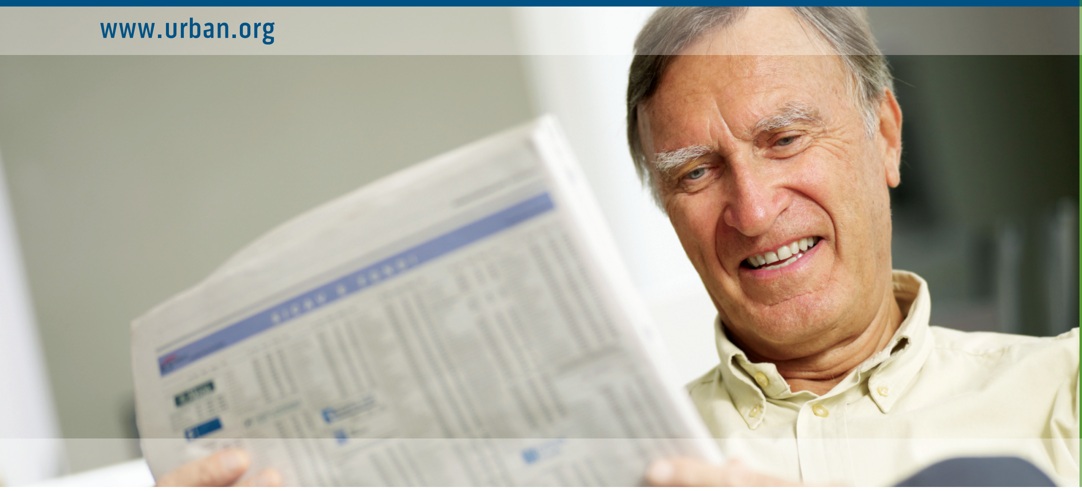
URBAN INSTITUTE

BRIEF # 34
FEB. 2012

Program on Retirement Policy

www.urban.org



INSIDE THIS ISSUE

- Boomer women have worked more than ever before, boosting family incomes and retirement wealth.
- The shift from pensions paying regular retirement income for life to 401(k) plans subject to market volatility adds uncertainty to boomers' retirement income.
- 30 to 40 percent of the youngest boomers will not replace 75 percent of earnings received in their early fifties, making it difficult to maintain preretirement living standards.

Boomers' Retirement Income Prospects

Melissa M. Favreault, Richard W. Johnson, Karen E. Smith, and Sheila R. Zedlewski

The debate over the economic security of future retirees has special meaning for baby boomers, the 77 million surviving Americans born between 1946 and 1964. Many of the oldest boomers, who began turning 65 last year, have already retired or will soon. The youngest boomers are now in their late forties, prime earning years when retirement savings typically ramp up. Because of their sheer numbers, the boomers' exit from the labor force and reliance on public retirement benefits will reverberate through society, affecting business, government, and younger taxpayers as well as retirees themselves. By 2030, when the last boomers have turned 65, the share of Americans age 65 or older will rise by almost half, from 13 percent today to 19 percent.[1]

Boomers face increasingly uncertain retirement prospects. Traditional employer-sponsored pensions that pay a fixed benefit from retirement until death—once a mainstay for middle-class retirees—have been disappearing, replaced by 401(k)-type plans whose payout depends on unpredictable investment returns. The 2008 stock market crash wiped out trillions of dollars in retirement savings, and stock values still hadn't recovered by the end of 2011. The worst housing slump since the Great Depression combined with widespread mortgage borrowing when home values were increasing has suppressed home equity values. Rising health care costs, stagnant wages, and potential Social Security cutbacks add to boomers' concerns.

