

BACKGROUND

THE RETIREMENT CRISIS

THE PROBLEM: LACK OF ADEQUATE RETIREMENT SAVINGS

1. Inadequate Account Balances

Most workers approaching retirement do not have enough saved to maintain their living standards in retirement, regardless of income. The typical older worker in the bottom 50% of the income distribution (earning less than \$40,000/year) has nothing saved for retirement. The median savings of worker in the middle 40% (earning between \$40,000 and \$115,000/year) are only \$60,000. Among workers in the top 10% of the income distribution (above \$115,000/year), the median amount saved is \$200,000. See Figure 1.

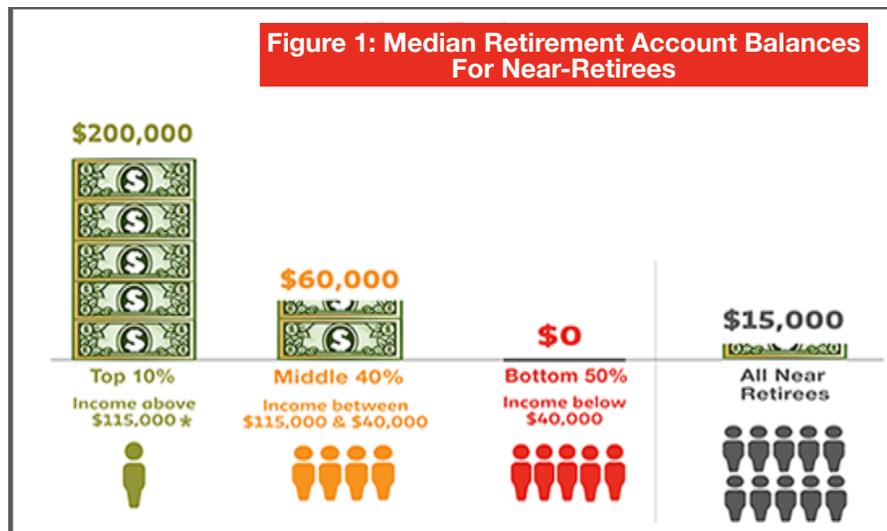
2. Lack of Needed Retirement Income

Low savings mean that all income groups fall short of their target replacement rates – the percentage of pre-retirement income needed to maintain

one's standard of living in retirement – by over 20 percentage points. The typical worker in the bottom 50% of the income distribution needs 85% of their pre-retirement income in retirement to maintain their standard of living. However, they can expect to have only 60% based on their current savings and Social Security benefits. In the middle 40%, older workers need 75% of their pre-retirement income, but will be able to replace only 54%. Even older workers in the top 10% are likely to experience a shortfall. As retirees, they will need 65% of their pre-retirement income, but will be able to replace only 40%. See Figure 2.

3. Downward Mobility in Retirement

The systemic problem of inadequate retirement saving leaves retirees at risk of experiencing a sharp decline in their living standards. With less income in



Source: SCEPA's calculations using 2014 Survey of Income and Program Participation (SIPP) data. Note: Near-retirees are the age group 55-64. * Income per year.

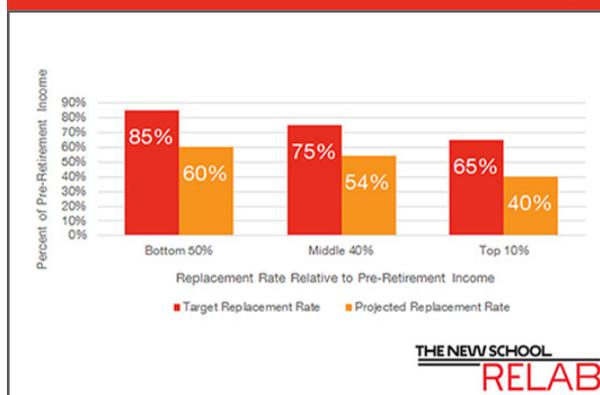
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retirement, many will have no choice but to cut back. For some, this deprivation means falling into poverty or near-poverty when they retire.

ReLab defines workers as downwardly mobile if their and their spouse's current income is more than twice the 2014 Federal Poverty Level (\$23,340 for a single individual and \$31,260 for a couple), but projected to fall below this level in retirement.

Relab projects that out of 21.5 million older workers ages 50-60 and their spouses who are not poor or near poor, 8.5 million - or 40% - will fall into poverty or near poverty when they retire at 62.

Figure 2: American Workers Fall Short of Target Replacement Rates for Retirement Security



Source: Papadopoulos, M., Ghilarducci, T., and Webb, A. (2018) "Millions of Older Workers Will Fall into Poverty in Retirement." Schwartz Center for Economic Policy Analysis and Department of Economics, The New School for Social Research, Policy Note Series.

