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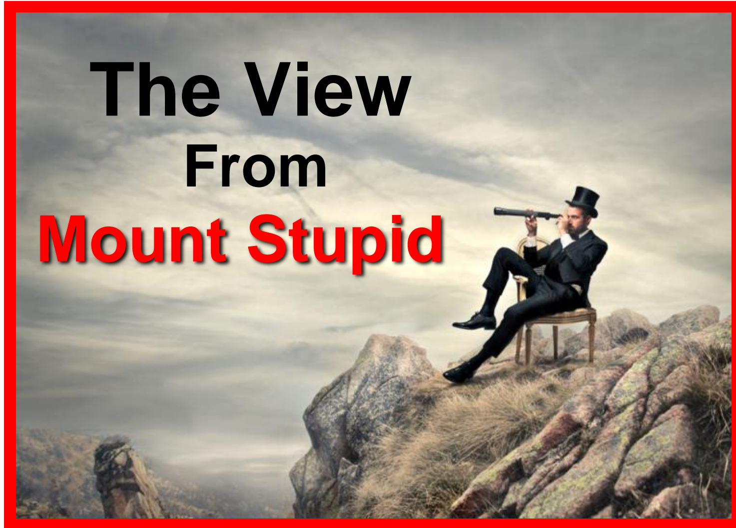


**You may have heard: We are in the midst of a pandemic.** The novel coronavirus is a world-wide health event, one that portends dramatic far-reaching changes to life as we know it. But what kind of changes? Everyone wants some guidance on what our "new normal" will look like.

As of August 2020, these were some trending sentiments about post-pandemic life in the United States:

**The economy will be different.** In an instant, the mandate for social distancing shuttered or dramatically altered the service industry, which some experts estimate accounts for 60 percent of the economic activity in the United States[1]. In the aftermath, many service-oriented businesses will take years to return to pre-pandemic levels of revenue and profitability. Alternatively, they will go out of business. Long-term, this projects to higher unemployment, slower growth.

**Work will be different.** Remote work is no longer an experiment. For a larger segment of the workforce, it's the default arrangement of the future. When remote work is commonplace, employers have a greater pool of potential hires because geography is no longer a limitation. Combined with rising unemployment, this makes job-seeking more competitive; more eligible applicants are chasing fewer available positions.

**Education will be different.** Remote work may be a new normal, but remote learning? Not so much, at least for elementary and secondary education. Instead, the buzz is about "coronavirus school pods" and "micro schools" where a few families combine resources and schedules "to share the teaching load and let their children interact with others." An Ivy League professor gushed that this "will be completely transformational…it's going to happen everywhere."

**Saving will be different – primarily for those who were saving already.** If you've been fortunate enough to maintain your income during the pandemic, what do you do when options for spending money are limited by shelter-in-place orders, social distancing constraints and travel restrictions? Order a pizza with contactless delivery and save money.

Harvard researchers who track spending patterns found that the biggest decline in discretionary spending has occurred in higher-income households; given the uncertainties and dearth of options for travel, entertainment and leisure, wealthy Americans are electing to save. Consumer spending is a huge driver of economic activity and some economists have speculated that this turn to saving will further "tank the economy," according to a June 2020 NPR report. [2]

**Eating will be different.** The demand for eggs in the United States is up 60 percent compared to last year. Everyone is baking bread. Hershey's predicts less chocolate will be consumed at Halloween. And the majority of meals will be eaten in homes; dining out will become a rarity.

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## Are These Markers for a New Normal?

Who knows? Some of these conclusions seem plausible. But before you start making plans, consider the Dunning-Kruger Effect and how it might relate to post-pandemic predictions.

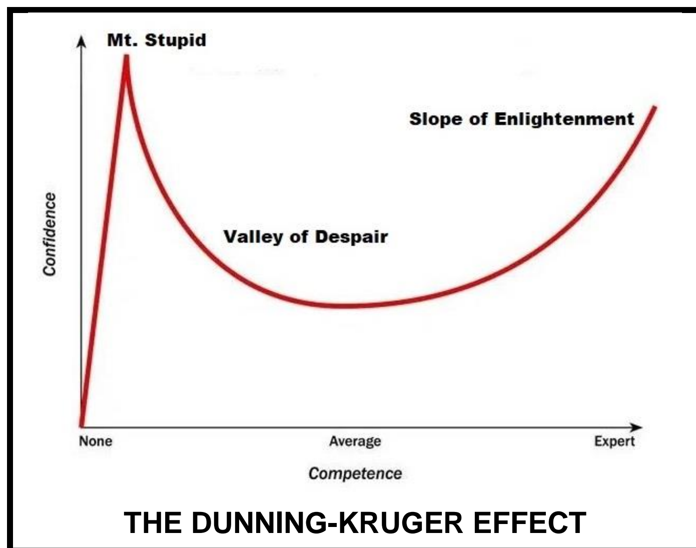
## The Dunning-Kruger Effect

The **Dunning–Kruger effect,** named after social psychologists David Dunning and Justin Kruger, is a cognitive bias in which people with limited knowledge or ability overestimate their competence in understanding or executing a particular issue.