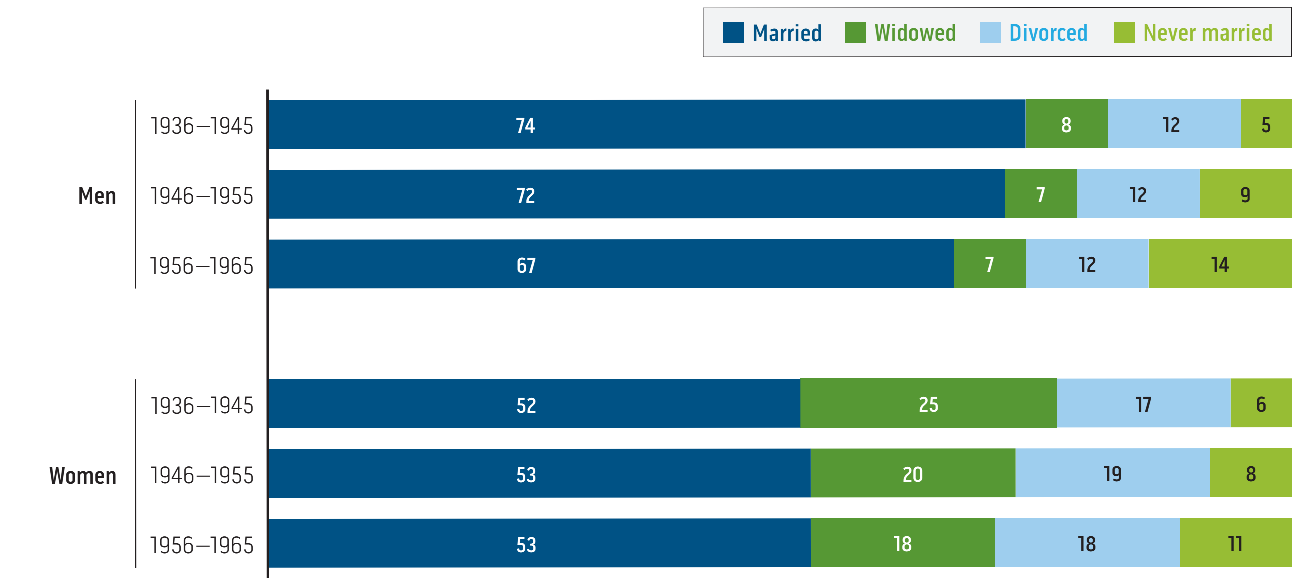
But there also is encouraging news. Boomer women have worked and earned more than ever before, propping up family incomes and boosting retirement wealth. Average earnings grew earlier in boomers' careers, health status improved (especially at older ages), and strong economic growth propelled home and stock market values to new highs, despite recent setbacks.

How will these conflicting forces play out? This brief shows how changing patterns of lifetime earnings, pension participation, and wealth accumulation outside of retirement plans will combine to shape boomers' economic well-being by the time they reach age 70, when most have retired and accrued all their retirement savings. Our focus on age 70, however, generates a somewhat rosier retirement picture than if we considered boomers at a younger age, since high-income, better educated people tend to live longer.[2]

Using DYNASIM3, the Urban Institute's dynamic microsimulation model, we compare

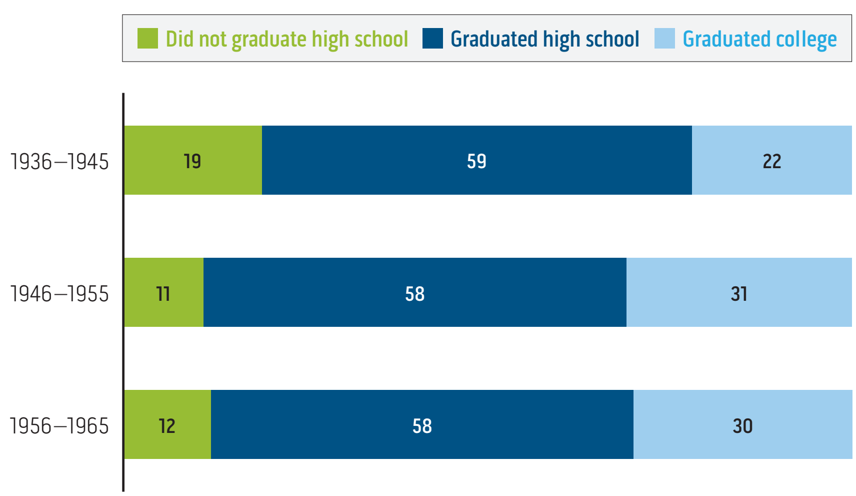
Social Security historically has provided the bulk of retirement income, at least for lower- and moderate-income retirees, and will continue to play this role for boomers.

Figure 1. Marital Status at Age 70, by Birth Cohort (%)



Source: Dynamic Simulation of Income Model 3, Run Number 834.

