The Financial Navigator – April Newsletter

It is that time of year again, parents and their children are reviewing their college options and the various financial aid packages, along with their potential majors. The article below – *Return On College* might add some perspective if you are, or will be, considering the various options now or a few years in the future. The second article, *Will Social Security Be There When I Retire?,* may be timely as the presidential election season has kicked off, and inevitably the candidates will debate how to save Social Security, and then after the election the topic will be quickly forgotten. The final article, *Is America In Economic Decline*, provides a counter argument to some of the conventional wisdom that the US is becoming less relevant economically.

Sincerely,

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Return On College

What are those diplomas really worth?

Let's say you're giving your daughter, niece or grandson some advice on which major to select in college. Do you tell them to get an art degree, or take courses in social sciences? Or should they focus on business and finance?

The decision should not ignore their natural abilities and interests, of course. But if they're looking for the best return on their tuition dollar, then they might consider spending their time in the computer sciences and math buildings.

This information comes from a report published by PayScale.com, which helps people manage their careers and figure out what they're worth on the job market. PayScale's research team tracked the median salary for people who completed its salary survey online. They then compared the 20-year earnings of people following different careers with what was earned, on average, by competing workers with a high school diploma but no college degree. Then they subtracted the cost of 4 years of college tuition, to arrive at a return on investment figure—the additional money the degree provided. Advanced degrees like law and medicine were excluded; the survey focused on bachelor's degrees.

The results were striking. Business and finance majors came away with a respectable $331,345 average ROI over 20 years, but they actually finished a distant third on the list,

just ahead of sales, marketing and public relations ($318,212). The highest ranking majors, by this metric, were computer and math, whose degree-holders saw a net return on their tuition investment of $584,339 over the 20 years after graduation. These nerdy individuals nosed out the architecture and engineering graduates, whose average ROI came to $561,475.

Life, physical and social sciences majors fared somewhat less well, earning almost exactly $250,000 more than their high school diploma competition. Graduates with an arts, design, entertainment and related degree came in last in the survey; they are expected to make a little over $125,000 as a result of their college training.

Interestingly, the PayScale website also tracks the average return on tuition investment for different colleges. Graduates of Harvey Mudd College in Claremont, CA can expect to earn nearly $1 million over the 20 years after graduation, with a typical starting salary north of $75,000—with a 4-year college investment of $237,700. Numbers 2-10 on the rankings include the California Institute of Technology ($901,400 earnings, $221,600 cost); The Stevens Institute of Technology in Hoboken, NJ ($841,000; $232,000), the Colorado School of Mines in Golden, CO ($831,000; $112,000); Babson College in Wellesley, MA ($812,800; $230,200); Stanford University ($809,000; $233,300); the Massachusetts Institute of Technology ($798,500; $224,500); Georgia Institute of Technology ($796,300; $86,700); Princeton University ($795,700; $217,300); and the Virginia Military Institute ($767,300; $95,700).

You can look up your own alma mater here: http://www.payscale.com/college-roi/

Will Social Security Be There When I Retire?

Here's an antidote to the prevailing pessimistic view.

Social Security's future solvency has become one of the most commonly-discussed issues in retirement planning—and for good reason. Gallup polls show that an estimated 57% of retirees rely on Social Security as a major source of retirement income—a number that has held steady since the early 2000s. But when Generation X and Y individuals plan for their future retirement, they'll often ask their advisor to assume that Social Security won't be there for them 20 or 30 years down the road.

However, if you look closely at the numbers, you see a very different story. Up until 2011, the Social Security system actually collected more revenues from workers' FICA payments than it paid out—and that has been generally true since the 1940s. Most of the Social Security benefits that people receive today are simply a transfer; that is, the money is collected from worker paychecks (and, of course, employer matches), spends a few days at the U.S. Treasury and then is paid out to recipients. The surplus has been

used to pay government operating expenses, and for seven decades, the government issued “special issue federal securities” (essentially fancy IOUs that pay interest) to the Social Security trust fund.