THE CAUSE: THE "DO-IT-YOURSELF" RETIREMENT SYSTEM HAS FAILED

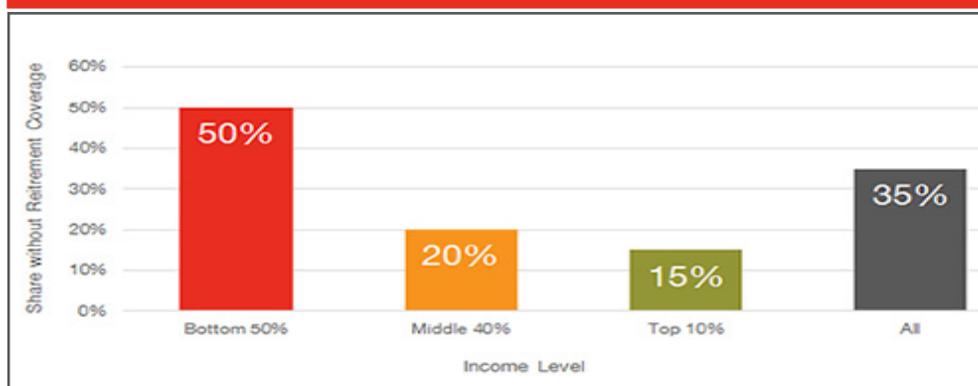
1. Lack of Coverage

Inadequate retirement savings result from systemic failures of the American retirement system. Workers do not have access to employer-sponsored retirement savings plans. Half of all older workers in the bottom 50% of the income distribution do not have access to a retirement savings plan at work. In the middle 40%, a fifth of workers do not have access. And in the top 10%, 15% of older workers do have access to a plan at work.

2. Switch to 401(k)s

Since the 1980s, employers have increasingly replaced their defined benefit (DB) pensions with defined contribution (DC) savings accounts such as the 401(k). DC accounts fail American workers for the following reasons: participation is [voluntary and conditional on the employer offering a plan](#), so that many contribute sporadically, if at all; [many withdraw funds before retirement](#); investment returns are eroded by high fees and sub-optimal portfolios; balances are paid out as lump sums rather than in the form of a lifetime income; and the tax preferences for retirement savings [disproportionately benefit high earners](#). See Figure 3.

Figure 3: Older Workers Lack Retirement Coverage at All Income Levels



Source: Ghilarducci, T., Papadopoulos, M., and Webb, A. (2017) "Inadequate Retirement Savings for Workers Nearing Retirement" Schwartz Center for Economic Policy Analysis and Department of Economics, The New School for Social Research, Policy Note Series. Survey of Income and Program Participation. SCEPA's Calculations. Note: Older Workers are the age group 55-64.

THE SOLUTION: NOT “NUDGES” OR WORKING LONGER, BUT SYSTEMIC CHANGE

Scholars and analysts who view the retirement crisis as a problem of human error and poor individual choices offer two solutions: behavioral “nudges” to increase savings, such as auto-enrollment into existing DC plans and auto-escalation of account contributions, and working longer.

1. Nudges Are Not Enough

Behavioral nudges are inadequate for the task as they ignore the reality that almost [all workers](#) experience swings in income over their careers that make it difficult to maintain the consistent contributions necessary to accumulate enough retirement savings in a 401(k)-type account. Over a working lifetime, almost all workers experience multiple unemployment spells lasting over a year and reductions in earnings of 10% or more, with the bottom 50% of earners more vulnerable to both. When these income shocks occur, DC accounts are often tapped, [serving double-duty](#) as both emergency funds and retirement saving and making them less effective at both.

2. Working Longer Won’t Work

If workers with inadequate savings are forced to work longer to avoid deprivation in retirement, the quantity and quality of the jobs available to them is dependent on the whims of the labor market. Currently, the labor market for older workers leaves many [suffering](#) from long-term unemployment, low wages, and a lack of employer-sponsored retirement coverage, particularly for [older women](#). Additionally, many older workers cannot continue working due to [physical limitations](#), particularly [black workers](#).

Given these realities of the labor market, a structural change in how we approach retirement security is necessary to solve the retirement crisis.

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3. Guaranteed Retirement Accounts

Comprehensive reform includes two necessary steps: 1) strengthening Social Security, and 2) creation of Guaranteed Retirement Accounts (GRAs) as individual accounts to supplement Social Security.

Conceived as “pensions for all”, GRAs are universal, professionally-managed, portable, mandatory retirement savings accounts. Workers and their employers split annual contributions of at least 3% of wages. Additionally, GRAs benefit from risk-pooling, guarantee workers’ principal, provide a tax credit to offset low-earners’ contributions, and prohibit early withdrawals to ensure savings are preserved for retirement.

GRAs are designed to close the gap in retirement savings left by the loss of traditional DB pensions in the workplace, low access to any kind of coverage on the job, and inefficient DC accounts such as 401(k)s. They provide a safe, effective vehicle for workers to accumulate personal retirement savings over their working lives.

Note: With the exception of downward mobility, our analysis of the retirement crisis focuses on individuals, rather than households. The reality of [growing divorce rates among near-retirees](#), and the [disproportionate effects of divorce on women’s health and financial security](#), make it imperative that retirement income adequacy be studied at the individual level. When estimating the risk of downward mobility, we focus on the household, not the individual, because poverty is measured at the household level.

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