Figure 2. Educational Attainment at Age 70, by Birth Cohort (%)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

early boomers, born between 1946 and 1955, and late boomers, born between 1956 and 1965, with the pre-boomer cohort born between 1936 and 1945. The projections begin with recent patterns in earnings, retirement, and financial assets and then base future growth on the intermediate assumptions in the 2011 Social Security Trustees report.

The results from the projection are mixed: boomers will receive more income at age 70 than their predecessors, but that income will replace a somewhat smaller share of their preretirement earnings. Compared with their pre-boomer counterparts, boomer men will have less in retirement assets while boomer women will have more. The projections indicate 30 to 40 percent of late boomers will not reach a 75 percent replacement rate, suggesting that they may be unable to maintain their preretirement living standards at age 70. However, the predicted share at risk is only slightly higher than for their predecessors.

Changing Demographics

Shifting demographics at older ages will play an important role in boomers' retirement income security. Americans are living longer. Between 1980 and 2007, life expectancy at age 62 increased three years for men and two years for women.[3] Reduced mortality is a significant achievement, although the gains have been concentrated among well-educated and high-income Americans.[4] Longer life expectancy has lengthened retirements, even though some people have begun working longer. Longer lives in turn boost the cost of Social Security and traditional pensions, and mean that retirees' savings must last longer.

Lower mortality reflects better health at older ages and greater investments in health care. The share of Americans age 65 to 74 reporting fair or poor health fell from 32.5 percent in 1983 to 21.6 percent in 2008.[5] It's not clear, however, whether this trend will continue. The gains occurred mostly before 2000. Reported health hasn't improved much since then and disability rates are now inching up for people in their forties and fifties.[6] Nonetheless, the Social Security trustees project that age-62 life expectancy will increase another two years for men and one year for women by 2025.[7] Other analysts predict that future generations will live even longer.[8]

Marriage, divorce, and widowhood patterns are also changing and will influence financial security at older ages. Retirees often lose some of their spouse's Social Security and pension benefits when they become widowed or divorced and singles forgo the financial security of a second paycheck and the cost savings from shared expenses. As a result, widowed, divorced, and never-married seniors have much higher poverty rates than married couples.

As men's life expectancy rises, the gender gap in mortality will shrink and widowhood will become less common among older women. The projections indicate that only 18 percent of late-boomer women will be widowed at age 70, down from 25 percent among pre-boomer women (figure 1). Falling marriage rates, especially among boomers born after 1955, will increase the share of singles at age 70 compared with earlier cohorts—an uptick that will be offset by the decline in widowhood among older women. However, a smaller share of boomer men (and especially late-boomer men) will be married at age 70 than in earlier generations.

Adult children often support their retired parents, sometimes with financial assistance but more often with chores and personal care when their parents become frail. However, declining fertility rates will leave about one in six late-boomer women childless, compared with only about 1 in 12 pre-boomer women. With fewer adult children, more boomers will need to pay for help if they become frail.

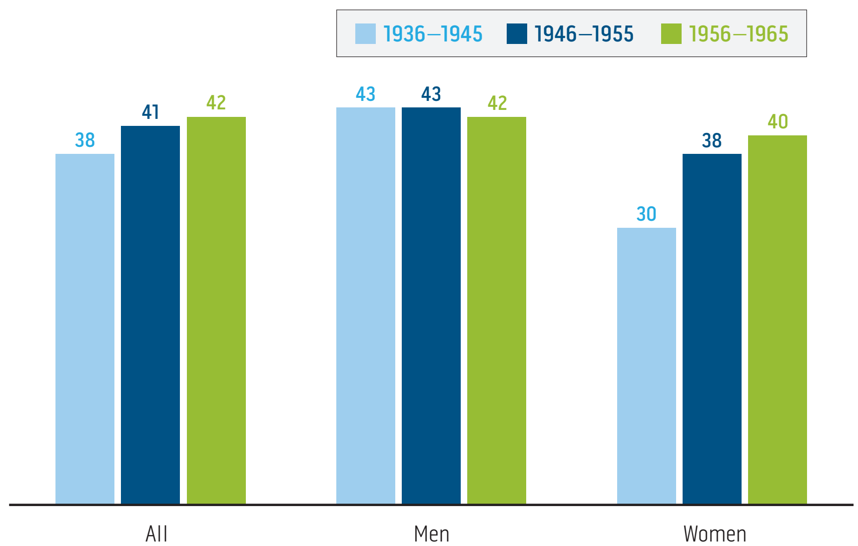
Higher educational attainment by boomers should enhance their financial security. Education boosts earnings and helps qualify workers for less physically demanding jobs, promoting work at older ages. The surge in college attendance in the 1960s and 1970s increased the share of late boomers with a bachelor's degree to 30 percent, up from 22 percent for those born between 1936 and 1945 (figure 2). Only 12 percent failed to complete high school, less than two-thirds the dropout rate for pre-boomers.