When we have no exposure or experience with an issue, we have neither competence or confidence; we are ignorant, and we know we are ignorant. But as we learn about the subject or get some experience, our confidence grows substantially. Grasping the basics of a new topic or skill, we may quickly come to see ourselves as competent, despite our limited experience. This early period of excess confidence is often referred to as "Mount Stupid."

Eventually, people who are truly interested in understanding an issue or acquiring a skill recognize its nuances and complexities. At this point, confidence dips sharply, even as competence increases. This stage has been dubbed the Valley of Despair – ***"I didn't know it would be this hard!"***

For those willing to persevere through the Valley of Despair, confidence and competence will increase in tandem, bringing us to the Slope of Enlightenment, a place of mastery.




THE DUNNING-KRUGER EFFECT

## Right Now, We're All on Mount Stupid

Because of its ubiquitous presence, all of us have gone from knowing nothing about the coronavirus to discussing it every day. But even as it has become a dominant issue in our lives, no one has enough information and/or experience to competently predict the future impact of the pandemic. Right now, we are all on Mount Stupid when it comes to Covid-19.

This is not to say we are stupid, but rather that all of us – epidemiologists, politicians, citizens – are in the first stages of learning about the virus and how to respond to it.

Which makes long-term decisions based on Mount Stupid perspectives problematic. Despite the confidence of our convictions, and the calls to "do something," our competence may not be equal to the task. Consider how many strong, yet conflicting, assertions we have heard in the past six months about the virus, the economy, and the social challenges.

The 20th-century philosopher Bertrand Russell was not a contemporary of Dunning and Krueger, but he aptly described the dangers of Mount Stupid thinking:

> ***"The whole problem with the world is that fools and fanatics are always so certain of themselves, and wiser people so full of doubts."***

Instead of reacting to every well-intended but ill-advised declaration from Mount Stupid, maybe we should wait to hear from the wiser ones, who are working through the Valley of Despair.

## Waiting Through the Valley of Despair

John Mauldin is a financial commentator, author and investment advisor who regularly appears on the business news networks. Over the past three decades, Mauldin has made a few economic predictions that have been off-target, particularly in regard to their timing. Older and wiser, he tends to avoid Mount Stupid proclamations, often describing himself as a "muddle-through analyst," one who keeps moving forward through his own ignorance. In a July 2020 commentary, he offered these comments about the pandemic:

**"Understand, the world is not coming to an end. We are just repricing everything and trying to figure out how we move forward."**

With so many unknowns, Mauldin adds: "I am not merely coming up with a plan B. Given the uncertainty in the world, I am having to do my own personal wargame of plan C, D, and so on. I want to take advantage of the opportunities, just like you should, but we also all need to recognize that our worlds are going to change and be prepared to change with them."

Sounds like someone who is muddling through the Valley of Despair. The only specific financial recommendation: Be prepared to change.

And this recommendation is not based on an opinion about the future, but about how unprepared many Americans were for the past six months. An unimaginable event happened, and it has shown us that our lives, our livelihoods and our plans for the future are more fragile than we previously imagined. ❖

**The world is just entering the "Valley of Despair" about Covid-19, which might be an ideal time to refocus on financial confidence as a first step in preparing your plans "B, C, D and so on" for the future.**

**You don't have to guess about tomorrow to make adjustments. You can look at how your finances have withstood the past six months and know that, regardless of what may come, you have the best chance of reacting with confidence and competence when you maximize your financial stability.**

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# Non-Guaranteed Assets: In

*"In theory, theory and practice are the same. In practice, they are not."*

This quote, or a variation of it, has been attributed to both Albert Einstein and Yogi Berra, two people perceived to be on the opposite ends of the intellectual spectrum. Which, in a way, validates its accuracy. In almost every aspect of life, there is a gap between what is possible and what actually happens. This is true with retirement strategies, especially with non-guaranteed assets; what is theoretically possible is rarely achieved in real life.

