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# Japan’s Two Lost Decades: Can It Happen In The U.S.?

Twenty years after Japan’s “economic miracle” collapsed, the Asian nation still has not recovered its once-vaunted economic clout. Japan’s debacle involved a spectacular jump in stock and real estate prices followed by an equally spectacular fall as those bubbles burst, much like the twin “pop” that sent the United States into a recessionary spiral in December 2007.

Does that mean Americans are doomed to spend the next two decades struggling to get their economic lives back? And what lessons can investors learn from the Japanese experience?

**Echoes of a debacle in Japan.** The start of Japan’s so-called “lost decade” in 1990—which has stretched to two decades since that phrase was coined to describe Japan’s extended economic malaise—was triggered by a period of irrational exuberance in the 1980s. Loose monetary policy fueled a rapid rise in stock and real estate prices. Driven by speculation, leveraged assets, and investing excess, Japanese industrial production rose by 50% during the 1980s, and by 1989 Japanese banks had become the largest in the world. When the bubble burst in 1990 and the economy collapsed, investors belatedly realized that much of the growth had been illusory.

The same thing happened in the United States during the period 2002 to 2007, as “easy money” policies, consumer spending, and foreign investment pushed real estate and stock prices ever upward—until the bubble burst, sending over-leveraged financial institutions to the brink of bankruptcy and the U.S. economy to the edge of systemic failure. Two years later, the U.S. jobless rate surpassed 10%, businesses have trouble obtaining credit, and government officials are weighing further intervention in the economy even as the national deficit soars to unprecedented levels.

From an investor’s point of view, the story is illustrated vividly by looking at the most-quoted stock market averages in the two countries. Japan’s Nikkei average hit an all-time high of 38,957.44 intraday Dec. 29, 1989, then fell off a cliff. In 2009, the Nikkei never exceeded 10,800, and it nearly fell below 7,000 in March. In the United States, the Dow Jones Industrial average soared to a record intraday high of 14,198.10 on Oct. 11, 2007, then plunged as the economy deteriorated, dropping as low as 6,547.05 in March 2009 before rallying back above 10,000 in the last few months of the year.

**Why the U.S. should fare better.** While the similarities between the countries’ boom-and-bust debacles are striking, there are also fundamental differences. For instance, the U.S. crisis is unlikely to be as deep and long-lasting as the Japanese downturn largely because the U.S. boom period did not even approach the stupendous

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## *Deleveraging: We'll Be Hearing A Lot About It*

It’s a big word that encapsulates the process of paying off debt. By now we all know that consumers, corporations and even the government used debt to grow the economy with money they did not have.

I have been warning about the excessive use of debt for years and many of you have adopted my debt-free lifestyle. Being debt-free has not meant I have been free of concerns, but that portion of my wealth was largely unaffected by the whims of the markets, making it easier to sleep at night.

Now that the economy has been slammed, corporations and consumers are in the process of paying down debt. In the long run this is healthy; however, it does leave less cash in which to propel the economy.

We are in a new environment of very slow growth. We have to invest in a more defensive way and aggressively seek higher yields than those currently available from traditional certificates of deposit and government bonds.

I have guided many of my clients through the difficult waters in the past ten years and have ideas to help you move forward from here.

Give me a call if you would like to review your options.

Ron Dickinson

# The Right Way To Manage Money

In any relationship between financial advisor and client, trust is crucial. But in the post-Bernard Madoff era, it's not enough to sense that an advisor or a financial firm is reliable. Everyone trusted Madoff. His clients recommended him to their friends, who lined up for the privilege of having him manage their money. Yet all of those trusting clients ended up on the losing end of a $50 billion Ponzi scheme, and several other recent frauds have further shaken investor confidence. These days, trust requires proof, delivered regularly. Keeping your investments in the custody of a major financial firm can help provide that proof.

Madoff didn't use an outside custodian. Client funds were reportedly handled by a custodian at a remote storefront office that had few employees and no independent auditor. That left Madoff with unfettered access to clients' money and little or no accountability. It now appears he claimed to have made trades that never occurred and exaggerated returns from other transactions. But without reports or account statements from an independent custodian, there was no way for clients to know there was a problem.

Although Madoff's firm was a registered investment advisor, that kind of set-up is extremely unusual among RIAs, which are regulated by the Securities and Exchange Commission or the individual states. More than nine out of 10 RIAs serving individual clients work with independent custodial firms that have physical possession of client assets, monitor their value, and provide trade confirmations and account statements directly to clients, who can also check on investments by logging in to their account on the custodian's website.

Custodians, such as Fidelity, Schwab Institutional, TD Ameritrade Institutional, Pershing, and others, provide other kinds of security as well. Insurance from the Securities Investor Protection Corporation covers investors for up to $500,000 of losses of securities and $100,000 of losses of cash if a custodian becomes insolvent, and custodial firms often also purchase additional insurance. A common level of supplemental coverage is for up to $5 million of losses of securities. One company provides coverage for losses in securities accounts of up to $149.5 million and up to $900,000 in cash accounts. Moreover, most firms have automated systems to monitor client accounts.