Lifetime Earnings

Retirement incomes depend critically on how much people worked and earned when they were younger. Higher lifetime earnings mean more Social Security and—for those with coverage—larger pensions and retirement account balances. It also means the ability to save more outside of retirement accounts.

The employment rate for women grew dramatically over the past generation. Between 1975 and 2007, the share of women age 25 to 54 participating in the labor force (either working or looking for work) went up from 55 to 76 percent.[9] Over the same period, their male counterparts scaled back their work somewhat,

Figure 3. Median Number of Years Employed by Age 70, by Birth Cohort



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

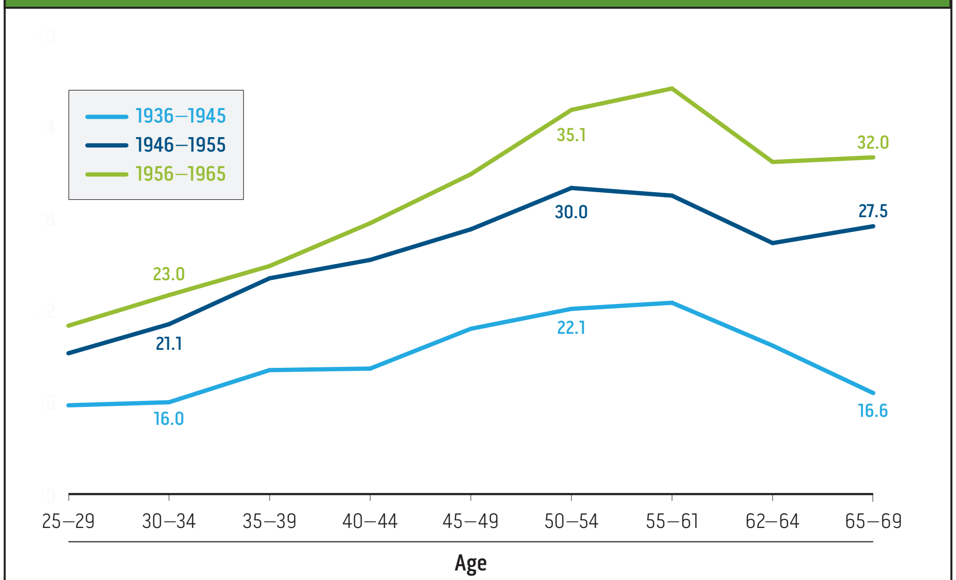
with labor force participation rates falling from 94 to 91 percent as job opportunities for low-skilled men eroded.[10]

Older men and women are both working more. Between 1990 and 2010, labor force participation rates at ages 62 and older increased from 22 to 29 percent for men and from 12 to 20 percent for women.[11] This growth reflects Social Security changes that boosted work incentives (by raising the full retirement age and eliminating the work penalty for older beneficiaries), as well as the shift away from traditional private-sector pension plans that reward early retirement.[12] Older women's employment growth also reflects the aging of a generation that has always worked much more than earlier ones.

These trends will significantly boost lifetime employment and earnings for boomer women, according to our projections. By age 70, late-boomer women will have worked a median 40 years of employment, compared with 30 years for pre-boomer women (figure 3). By contrast, a typical boomer man will work roughly the same amount as a typical pre-boomer man. Employed early-boomer women ages 50 to 54 earn 36 percent more per year in inflation-adjusted dollars than their pre-boomer counterparts ($30,000 versus $22,100), while late-boomer women will earn 59 percent more ($35,100) (figure 4).

