



Emotions and Human Impulses Drive Retirement Investment Decisions

ING, a global financial services leader, today released a report entitled "Psychology, Emotion, Investing and Retirement: Exploring Participant Behavior in Defined Contribution Plans" that examines a growing body of data that sheds light on how human psychology and emotion can cause barriers to adequately preparing for retirement financial security. However, employers can play an important role in providing employees resources to help make better retirement savings decisions.

The report examines how these emotional behaviors can impact an investor's investment decisions and discusses some of the solutions that employers can make to encourage "good" behavior by employees that participate in their employer-sponsored retirement plans.

The tenets of behavioral finance, a discipline that combines the cold analytics of finance and investing with the human element of emotion, indicate there are emotional reasons that cause people to make mistakes in retirement plan investing.

Common emotional and behavioral drivers include:

- **Procrastination and inertia** - While most people know they should contribute to their workplace retirement plan, many put off doing so. Others who do participate in an employer-sponsored retirement plan are simply not saving enough.
- **Information Overload and Analysis Paralysis** - When there are too many choices - both in the "real world" and within a retirement savings plan - people may be overwhelmed, and make no choice at all, which could have detrimental effects for retirement planning.
- **Irrational Investment Decision Making** - Rather than using analytical tools, many people invest based on "irrational biases," such as

arbitrary rules of thumb, familiarity, overconfidence, and fear of loss.

"The power of emotional behaviors and their impact on how individuals invest cannot be underestimated," said Brian Haendiges, senior vice president, ING Defined Contribution. "But there are ways for companies to help their employees make better decisions when it comes to investing in their workplace retirement plan."

"For employers, there's a new dynamic to building, implementing, communicating and managing defined contribution plans, such as 401(k)s, 403(b)s and 457 plans, given the vastly expanded role they are being called upon to play in helping employees plan for their future retirement income."

The various emotions and human impulses can negatively effect how participants invest including:

- **Poor diversification** -- participants have poor diversification with respect to equity exposure. Younger workers tend to invest too conservatively (do not invest enough in equities), and older workers tend to invest too much (too aggressively).
- **Rebalancing** - revisiting allocation across asset classes four to eight times per year tracks with a greater instance of beating the S&P 500. Yet 68% of those studied did not rebalance at all. Only 12% rebalanced

the optimal number of times (four to eight).

- **Fund Choice** - over the longer-term period studied (five years), the participants who most significantly outperformed the S&P 500 Index invested in between six and 15 funds. Yet the average number of funds used by 401(k) participants was just 4.1.
- **Asset Allocation** - Over both the three and five year period, investors who included an asset allocation fund in their portfolio were significantly more likely to beat the S&P 500 than those who did not. Yet just 34% of the investor population uses these funds.

The report discusses various elements employers can use in their Defined Contribution plan to help their employees make better retirement plan investment decisions. Plan design elements such as an employer match, automatic enrollment, contribution increases, the inclusion of a target date or lifecycle funds and a limited fund selection can help participants make beneficial decisions.



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Employers View Older Workers as Very Productive

H SBC finds 49% of the world's employers view older workers as productive and motivated as younger workers, however, most employers are not taking advantage of the opportunity their older workers present.

In a global survey of 20 countries and territories called "Future of Retirement: What the world wants", HSBC's research revealed that 91% of Canadian employers view older workers as productive as younger workers. Fifty-eight per cent of employers across the globe believe older workers are more loyal and 53% believe them to be more reliable than younger workers. While in Canada, 99% of employers perceive older employees at least as reliable and loyal and 82% said they are as motivated as younger ones.

Globally, 72% of respondents reject the idea of a mandatory retirement age. Individuals indicate they want more flexible employment practices to help them continue working past traditional retirement age. Thirty-nine per

cent of respondents said they would like to teach younger workers, 32% said they want to learn new skills and want the opportunity to work fewer hours. However, HSBC found that employers are not doing enough to retain these workers.