To deter fraudulent activity, the SEC recently proposed a rule change that would require certain RIAs with custody of client assets to use an independent public accountant to conduct surprise audits of client accounts. But you don't have to wait for a new rule to protect your investments. We work with an independent firm that maintains custody of your assets, and you can easily compare the portfolio performance statements we provide with the custodian's account statements. This relationship is just one way we are working to prove that we deserve your trust. ●

# Fighting For Lower Credit Card Rates

For beleaguered credit card users, help has arrived. The Credit CARD Act (officially, the Credit Card Accountability, Responsibility, and Disclosure Act), signed into law in May 2009, is being phased in, and major new rules went into effect in February 2010. Banks and other card issuers must now give you 45 days notice before a change to your card agreement can take effect, they can no longer raise interest rates on existing balances unless you're more than 60 days late with a payment, and they aren't allowed to hike the rate on a new card during the first year.

But these changes come at a tough time for banks. The recession has pushed millions of consumers to the brink of bankruptcy, and credit card losses are soaring. In advance of the new rules, credit card issuers have raised rates, slashed credit limits, and demanded higher minimum payments. To avoid paying punitive fees and rates, consider these tactics.

**Don't be late.** If your payment arrives even a day after it's due, you'll likely be hit with a steep fee and a harsh interest rate increase—in some cases to annual rates exceeding 30%. On a $10,000 balance, that comes to more than $250 a month. The simplest way to avoid being hit with these extra charges is to be vigilant about paying up, perhaps by arranging for automatic payments. And if there's no time to mail a check, pay by phone or online. Even if there's a small fee, you'll come out ahead.

**Read your mail.** Card companies can't make changes without notifying you in writing—but that's what fine print is for. Don't throw away inserts that come with your bill or delete email notifications without reading them. If you don't want to accept a higher interest rate or a lower credit limit, write back to say you're closing the account.

**Ask for a better deal.** Banks have

# Survey: Many Worried About Retirement

It takes a clear plan of action to reach a goal—or so countless self-help books and motivational seminars have told us. Yet when it comes to reaching financial objectives, the message doesn't seem to be getting through.

In the 2009 National Consumer Survey, conducted by the Certified Financial Planner Board of Standards, 1,742 consumers were asked in May and June about their major financial concerns and the steps they've taken to address them. A majority of respondents, about half of whom have more than $1 million in investable assets, said they are worried about managing retirement income, keeping their health care insurance, handling debt, and building a retirement fund. Yet 64% have never had a written financial plan, 11% had one once but not now, and 8% have a plan that needs to be updated. Only 17% have a current, written plan.ï€†Among those who have a financial plan and work with a financial advisor, 65% said they have benefited from the process. Among those with a written plan but no advisor, just under half said the plan has been helpful. "Clearly, consumers who have a financial plan are more confident that their finances are in order and that they can reach their financial goals," says Kevin R. Keller, CEO of the CFP Board.

Those without a written plan cited a number of reasons for not having one:

- 42% said their financial affairs weren't complicated
- 42% said it was too costly to hire a financial planner and develop a plan
- 41% said they do their own informal planning
- 40% said they get along fine without a plan
- 30% said it's hard to know who provides the best planning services
- 24% said they don't really know what is in a financial plan and how it benefits people
- 20% said they couldn't trust the recommendations of financial professionals

The survey notes that 36% of respondents who work with an advisor said they've turned to the advisor more often during the global economic crisis that began in October 2008.

The higher the respondents' income, education level, and asset level, the more likely they are to employ a financial advisor and follow a financial plan, the survey shows. For instance, about one in four with a high school education has a written and updated plan in place, compared with 49% of college graduates. Just 26% of those with household income below $50,000 a year have an updated plan, compared with 53% of those with income exceeding $150,000 a year. In terms of asset levels, a quarter of those with assets of less than $100,000 have an updated plan, compared with 53% of those who have from $100,000 to $1 million in assets, and 67% of those with $1 million or more.

"Americans of every type of background and income level think carefully about their assets and how to improve their financial state," says Eleanor Blayney, a consumer advocate for the CFP Board. "Yet many don't realize that anyone, regardless of wealth or social status, can benefit from having a financial plan."

Among all respondents, 59% listed generating current income as a top financial concern. Other top concerns included:

- Providing health insurance coverage (55%)
- Managing or reducing current debt (53%)
- Building a retirement fund (51%)
- Building an emergency fund (47%)
- Preparing for future family medical needs (42%)
- Managing retirement income (40%)
- Providing life insurance coverage (35%)

These answers varied widely according to respondents' levels of education, income, and assets. For instance, 56% of those with a high school education cited "managing or reducing current debt" as a major concern, compared with 48% of college graduates. That worry was also cited by 58% of those earning $50,000 or less and 41% of those earning $100,000 or more, and by 61% of those with assets of less than $100,000 and 45% of those with assets between $100,000 and $1 million.