Median earnings have been falling or stagnant for men, however. Through age 50, working boomer men earn less than their pre-boomer counterparts (figure 5). Earnings for the three cohorts generally converge after age 50, when most estimated boomer earnings are based on model projections (that assume inflation-adjusted earnings rise 1.2 percent per year, somewhat faster than actual recent growth) rather than direct observation. The long-term stagnation in men's median earnings, which has been widely debated among scholars and policymakers, has been driven by the poor job prospects for men with no more than a high school diploma.

Figure 4. Median Annual Earnings for Employed Women, by Birth Cohort (000s, $2010)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Retirement Incomes

While more retirees will rely on earnings to augment their incomes at age 70 and beyond, most will still rely primarily on traditional sources of retirement income. Social Security historically has provided the bulk of retirement income, at least for lower- and moderate-income retirees, and will continue to play this role for boomers. Many will receive some income from traditional pensions, although more will have riskier 401(k)-type plans. Most boomers also will have some other financial assets and housing equity. Whether these income sources will adequately replace preretirement income, though, depends on how much retirees will spend, especially on health care.

Social Security. Social Security will continue to be the primary income source for boomer retirees, despite the ongoing controversy over its financing. The system now pays more benefits than it collects in taxes, but is paid for through 2036 by a reserve fund built up over the past 25 years when taxes exceeded benefit payments.[13] While some scaling back of Social Security may be necessary to ensure benefits beyond 2036, any changes likely will affect boomers far less than later retirees.

Social Security retirement benefits are based on earnings (up to the taxable maximum) over 35 years. Retirees who have worked at least 10 years qualify for these worker benefits. Those who have not worked enough to qualify on their own can receive a benefit equal to half their spouse's benefit, but divorced spouses must have been married for at least 10 years. Widows and widowers may receive the spouse's full benefit. Those with small worker benefits receive partial spouse or survivor benefits so that the combined payment equals the full spouse or survivor benefit.

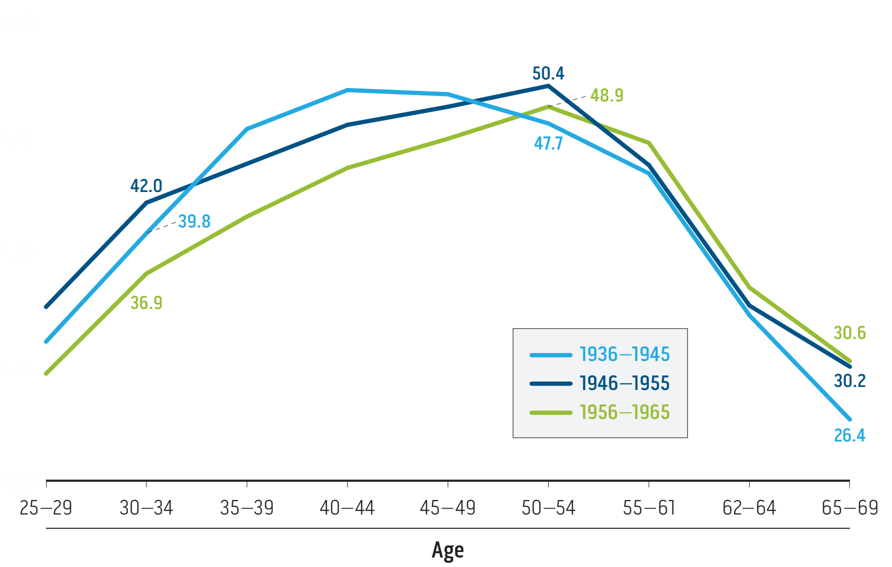
The projections show that boomer women's higher labor force participation and earnings will boost their Social Security benefits. Two-thirds of women in the late-boomer cohort will qualify solely for a worker benefit, compared with 44 percent of pre-boomer women (figure 6). It is likely only about 1 in 10 late-boomer women will rely solely on spouse or survivor benefits. The projections indicate that late-boomer women will receive much more Social Security income than their predecessors. Median benefits for late-boomer women will be 44 percent higher in real terms than those for pre-boomer women and 17 percent higher than for early boomers ($15,500 compared with $10,800 and $13,300) (figure 7). Lifetime Social Security benefits will rise more rapidly for late-boomer women because they will live longer and collect more monthly benefit checks than their predecessors.