The research also shows that most individuals worldwide want to be primarily self-sufficient in funding their retirement. About 38% of Canadians want the government to enforce additional private savings to help individuals help themselves and 28% want retirement age increased.

Canadians are more likely than most to believe they should bear most of the financial cost of retirement. Canadians also are far less likely to rely on assistance from their children in their old age, with only 13% expecting their children to help pay living expenses compared to 29% globally and 16% expecting their children to help pay for medical expenses compared to 30% globally.



Over Half of Employers to Reduce Post-Retirement Benefits

Over 57% of Canadian employers plan to reduce the level of health benefits offered to retirees over the next three years, according to a survey conducted by Hewitt Associates. Four per cent plan to eliminate them entirely.

"Canadian organizations that currently offer retiree healthcare benefits are in a difficult position right now," says Jason Kolysher, senior benefits consultant at Hewitt in Calgary. "Many are simply uncertain as to how to manage rising healthcare costs while still providing the quality coverage needed to attract and retain key talent."

Forty-three per cent cited the large number of employees predicted to retire in the next decade as a factor causing them to reduce retiree benefits.

Reductions in retiree health benefits will likely include stricter eligibility requirements, reduced medical coverage, increased cost-sharing and increased flexible retiree benefits plans over the next while.



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sions. Additionally, regular, ongoing and simple communication (versus simply relying on traditional "education enrollment meetings") about retirement plan investing - not just at one point in time - may help employees feel good about participation decisions and help them understand their options and help them make the appropriate investment decisions.

"The solutions proposed in this report each have the potential to improve the retirement preparedness for participants of employer sponsored retirement plans," said Haendiges. "ING recognizes the need to work closely with employers to continue to look for new ways to help them, help their employees make the right decisions when it comes to investing for retirement."

To access a copy of the report, go to <http://www.ing.com/us>.

Emerging Markets Posting Strong Returns

Institutional investors are gradually moving away from investing in the U.S., focusing instead on international equities (Europe, Asia)-and more than ever-emerging markets like China, India, Russia, Brazil and Mexico.

"The focus in the past has really been U.S.-centric," said Robert Jasminski, vice-president, international equities with GE Asset Management in Stamford, CT, speaking in Toronto on March 1, 2006. "Emerging markets had a really strong run [in 2005]."

According to Jonathan Passmore, GE's senior vice-president and portfolio manager, international equities in London, U.K., the idea of globalization suddenly became mainstream last year among larger Canadian investors, perhaps the result of the removal of the Foreign Property Rule, he theorized. That led to a renewed interest in international investing and emerging markets. "The concept--all of a sudden it seems like it's been here forever," he said.

What have fuelled this interest are strong returns from international equity markets. Though the highest returns were seen in the last quarter of 2005, overall annual returns were solid, with Japan posting a return of 25.5%, EAFE

at 13.5%, Europe with a return of 10.5% and emerging markets at 34%.

U.S. equity returns have been much poorer, hovering in the 5.3% to 7.1% range. U.S. discretionary spending has also been dipping and the real estate market has cooled off. Despite this, Passmore predicted a "fairly optimistic outlook for the U.S." And U.S.-based Jasminski said the new U.S. federal reserve chairman, Ben Bernanke, will likely follow the lead of former chairman, Alan Greenspan. "I think Bernanke thinks we can grow our way out of this," he said.

But emerging markets "are one area we're excited about," said Passmore, adding that "enormous markets" like China and India are being seen as huge growth opportunities. He added that those institutional investors seeking to diversify their portfolios would be well-advised to consider moving into investments in these markets. Said Passmore, "There is a lot less risk in emerging markets than there was 10 years ago."

Three Pillars of Retirement Stable

The financial reserves in Canada's three principal retirement programs have doubled since the 1990s according to Statistics Canada. Adding up the total amount for registered pension plans, registered retirement savings plans and the Canada/Quebec Pension Plan, Canadians have saved up more than \$1.3 trillion. Employer sponsored plans accounted for the biggest pool of assets at about 63% of savings. However, the percentage of paid workers covered by a registered pension plan fell to 39% in 2003 from 45% in 1991.