## The Rise of Non-Guaranteed Assets for Retirement

Non-guaranteed assets are investments whose values are determined by the opinions of buyers and sellers in the marketplace. These values are not fixed or guaranteed to increase over time; owners of non-guaranteed assets accept that these assets will fluctuate and may lose money.

Historically, non-guaranteed assets have frequently yielded higher returns compared to guaranteed assets. The prevalence of defined contribution retirement plans (e.g., 401(k)s) and the subsequent shift to individual responsibility for both retirement funding and income are strong incentives for individuals to pursue higher returns. These factors have led to the widespread use of non-guaranteed assets in retirement strategies, based on the following assumptions:

### 1. For Accumulation:

- ***If you are willing to accept some risk of loss, it is theoretically possible to accumulate more money than can be earned by simply depositing funds in a guaranteed account.***

### 2. For Decumulation:

- ***If you are willing to accept some risk of loss, it is theoretically possible to determine a withdrawal rate at the beginning of retirement which will provide a stable annual income for as long as retirement lasts.***

But, as Albert and Yogi both knew, there are big differences between theory and practice.

## Emotions Get in the Way

With accumulation, the gap between theory and practice often occurs because individuals cannot stay invested in non-guaranteed assets long enough to maximize the probability of higher returns; emergencies and emotional responses to fluctuations prompt them to buy and sell at inopportune times. Statistical studies repeatedly show significant negative differences between the reported returns from a particular investment and the actual returns achieved by individual investors.[3]

This "practice" flaw in accumulation is primarily seen as a behavior modification challenge. Through education, experience and self-awareness, individuals can avoid self-sabotage and allow their real returns to approach the theoretical ones.

## Too Many Variables Changing Too Often

For decumulation, the difference between theory and practice isn't a matter of user error. It's that the variables used in calculating a withdrawal rate are susceptible to frequent change during retirement.

In a May 2020 commentary, retirement researchers Michael Finke and David Blanchett pointed to two Monte Carlo simulations made three weeks apart, between late February and early March 2020, to illustrate this variance.[4] (Monte Carlo simulations analyze volumes of historical data to determine the likelihood of a specific outcome.)

A February 20, 2020, simulation determined an annual withdrawal rate of 3 percent had a 94 percent chance of success. For an individual with $1 million accumulated for retirement this means, "You would have had a 94% chance that you could maintain $30,000 plus inflation each year in retirement," says Finke.

But that was before the pandemic arrived. On March 12, the same Monte Carlo simulation had only a 64 percent chance of success.

Finke and Blanchette say this variance during a three-week interval shows "the traditional methodology for retirement withdrawals from a risky portfolio to fund a safe and stable income is not 'exactly realistic.'" There are too many interdependent factors that vary frequently. "Those events will change your reality every year, and you have to adapt."

In practice, retirement income from non-guaranteed assets cannot be stable or guaranteed, even if a theoretical model suggests otherwise. Retirees using non-guaranteed assets to provide income should expect fluctuations, including the necessity of decreasing income should these assets underperform.

## Practical Options

The reality of retirement is that most retirees need income certainty because many of their monthly obligations, like housing, transportation, and insurance are fixed costs. If non-guaranteed assets cannot consistently deliver steady income, what are the alternatives?

The obvious answer: include guaranteed assets in your retirement strategies, particularly for decumulation. Combined strategically with non-guaranteed assets, it is possible to dampen fluctuations in values and stabilize income.

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An example: One of the problematic retirement variables when using non-guaranteed assets is determining life expectancy and how long income will be needed. As an individual, you need to plan not only for your average life expectancy but the possibility that you might live well beyond it.

Buying a guaranteed lifetime income product (i.e., an annuity*) can eliminate this uncertainty. By pooling your assets and lifespan with thousands of other annuitants, this guarantee often costs less than trying to self-insure using non-guaranteed assets that theoretically produce higher returns.

### Real Results > Theoretical Possibilities

Theoretical possibilities can be seductive; it's the possibility of getting the most from what you have. But there's always a difference between theory and practice. Especially when you're talking about money, reality often underperforms possibilities. ❖

To improve your real results, ask a financial professional about practical ways to integrate guaranteed assets in your financial program.

*Annuity contract guarantees are guaranteed solely by the strength and claims-paying ability of the issuing company.

## Has the Pandemic Locked You Out of a HELOC?

Unlike any other event in recent memory, the pandemic has reinforced the essential value of cash reserves in a financial crisis. For some, it revealed their emergency savings accounts were woefully underfunded. For others, maybe it was the realization that some assets thought to be available in an emergency were not under their control; they needed permission to tap these sources, and permission was denied.