Future benefits for boomers would be even higher if not for the scheduled increase in Social Security's full retirement age, which rose from 65 to 66 for the early-boomer cohort and will rise to 67 for much of the later cohort. Retirees may still collect benefits as early as age 62, but they will face a stiffer financial penalty—a 30 percent reduction in benefits for those born in 1960 and later, compared with only 20 percent for those born in 1938 and earlier. Increases in women's work and earnings, however, swamp the effect of the retirement-age changes.

For men, the retirement-age change, combined with their stagnant earnings, will dampen the growth in their retirement benefits. If recent earnings patterns hold, real Social Security benefits will inch up for the late-boomer cohort relative to the early-boomer cohort—just 3.8 percent over this 10-year period ($19,300 compared with $18,600). Of course, boomer men (and women) could end up with higher benefits, if more work longer and wait for unreduced benefits than current trends predict.

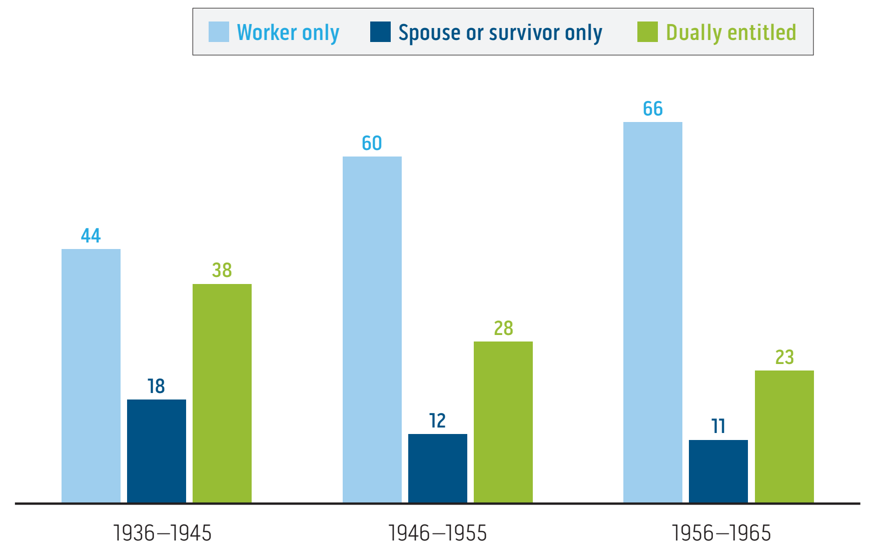
Pensions. Retirement plans have moved away from defined benefit (DB) pensions that pay a lifetime benefit typically based on earnings and years of service to defined contribution (DC) plans that usually combine employer and employee contributions over the years of coverage. Thirty-nine percent of

Figure 5. Median Annual Earnings for Employed Men, by Birth Cohort (000s, $2010)



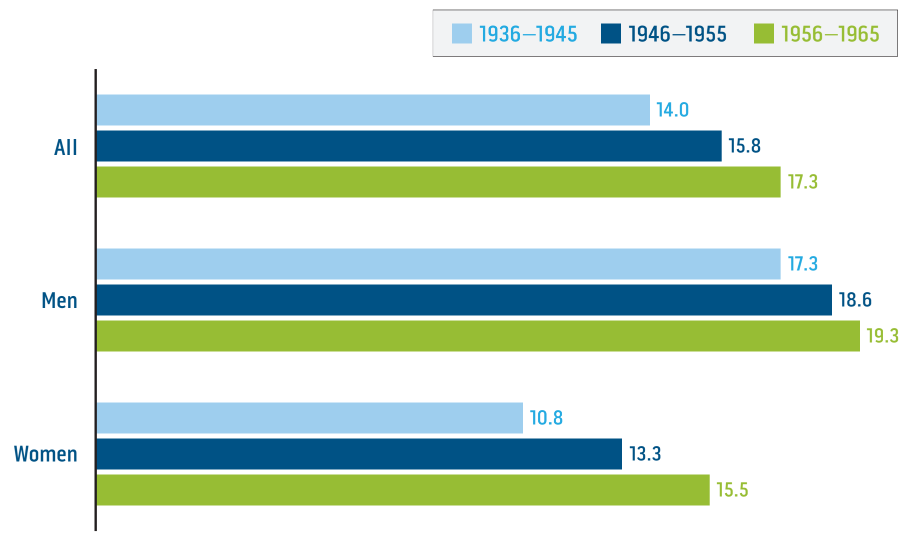
Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Figure 6. Social Security Benefit Type at Age 70 for Female Beneficiaries, by Birth Cohort (%)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Figure 7. Median Own Annual Social Security Income among Beneficiaries at Age 70, by Birth Cohort (000s, $2010)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

