County of Los Angeles
Savings Plan

April 2007

Focus On: Understanding How the Big Picture Affects You

Rolling with the Economy

How the business cycle impacts your bottom line

You can't read the paper without coming across the words "inflation" (rising prices for goods and services) and "interest rates" (the cost of borrowing money). Experts often use them to explain movements in the financial markets. Economic fluctuations can impact the value of your retirement savings. To understand this connection and benefit from it, we need to discuss what economists refer to as "the business cycle."

Think of the business cycle as a wave—something that moves up and down. When the economy grows, the wave goes up. There is more competition for loans, workers and goods and services—pushing up prices and wages. With more money circulating in the economy, people are more likely to take out loans. In order to keep this economic movement in check and to prevent inflation, the Federal Reserve Board (the Fed) will eventually raise interest rates.

Rising interest rates can cause a slowdown in the rate of economic growth—or even a recession, which occurs when the Gross Domestic Product (GDP), the total value of the goods and services produced by our economy, shrinks. As the wave turns down, falling demand for loans, goods and services, and workers may cause interest rates, prices and wages to decline. In severe cases, the result is deflation, which is defined as a drop in GDP lasting four or more consecutive months.

Recession can be kept in check by the Fed lowering interest rates, making it less expensive to borrow. Subsequent spending ignites economic growth, causing a rise in the GDP before deflation sets in. The economy begins to recover and the business cycle starts to move up once more.

Following the Fed

The Fed helps determine the growth rate of our economy. Economic expansion has an impact on factors ranging from inflation to corporate growth, which, in turn, influence the financial markets.

The Fed can act to increase the rate of economic growth by buying government bonds from securities dealers. The dealers then lend and invest some of that money, injecting cash into the economy. The Fed can also reduce the "fed funds rate," the rate at which commercial banks make overnight loans to each other to encourage more lending.

Conversely, it can help to slow economic growth and fend off inflation by selling government bonds or increasing the fed funds rate.

But whatever action the Fed takes, its ultimate goal remains the same: to maintain steady economic growth and low inflation over the long term.

Yen, Euros, Dollars and You

In the middle of a global economy

If you live, work and shop in the United States, the value of the dollar will vary with inflation. However, if you go abroad, the dollar's value changes constantly.

For good or bad, the U.S. dollar is considered one of the benchmarks in international currency. The value of the U.S. dollar is not only a measure of how competitive our products are in the international market, but it can also be used to measure the health of our economy. And, as one of the world's largest consumers, how money is spent by U.S. consumers can have a direct effect on foreign economies.

With a "strong" U.S. dollar, American consumers have more purchasing power, resulting in an increase of cheaper imported foreign goods. However, U.S. businesses have a more difficult time competing with foreign companies because their goods are more expensive in foreign markets. This results in less demand for U.S. produced products and a boom for foreign businesses. As a consequence, consumers are buying more imported goods compared to the revenue generated by U.S. business exports—known as a "trade deficit."[1] If not controlled, U.S. business growth could be hampered and lead to a downturn in the business cycle.

On the other hand, a "weak" U.S. dollar makes products made by U.S. producers more competitive in foreign markets and could potentially stimulate business growth at home. Simply put, a weak dollar means fewer imports of expensive foreign products. This sounds like a perfect situation for a strong domestic economy. However, a prolonged drop in U.S. imports could produce a vicious cycle that bites our economy. Unable to sell their products, foreign businesses suffer, their economies decline and the value of their currency declines, making the U.S. dollar stronger. U.S. products become more expensive and less attractive in the international market; U.S. business suffers, which directly affects our economy.

Here's an example of the change in the value of the U.S. dollar. In June 2002, you could buy one euro for $0.95. In late 2006, one euro cost $1.31. One British pound cost $1.46 in June 2002. At the end of 2006, $1.95 purchased one British pound.[2]

Foreign Investors and the U.S. Economy

Of the $12.9 trillion of U.S. stocks, foreigners own about $1.3 trillion worth.[3] Foreign investing is considered critical to our economy. These investors are directing international cash flow into the U.S. financial markets, which builds and strengthens our economy. As more money flows into the U.S. economy, more jobs for workers, new products and services, and eventually more innovation are possible. These factors feed economic growth. If the U.S. dollar and economy strengthen, more foreign investors looking for investment and growth opportunities will be attracted to the U.S. financial markets.

Finding a Balance

As you can see, the value of the U.S. dollar can play a significant role in the long-term health of both U.S. and foreign economies. It is the federal government's role to make sure the dollar is healthy by implementing sound trade practices and monetary policies.

1 A trade deficit occurs when the value of goods entering into a country is less than the value of goods leaving the country to be sold in foreign markets.
2 Federal Reserve Statistical Release H.10, Foreign Exchange Rates (Weekly). Release dates June 10, 2002, and December 29, 2006.
3 Bureau of Economic Analysis News Release: U.S. International Investment Position, 2005, June 29, 2006.
4 Federal Reserve Bank of New York, 2006.

Did you know:
The value of the dollar and other currencies in the international market fluctuates every day depending on economic, political and international events. Banks worldwide trade more than $1.2 trillion worth of currency every day.[4]

The Big Picture

Building a diversified long-term retirement plan

Now that you've read three big-picture articles about the business cycle, the Fed and the global marketplace, you may be wondering how it affects you and your retirement strategy. Your best weapon against the changing economy is to carry a diversified portfolio within a blend of asset classes.