### HELOCs

A relevant example of financial permission pertains to Home Equity Lines of Credit (HELOCs). A HELOC is an open line of credit with a home as collateral. Similar to a credit card, borrowers may draw against this account up to a preset limit, typically a percentage of the homeowner's equity in the property.

As an emergency resource, HELOCs can be attractive because the cost of borrowing is often lower than unsecured credit cards, and monthly repayment obligations can be minimal (often just the interest charged on the outstanding balance).

For homeowners with substantial equity, a HELOC can be an emergency alternative to keeping larger amounts of cash in low-yield accounts. But having a HELOC requires the approval of a lender. And per a June 18, 2020, *Wall Street Journal* article, while the pandemic has put millions of Americans out of work, "for many, tapping their home equity isn't an option."

This is because lenders are acutely aware of their default risks with HELOCs during an economic downturn. While almost 50 percent fewer consumers had an open HELOC in 2020 compared to three years earlier, balances jumped almost as soon as the coronavirus hit the United States in March. "Every indication pointed to people tapping into home equity lines," a banker told the *WSJ*.[5]

Having been burned in the 2009 recession by falling real estate values and defaults, many lenders either tightened their standards for offering HELOCs or simply stopped taking applications at the pandemic's onset. Consequently, "out-of-work borrowers and others who could benefit from HELOCs might be locked out by lofty lending requirements." [5]

### The Right Move for Wealthier Households?

It is interesting to note that HELOCs are much more prevalent among wealthier households. A recent New York Federal Reserve study found that almost 1 in 10 homeowners in the highest-income zip codes had tappable lines of home equity, a rate three times the national average. [5] Which sort of makes sense: higher-income households probably have more equity and other assets; even in tough times, they are better equipped to make timely payments.

There's an old saying about borrowing that the best time to ask for money is when you don't need it. The wisdom of this statement is debatable but securing the option to draw on your home's equity in the future might be a prudent move. A HELOC could be a financial backstop; it may be better to have it now than risk being denied when you really need it.

### Some Cautions

- Unlike home equity loans or cash-out refinancing, HELOCs are usually listed as revolving credit like a credit card, not a second mortgage. As an additional line of credit, a HELOC could potentially reduce your credit score.
- While having a secured loan might mean a lower interest rate, you're taking on additional risk because the security is the home. If you default on HELOC debt, you risk foreclosure.
- Where home equity loans offer a fixed interest rate, HELOCs have variable rates, usually tied to decisions of the Federal Reserve. This can change the minimum payment and/or make repayment longer. In some cases, taking a second mortgage or refinancing your existing mortgage to turn a chunk of home equity into cash might be a better option because these loans will have a fixed interest cost and specific payoff date.

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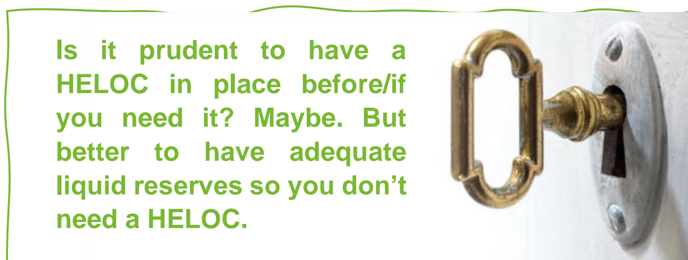
- Your line of credit is tied to the property's value. Some lenders have been reducing the HELOC limits in anticipation of a decline in housing values as a result of the pandemic; your borrowing limit may be lower than you think.

### Could You, Should You Have a HELOC?

That's a great question for your financial professionals. As a pseudo-credit card that's only used for emergencies, a HELOC might be a financial resource. As a way to consolidate other high-interest debt, you might realize interest savings and improved cash flow, but connecting the debt to a property also increases the chance of foreclosure if you default.

While a home equity line of credit can be a supplemental source of emergency cash, there is simply no substitute for cash reserves. The title of the *WSJ* article referenced above highlights this truth: "The Economy Is in Disarray. But Borrowers Aren't Getting Home-Equity Lines." The reason borrowers are seeking home-equity lines? Because they need cash. Why? Because their personal economies are in disarray. ❖




Guardian and its subsidiaries do not issue or advise with regard to mortgages or home equity lines of credit.