private-sector workers were covered by DB plans in 1980, compared with 19 percent in 2010. During the same period, the share participating in DC plans rose from 19 to 41 percent.[14] Nonetheless, many boomers will receive a traditional pension because many work in industries where DB plans are common, including the public sector.[15]

The shift toward DC plans and away from DB plans will have mixed effects for boomers' retirement income security. Workers who often change employers typically do not earn much of a DB benefit because these benefits typically accrue most rapidly in the years immediately before retirement age. Benefits accrued early on erode with inflation. In contrast, DC balances earn investment returns even after workers change jobs, but the uncertainty of investment returns makes DC plans more risky. Prolonged market downturns, for example, can leave workers with a small account that generates little retirement income. Retirement account assets (DC and IRAs) dropped by $2.7 trillion (31 percent) from the third quarter of 2007 through the end of the first quarter of 2009.[16] While most of this aggregate loss was recovered in subsequent years, by the end of 2011 account balances remained below their peak in 2007. Another potential risk in DC plans relative to DB plans is the temptation they present for workers to withdraw assets before retirement.[17]

Since more women boomers worked, more women will qualify for a pension based on their own earnings, improving retirement income security for themselves and their families. Pension coverage among women has steadily increased since the late 1980s so that it is now on a par with coverage for men.[18] Because future pension benefits are tied to earnings, these benefits grow as women earn more.

The shift away from DB pensions, the increases in boomer women's pension coverage, and assumptions about rates of return on account assets will substantially affect future pension wealth, according to our projections.[19] For example, median predicted pension wealth for those with DB pensions will drop by nearly half between the pre-boomer cohorts and the late boomers ($141,600 to $75,600) (figure 8).

In contrast, projected DC pension wealth will rise by 51 percent (from $68,700 for the pre-boomers to $103,900 for the late boomers) and the share of 70-year-olds with DC wealth will increase slightly from 52 to 54 percent. The combined pension picture shows that 63 percent of late boomers will have some pension wealth at age 70. Projected pension ownership and wealth will go up slightly between the pre- and the early-boomer cohorts, and then decline for the later boomers.

The share of women with pension wealth at age 70 increases across the three cohorts, while the share of men with pension wealth declines somewhat.[20] Projected pension wealth also grows for women but not for men, although men will continue to outpace women in total accumulations. For example, total pension wealth for women with pensions increases from $91,400 to $111,200 between the pre- and later-boomer cohorts (22 percent), while wealth for men falls from $197,700 to $164,500 (17 percent).

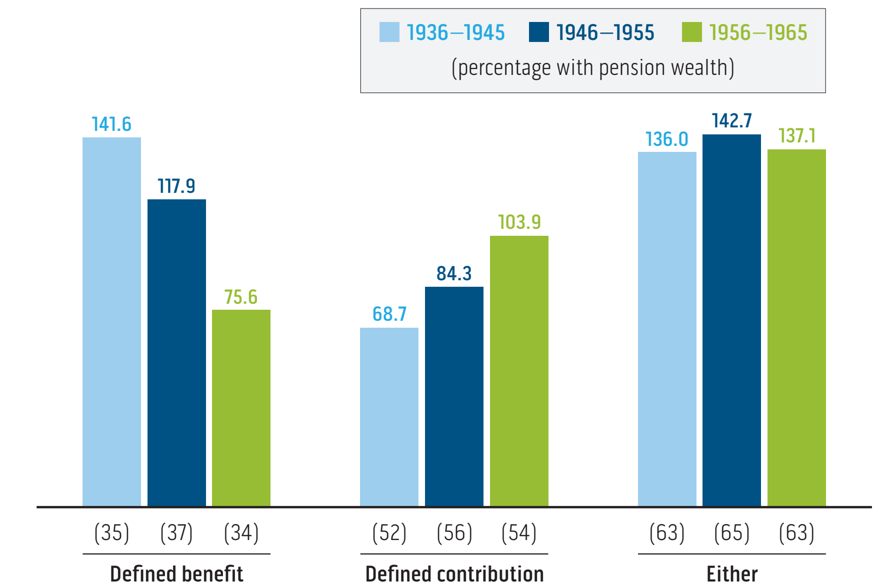
Ownership and levels of pension wealth differ dramatically by education and income quintile, our detailed projections show. Only 3 in 10 individuals without a high school diploma have some pension ownership among later boomers and their median pension wealth is only $24,500—less than half the pension wealth of early boomers without a high school diploma. These results reflect the steady erosion in unionized, lower-skilled manufacturing jobs that typically provided pension coverage. Today, higher-skilled jobs more often provide pensions. Predicted pension wealth rises dramatically with income. Late boomers in the bottom income quintile with any pension wealth typically accumulate only $16,600 compared with $58,800 for those in the second income quintile. Nearly 9 in 10 individuals in the top income quintile have projected pension wealth, and median accumulations reach $388,500, about 23 times the median wealth of those in the bottom income quintile.

