

# International Pension Issues 2|09

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United States

## Severe setback in financial and retirement assets

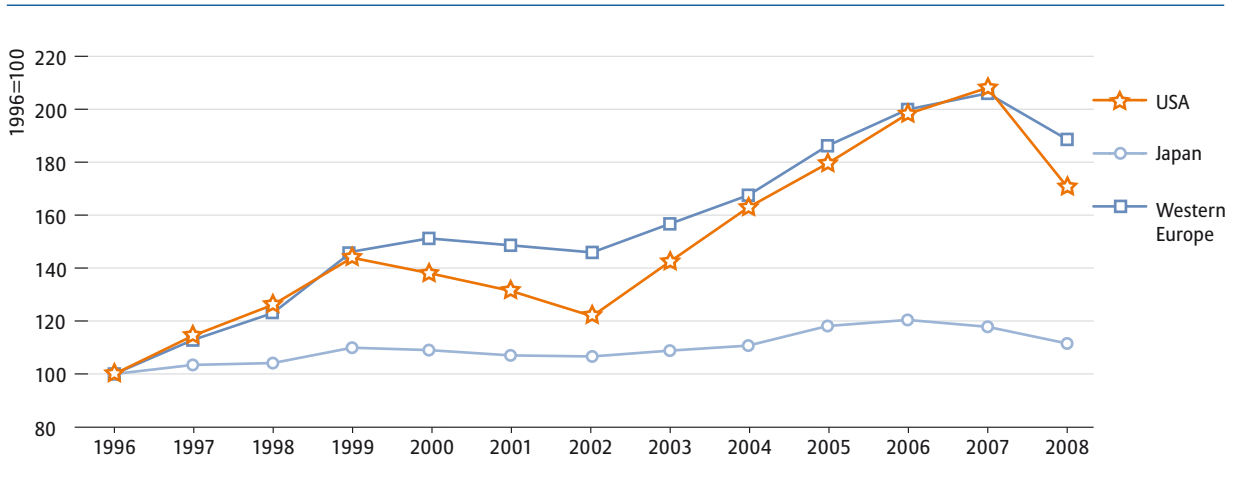
Financial assets of private households in the U.S. tumbled 18% in 2008, an annual decline not seen in the decades since World War II. Gross financial wealth amounted to USD 40.8 trn at the end of 2008 down from USD 49.7 trn at year-end 2007, as reported by the Federal Reserve in its flow of funds statistics.

Actually, the landscape had already changed in 2007 following the eruption of the subprime crisis and the downturn in housing markets. But equity markets were still heading up until the third quarter of 2007. By then households enjoyed an all-time-high in financial wealth as the USD 50trn threshold was crossed. But the sliding stock and housing markets have since wiped out around USD 9trn in financial assets alone, which corresponds

to the combined financial wealth of Germany and Spain.

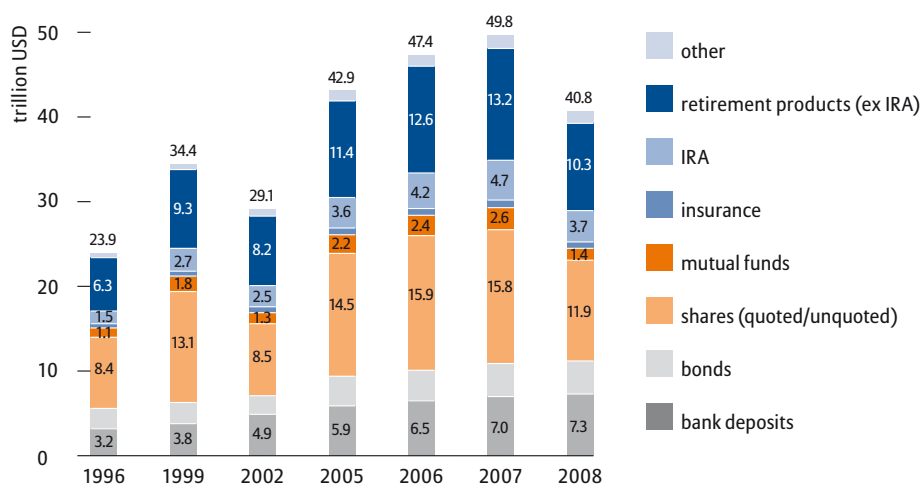
While the downturn had a much larger impact on households' portfolios in the U.S. those in Western Europe and Japan also took a hefty knock. The more conservative investment pattern in Western Europe led to an estimated decline of around 8.5% (the loss ►

Financial assets of private households – world regions in comparison



Source: Allianz Global Investors' estimates for Western Europe 2008

## U.S. Financial assets of private households



Source: Federal Reserve; ICI; Allianz Global Investors estimation for IRA 2008

particularly in Germany was comparatively small; see IPI 1/09), whereas Japan had to face a loss of 5.5% in 2008 compared to 2007.

The most dramatic decline in the U.S. (USD 3.66 trn) was recorded in the corporate equities segment, as one would expect given the decline of more than 40% in the S&P 500 index. This was attributable solely to devaluations as households did not withdraw equity from their portfolios. However, apart from bank deposits, all asset classes were caught by last year's downturn. This means diversification of portfolios did not shield American households from exceptionally large losses. In addition, households that had diversified into real estate suffered even more losses in total wealth. In contrast, to the equity market downturn at the beginning of the century the housing market slide had a crossover affect on financial assets and worsened the situation as some pooled asset classes encompass real estate investments (as can be seen in the position 'investment in unincorporated businesses' with a loss of 11% – USD 900bn in absolute terms, due mainly to the drop in real estate prices). With their large exposure to equity and mutual funds

investments in their pension arrangements as well, American households lost USD 3 trn of pension fund reserves as shown in the flow of funds statistics. In addition to these there are the tax-favored individual retirement accounts (IRA) which can be invested in other product types. To gauge the value loss in the total retirement market, IRA assets have to be extracted from mutual funds, bank accounts and other products. At the end of 2007 IRA assets stood at USD 4.75trn; one year later they amounted to an estimated USD 3.65trn. This means the U.S. retirement market shriveled from USD 18 trn at the end of 2007 to roughly 14trn in 2008. This is a deep cut into retirement provision for many households and the gap will need to be filled. As an upshot, we expect many people to step up their savings efforts and many others to extend their working life, particularly those who are close to retirement.

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