of aging, unfunded entitlements, global monetary policy, and all those other amorphous imponderables we can't predict, much less control. Focus on what we may be able to control, if and only if the client will let us: whether the money outlives the folks, or they outlive their money. There is treasure on Earth and in heaven for those advisors who make it their mission to help people plan their way through Door Number One.