Dan Buettner is an explorer, educator, author, and public speaker known for his "Blue Zone" works on longevity and happiness, beginning with his 2008 book, *"Blue Zones: Lessons for Living Longer From the People Who've Lived the Longest."*

Buettner's research focused on the common activities and diets found in what he called "Blue Zone" communities, places where the population included an unusually large number of centenarians and the general population reported a high level of happiness and personal satisfaction. These common factors were not ground-breaking discoveries; Buettner describes them as "simply a balance of good health habits and social engagement." Such as:

- A motivating purpose for living
- Regular but sub-maximal physical activity
- Moderate calorie intake, primarily from plants
- Modest alcohol intake (preferably wine, and consumed among friends)
- Engagement in spirituality or religion
- Strong family ties
- Participation in a local community.

In subsequent work, Buettner refined his Blue Zone theories, moving from recommendations for personal change to creating better environments for happiness. In a December 2019 interview published on insider.com[6], Buettner explained this subtle shift in perspective. "If you want to live longer and be healthier, don't try to change your behaviors, because that never lasts for the long run," he said. "Think about changing your environment."

Buettner gives several examples, both large and small, of how changing your environment can increase happiness.

- **Work with people you like.** "The biggest determinant of whether or not you'll like your job is if you have a best friend there, more so than how much you're paid."
- **Find someone to marry, make friends.** "You're three times more likely to be happy if you are married, and each new friend will boost your happiness about 10 percent."
- **Live near water.** Whether it's a lake or river or an ocean, people living near water are about 10 percent more likely to be happy than people who don't.
- **Have a sidewalk and place to ride your bike.** People whose house has a sidewalk are more likely to be happy, as are those who live in bicycle-friendly communities.

### The Blue Zone for Financial Happiness

Buettner also has a unique prescription for financial happiness: Make financial confidence a priority.

Financial confidence isn't about earning more money or acquiring more assets. It's about knowing that what you have is adequate, stable and protected.

"We know that financial security has a three-times greater impact on our happiness than just income alone," Buettner told NPR.[7] "Setting up an automatic saving plan and buying insurance is more satisfying than buying a new thing. The newness effect of a new thing wears off in nine months to a year, but financial security can last a lifetime."

### Who's Your Blue Zone Financial Professional?

"Financial professional" is a catch-all phrase for CPAs, attorneys, investment advisors, insurance agents, brokers, bankers, etc., people licensed to provide assistance and expertise

regarding financial matters. Need help with your tax returns? Consult a tax professional. Updating your will? See a legal professional. Looking to balance your portfolio? Review with an investment professional. So, who do you look to for financial confidence?

Until the start of the 21st century, many of the elements of financial confidence were taken care of by either the government or an employer. With Social Security, worker's compensation, pensions and group benefits, many American workers could take a hands-off approach to financial confidence. But today, a much larger percentage of responsibility has been shifted to the individual.

In 2019, two professional associations with long histories, the American Association of Life Underwriters (AALU) and the General Agents Managers Association (GAMA) announced a pending merger to "unify the entire financial security profession," i.e., those professionals, who "regardless of role, marketplace, or experience"[8] are focused on helping individuals and businesses achieve financial confidence through insurance, guaranteed financial instruments and legal arrangements.

Because individual financial services went mainstream in an era where many aspects of financial confidence were already addressed, a strong institutional emphasis has been to help clients

consumers and financial professionals are prioritizing the benefits of financial confidence over opportunities for more money. They want Blue Zone financial happiness. Do you have a financial professional whose focus is to help you live "in the zone?" ❖

Footnotes:

1 "The American Economy is Experiencing a Paradigm Shift," *The Atlantic*, November, 2018. Also, "Distribution of gross domestic product (GDP) across economic sectors in the U.S. 2017," Published by Erin Duffin, Feb 14, 2020, statista.com.

2 "The Rich Have Stopped Spending And That Has Tanked The Economy," June 17, 2020, npr.org

3 "Why Average Investors Earn Below Average Market Returns," by Dana Anspach, January 28, 2019, the balance.com.

4 "Finke, Blanchett on 4% Rule: Retirement Success Is Flexibility, Not Fixation," by Jeff Berman, May 29, 2020, ThinkAdvisor.com.

5 "The Economy is in Disarray. But Borrowers Aren't Getting Home-Equity Lines," by Orla McCaffrey, *Wall Street Journal*, June 18, 2020.

6 https://www.insider.com/blue-zones-dan-buettner-long-life-diet-exercise-2019-12

7 https://www.npr.org/transcripts/131571885

8 insurancenewsnet.com, July 29, 2019 (https://insurancenewsnet.com/innarticle/aalu-and-gama-international-to-merge-by-june-2020#)

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