In 2011, the program crossed that threshold where benefit payments slightly exceeded the amount collected. Why? Because the number of beneficiaries, compared to the number of workers, has steadily increased. In 1955, there were more than eight workers paying into Social Security for every beneficiary. Today, that number is closer to three workers for every beneficiary, and by 2031, if current estimates are correct, that ratio will fall to just over two workers supporting every retired beneficiary.

When Social Security Administration actuaries crunch the numbers, they have to take into account the shifting demographics, and then make estimates of fertility and immigration rates, longevity, labor force participation rates, the growth of real wages and growth of the economy every year between now and 2078. After adding in the value of the government IOUs, they estimate that if nothing is done to fix the system, the trust fund IOUs will run out in the year 2033. At that time, only the FICA money collected from workers would be available to pay Social Security beneficiaries. In real terms, that means the beneficiaries would, in 2034, see their payments drop to 77% of what they were promised.

In other words, the money being transferred from current workers to beneficiaries through the FICA payroll program, assuming no course corrections between now and 2033, will be enough to pay retirees 77% of the benefits they were otherwise expecting. The government actuaries say that if nothing is done to fix the problem over the next 63 years, this percentage will gradually decline to 72% by the year 2078.

So the first takeaway from these analyses is that today’s workers are looking at a worst-case scenario of only receiving about 75% of the benefits that they would otherwise have expected to receive. This is far different from the zero figure that they’re asking their advisors to use in retirement projections.

How likely is it that there will be no course corrections? There are two possible ways that this 75% figure could go up. One lies in the assumptions themselves. The Social Security Administration actuaries have tended to err on the side of conservatism, presumably because they would rather be pleasantly surprised than discover that they were too optimistic. But what if the future doesn’t look as gloomy as their assumptions make it out to be?

To take just one of the variables, the actuaries are projecting that labor force participation rates for men will fall from 75.5% of the population in 1997 to 74% by 2075, while the growth in female workers will stop their long climb and peter out

around 60%. If male labor force participation rates don't fall, and if female rates continue to rise, some of the funding gap will be eliminated.

Similarly, the projections assume the U.S. economy's productivity gains (which drive wage increases) will grow 1.3% a year, well below long-term U.S. averages and certainly below the assumptions of economists who believe that biotech and information age revolutions will spur unprecedented growth. If real wages were to grow at something closer to the post-Great Recession rate of 2% a year, then more than half of the funding gap would be eliminated. If the current slump in immigration (due to tighter immigration policies) is reversed, and the economy grows faster than the anemic 2% rates the Social Security Administration is projecting (compared to 2.5% recently), then the "bankrupt" system begins to look surprisingly solvent.

A second possibility is that Congress will tweak the numbers and bring Social Security's long-term finances back in balance, as it has done 21 times since the program originated in 1937. The financial press often cites the fact that the total future Social Security funding shortfall amounts to $13.6 trillion, but they seldom add that this represents just 3.5% of future taxable payrolls through 2081. Small tweaks—like extending the age to collect full retirement benefits from 67 to 68, raising the FICA tax rate by 3.5 percentage points or making the current 12.4% rate (employee plus employer match) apply to all taxable income rather than the $118,500 current limit—would restore solvency far enough into the future that today's workers would be comfortable adding back 100% of their anticipated benefits into their retirement projections.

How likely is it that Congress will take these measures, in light of recent partisan budget battles? It's helpful to remember that older Americans tend to vote with more consistency than younger citizens. The more you've paid into the system, the more you expect to at least get back the money you were promised.

The bottom line here is that if you're skeptical about Social Security's future solvency, then you should pencil in 75% of the benefits you would otherwise expect—rather than $0. Meanwhile, as you approach the age when you're eligible for benefits, watch for signs that immigration restrictions are loosening, the economy is growing faster than the SSA actuaries' gloomy projections, more people are working during traditional retirement years or yet another round of tweaks from our elected representatives.

Is America In Economic Decline?