Contrary to conventional wisdom, assembling a portfolio composed solely of the stocks with the hottest performance track records may not be the best idea. You may be surprised that the most important factor to consider in assembling a quality portfolio is asset allocation. Asset allocation is the mix of asset classes—stocks, bonds and cash equivalents—within your portfolio. A good way to think of your portfolio is like a pizza with several toppings. Just as you pick the right balance of menu items to suit your taste, you need to select a good mix of assets to suit your risk tolerance, which can be based on things like your age and desired return.

When you order a pizza, you don't simply ask for meat or veggies, you specify what you want—like pepperoni, sausage, mushrooms or onions. That same principle applies to your asset mix. Rather than just choosing to invest in stocks, you'll want to diversify within that asset class by electing different options—like large-cap, mid-cap, small-cap or international stocks[5] and—to ensure you have a variety of toppings. Diversification is the process of choosing multiple investments within an asset class and different asset classes and not relying on one type of investment to hold the weight of your entire portfolio.

Once you feel comfortable with your diversified, long-term investment strategy, you'll potentially notice a smoother ride during the twists and turns of the financial markets. You can't create a wholesome pizza with only dough and marinara sauce or establish a successful portfolio comprised solely of stocks. Spice up your retirement portfolio with extra toppings—just as you would your delectable pizza. The addition of bonds and cash equivalents can help to further diversify your investment portfolio. While you're at it, grab a newspaper and look through the funnies and sports pages instead of focusing on the ups and downs of individual stocks. You're well on your way to a satisfying retirement meal.

5 Equity securities of companies with relatively small market capitalization may be more volatile than securities of larger, more established companies. Medium sized companies may suffer more significant losses as well as realize more substantial growth than larger capitalized, more established issuers. Foreign investments involve special risks, including currency fluctuations and political developments. A bond fund's yield, share price and total return change daily and are based on changes in interest rates, market conditions, economic and political news and the quality and maturity of its investments. In general, bond prices fall when interest rates rise and vice versa.

Putting the Pieces Together: Economic Balancing Act

Our economy is a complicated balancing act with the domestic business cycle supplying the core stimulus for economic growth. It is influenced by the global markets through the value of the U.S. dollar and foreign investments, and it's tempered by the Fed.

Exciting Upcoming Plan Changes!

The Plan Administrative Committee (PAC), with the assistance of an outside consultant, has completed a thorough review of the investment options offered in the County of Los Angeles Savings Plan. In light of this review, some upcoming changes will be implemented to provide you with the opportunity to better diversify and simplify your investment choices in the Plan. Be on the lookout for additional communications regarding these upcoming changes.

Termination Pay Program

On January 26, 2007, the PACs of the 401(k) Savings Plan and 401(a) Termination Pay Pick-Up Plan ceased accepting before-tax termination pay contributions to their respective Plans. This action was necessary as a result of official notification from the Internal Revenue Service that before-tax termination pay contributions, as currently structured in the Plans, are impermissible under recent federal tax guidance.

If you are part of the Termination Pay Program or have a pending contract, you will receive a separate mailing explaining further action to be taken in regards to your account.

Great-West Retirement Services® Customer Service Is There for You

On-Site Customer Service Locations

Martin Luther King/Drew Medical Center
12021 S. Wilmington Ave., Los Angeles
First and third Monday every month in main lobby

LAC/USC Main Hospital
1200 N. State St., Los Angeles
Second and fourth Friday of each month in cafeteria

Kenneth Hahn Hall of Administration
500 W. Temple St., Los Angeles
Third Thursday of each month, second floor lobby entrance from mall

Public Works
900 S. Fremont Ave., Alhambra
Third Wednesday of each month in cafeteria

Health Services
313 N. Figueroa St., Los Angeles
Fourth Thursday of each month in the main lobby

Olive View Medical Center
14445 Olive View Dr., Sylmar
Fourth Wednesday of each month in cafeteria

Rancho Los Amigos Rehabilitation Center
7601 E. Imperial Hwy., Downey
Second Thursday each month in Café Los Amigos cafeteria

Harbor/UCLA Medical Center
1000 W. Carson St., Torrance
Second Thursday of each month in elevator lobby

Note: On rare occasions, a representative may not be available. Representatives also follow the normal holiday schedule.

How to Reach Us

On the Internet: www.countyla.com[6]

By Phone: (800) 947-0845

Call the L.A. County Service Center toll free and choose "1" from the menu of options you hear to obtain information or make changes to your account. You will be connected to KeyTalk®, an automated service available 24 hours a day, seven days a week.[6] Once you enter your Social Security number and Personal Identification Number (PIN)[7], you can retrieve personal account information and make changes to your account.

In Person: The L.A. County Service Center

Located at 500 N. Central Ave., Suite 220, Glendale, CA 91203. Office hours are Monday through Friday, 8:30 a.m. to 5:00 p.m. Pacific Time. Call (800) 947-0845 and choose "4" from the menu to schedule an appointment.

Representatives of GWFS Equities, Inc. are not registered investment advisers, and cannot offer financial, legal or tax advice. Please consult with your financial planner, attorney and/or tax adviser as needed.

6 Access to KeyTalk and the Web site may be limited or unavailable during periods of peak demand, market volatility, systems upgrades/maintenance or other reasons.

7 The account owner is responsible for keeping the assigned PIN confidential. Please contact Great-West Retirement Services immediately if you suspect any unauthorized use.

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