But employer contributions were up at the end of 2003, according to StatsCan, with total contributions coming in at \$29 billion-up 36% from 2001.

Nearly 1.4 million RRSP holders aged 25 to 64 cashed in all or part of the savings under the Home Buyers Plan. Close to nine per cent of tax filers in this age group took advantage of this program in 2004, withdrawing \$14.2 billion.



health tips

Get a Good Night's Sleep

Approximately 30 per cent of people suffer from sleep deprivation at some point in their life. This insomnia, also called sleep disruption, can lead to psychological stress, higher rates of work absenteeism, higher rates of accidents, and reduced quality of life. Fortunately, there are many effective treatments for insomnia, including medication, bed restriction, cognitive therapy, and more. If you suffer from this condition, seek treatment by talking to your family physician.

Exercise to Prevent Osteoporosis

"One of the best ways to build and maintain healthy bones is through exercise," says Professor Helmut Minne, author of a recent report on osteoporosis. Osteoporosis is a disease characterized by deterioration of bone tissue, which leads to increased bone fragility and risk of fracture. Minne adds that improving muscle strength causes a person's bones to strengthen. He recommends that people engage in brief 'load-bearing' exercises such as walking, climbing stairs, or doing household chores to build bone health.

Attitudes Changing on Post-Retirement Debt

Canada's aging baby-boomers continue to change the face of society, with a new attitude toward post-retirement debt beginning to surface, according to RBC Financial Group's 15th Annual RRSP survey

In a poll conducted by Ipsos-Reid, 48% of respondents said they did not believe it was necessary to pay off all of their debts before retirement. Among working Canadians, 85% said it was important to escape their debts first, but one-third of retirees are carrying debt. The average debt load among retirees is \$35,000, but 14% of them have debts in excess of \$100,000.

The most common forms of debt are mortgage and credit card debt, with 42% of retirees carrying such debt. Six per cent of retirees hold a line of credit, while five per cent still hold business loans or car loans.

"We seem to be observing an emerging mind-set where many Canadians do not see the need to retire their debt before they themselves retire from work,"

said Dave Richardson, vice-president, RBC Asset Management. "If this is in fact a new reality, Canadians will need to strategize and plan for their retirement differently to ensure they can achieve their desired lifestyle during retirement."

Among debt-carrying retirees, 44% said they never planned on paying off their debt before they retired in the first place, and 51% incurred their debt after they had retired. Among those who did incur post-retirement debt, 67% said they had not expected to take on debt.

"While entering retirement debt-free continues to be the most prudent approach, these findings suggest that some Canadians, especially baby boomers, generally have different lifestyle expectations for retirement and are making different choices than previous generations," said Richardson.

The survey found that women exhibited more of Richardson's prudence, with 57% believing it is "essential" to retire debt-free, compared to 46% of men. Younger respondents are also more



likely to consider it essential to clear their debts before retirement. Among 18 to 34 year olds, 36% said it was not essential. Among those aged 35 to 54, acceptance of debt rose to 49%, and hit 65% among those over the age of 55.

While a dramatically increased life expectancy is putting a pinch on retirement savings, Canadians are also retiring earlier than ever - on average, at the age of 58, during prime earning years.

While they are retiring from full-time employment, they are not necessarily leaving the workforce altogether. Twenty per cent of retirees supplement their income by working either part-time, occasionally, or by taking on contract jobs from time to time. Perhaps not surprisingly, those who retired with debts are more likely to work occasionally (35%) than are those who do not have debts (13%).

"In order to achieve their goals, Canadians should be thinking about planning investment horizons over a longer time period and from an earlier age," Richardson says. "For those who are planning to retire with debt, it is especially important they do their homework to make sure they'll be able to generate enough income and cash flow to both maintain their lifestyle and to successfully manage any debt."

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