It depends on how you measure it. In 1945, the U.S. made up more than half of the world's total gross domestic product (GDP), which basically means that half the world's economy took place inside U.S. borders. Today that figure is just under 22%.

There seems to be a bull market in doomsayers these past few years, as we're all reading arguments that the U.S. is slowly losing its grip on global preeminence. The rhetoric today sounds a lot like the hand-wringing back in the 1980s when Japan was allegedly taking over the global economy, and before that, when the Soviet Union had more missiles and a Sputnik circling over our heads.

There's no easy way to define the overall quality of an economy, but probably the most thorough assessment comes out each year via the World Economic Forum's Global Competitiveness Rankings. The most recent report ranked 144 countries around the world, including Qatar (16), Moldavia (82), Namibia (88), Lesotho (107) and the unhappy states of Chad (143) and Guinea (144), whose citizens eke out their lives on per capita incomes of $1,218 and $564 a year, respectively.

The survey looks at 12 "pillars" of economic competitiveness, including labor market efficiency, the quality of primary education and higher education, infrastructure, the strength of institutions, innovation, business sophistication, technological readiness and the sophistication of the financial markets. Each of these categories are broken down into dozens of subcategories, which are separately evaluated. For instance, when looking at the strength of each country's public institutions, the World Economic Forum researchers consider whether people in a given country have strong property rights and intellectual property protection, whether there is corruption and the routine payment of bribes, whether the citizens enjoy judicial independence and a solid legal framework, and how well investors enjoy shareholder protection.

In the most recent survey, the U.S. ranked third overall, with an overall rating of 5.5 on a scale of 1-6. Ahead of it were Switzerland (5.7) and Singapore (5.6). China, the country that you most often hear cited as the all-powerful up-and-coming economy, ranked 28th, two rungs below Saudi Arabia, one rung above Estonia. Brazil and India, which are sometimes mentioned as powerful competitors to U.S. economic hegemony, are ranked 57th and 71st, respectively.

The point of the rankings is to show which countries have created the healthiest (or, in the cases of Chad and Guinea, the least-healthy) economic climate for future growth. But of course there are other ways of measuring competitiveness, including the bottom line (as mentioned at the top of the article) of percentage of the world GDP, and whether you're moving up or down.

By that standard, the U.S. is indeed moving down. If you consider the size of the overall global and U.S. economies since 1991, you will find that the U.S. has enjoyed steady economic growth, while the world at large has essentially taken off like a rocket. The

years following the collapse of the Soviet Union, when several billion people were suddenly allowed to become capitalists, have been good for world growth. When China shifted from a communist to a capitalist economic posture, this added fuel to the rocket. The democratization of computer technology and the global Internet has empowered value creators everywhere.

The U.S., Europe and Japan, in other words, no longer have a monopoly on capitalism. And that's a good thing.

Is there a better way of evaluating how the U.S. economy is holding up in an increasingly competitive world? Since 1991, what percentage of all the world's business has been happening in the U.S., vs. Europe, Japan, China, India, Russia and Brazil? How much of the total global economy did each nation claim in each year, and how has that balance changed over time?

What you find is that the U.S. is still in the lead by a pretty wide margin, and in recent years has actually stabilized its percentage of total global GDP. The decline has come mostly because a lot of smaller emerging markets, plus China and, to a certain extent, Brazil, India and Russia, have all been growing. At the same time, America's traditional competitors—Europe and Japan—have been sinking. If you want to point a finger at decline, perhaps that's a better direction than the U.S.

Does the U.S. face economic challenges? Of course. Is our political system a mess? Sure. Could things be better? Certainly. But if you sift through a lot of variables with a fine-toothed comb, you discover that the U.S. has created a better environment to grow and prosper than almost anywhere else, and it has held its own with the roaring growth of the emerging markets while the other developed nations are losing ground. More than a fifth of all economic activity still happens in the U.S., and the long, slow decline in that figure is not due to stagnation at home, but abundant growth all around the world. That's not something to worry about; it's something we should be celebrating.