Creating and maintaining a financial plan can be an effective way to get and stay on track to reach your life goals. If you don't have a written, updated, and comprehensive plan to guide you to financial success, we can help you in this vital area. ●

the right to raise rates and fees arbitrarily. But you have leverage, too, and simply requesting more favorable terms may pay off. Suppose, for example, you're a long-time customer with a good payment record. If you mislaid a bill or you're having trouble meeting your monthly minimum, a call to customer service to explain your situation could win you a reprieve. Faced with the prospect of a defaulted account, credit card companies fairly routinely cut rates and extend repayment periods for responsible cardholders.

**Try some legal muscle.** Sometimes card issuers are just wrong. They may charge late fees for payments that arrived on time—and then penalize you for exceeding your credit limit. If you dispute a bank action and aren't getting anywhere, ask to speak to a supervisor, threaten to hire an attorney, even consider hiring an attorney to write a strongly worded letter on your behalf. Lawyers' fees aren't cheap, but here, too, a successful resolution could be well worth the cost. ●

# Beware Of Homeowner's Insurance Gaps

Disaster may strike your home when you least expect it. There could be damage from flooding, an earthquake, termites, or even mold—just to name a few possibilities. And though you probably assume repairs will be covered by your homeowner's insurance policy, they may not be. Your policy may exclude more events than you realize. Even when you are covered—for, say, flood damage—there may be "gaps" in your coverage that limit the amount you can recover.

The good news is that a typical homeowner's policy covers losses resulting from fires, tornadoes, and severe storms. But the list of what it normally doesn't cover may surprise you. For instance, coverage may not extend to floods and earthquakes, although you can usually add a policy rider for such events. The rider's cost will vary based on whether you reside in a high-risk area.

Similarly, if you have to clean up a mess created by a water or sewage backup, the expense won't be covered by standard homeowner's insurance. But here, too, you can purchase a special rider to avoid this headache, often for less than $100 a year.

The list of other types of damage that usually aren't covered range from mold to insect and termite infestations to acts of terrorism, war, and nuclear attack. Dig your policy out of your files and take a few minutes to assess your risk exposure for these events.


Even if you're covered for damage—through standard insurance or a rider—payments from the insurance company are based on the property's replacement cost, not its fair market value. Also, if your home is destroyed and it's insured for less than the replacement value, you'll have to pay some of the rebuilding cost. In addition, deductibles and maximum dollar caps may affect reimbursements for possessions that are destroyed or stolen.

In terms of liability exposure, one way to avoid dire consequences is to supplement your current coverage with an umbrella liability policy. As the name implies, the umbrella policy sits on top of your homeowner's and auto insurance policies to provide additional protection. For instance, if a neighbor slips and is injured on your icy sidewalk or a tree topples onto a car parked in front of your home, an umbrella policy may pick up the slack.

Just like other forms of insurance, you'll need to shop around for the best umbrella policy. And keep in mind that umbrella coverage kicks in only after other insurance is exhausted, and umbrella policies usually carry deductibles equal to the required underlying limits for the auto and homeowners policies. Still, the cost of umbrella coverage usually isn't prohibitively expensive. You may be able to obtain $1 million in liability coverage for $200 to $300 a year. And you may get a discount for using the same carrier. That could prove a small price to pay for plugging the gaps in policies. ●

## Japan's Lost Decades

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price increases seen in 1980s Japan. During the 1990s, Japanese real estate lost an average two-thirds of its value. In contrast, U.S. real estate prices are expected to fall 30% to 40%, although some areas, including Las Vegas, Phoenix, and Miami, have seen steeper declines.

Moreover, the U.S. economic structure is more open and fluid than that of Japan, where banks and major industries had a tendency to sweep problems under the rug. In the United States, major banks have quickly (with the push of the government) written off billions in bad debt in an attempt to get a recovery going without unnecessary delay.

But the most basic difference between Japan in 1990 and the United States today lies in the speed in which interest rates were lowered. American economists, most notably current U.S. Federal Reserve Chairman Ben Bernanke, have criticized Japan's central bank for failing to reduce interest rates quickly enough during the early 1990s, with the delay spawning rampant, long-lasting deflation. Eager to avoid that mistake, the Fed has taken several steps to cut interest rates and keep money flowing. And both the Bush and Obama administrations have pumped billions of dollars into the U.S. economy in the form of corporate bailouts and economic stimulus plans.

Even though the crisis in the United States seems unlikely to mirror the Japanese experience, it's impossible to know what will happen to stocks, real estate, commodities, and currencies in the near term. That's why we advise you to continue protecting yourself from the vicissitudes of the stock market and the world economy by remaining broadly diversified in your investments. That's the best way to ensure you are in a good position to benefit when the economy starts coming back to life. ●

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