Financial and housing wealth. Financial assets and housing equity are especially difficult to project. Recent stock market volatility shows that savings held in equities can dramatically fall (or grow) in any given year. Housing values began declining in 2007 and continued to fall in most markets through 2011.[21] However, the history of market indexes suggests an eventual return to long-term average growth. Our projections capture the falloff in financial and housing wealth through 2011, and assume that real rates of return eventually stabilize at their historic levels.[22] The projections also capture how changes in individual characteristics likely will affect these accumulations.[23]

While quite low, predicted median financial wealth per person grows across the three cohorts (figure 9). The median 70-year-old will have financial assets outside of retirement accounts valued at $42,300 for the late-boomer cohort, compared with $29,100 for the pre-boomer cohort. Predicted financial assets will be quite low for those in the bottom income quintiles and rise dramatically with income.[24] For example, the late boomers in the top income quintile have 100 times the projected median financial wealth of those in the bottom income quintile ($555,300 compared with $5,400). Boomer men will hold more financial assets than boomer women. Projections show that widowed and never-married women in all three cohorts will have accumulated few assets in financial accounts by age 70. For example, median values will reach just $29,500 for late-boomer widows and $23,500 for late-boomer women who never marry.

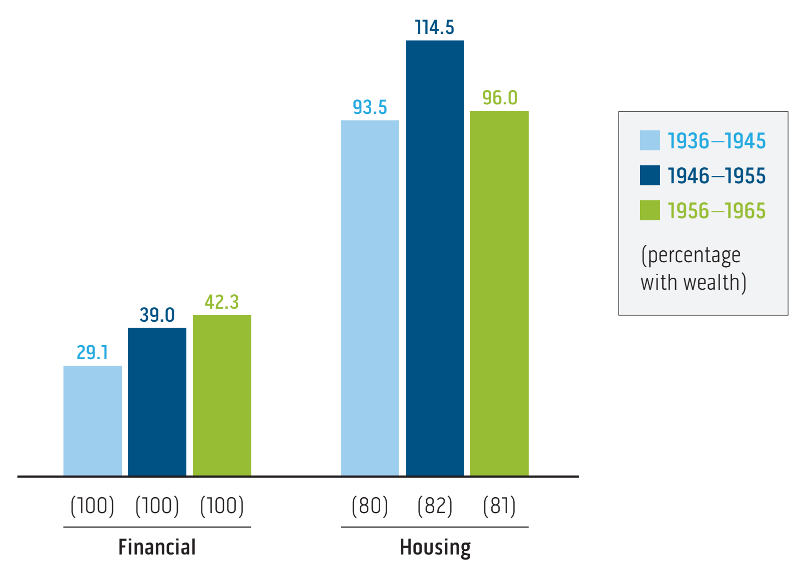
While most retirees do not tap into the equity in their homes, doing so can generate income through a reverse annuity mortgage or home equity line of credit.[25] The projections show that boomers, like their predecessors, will have high rates of homeownership, with about 8 in 10 owning a home. Early boomers benefitted from rising housing prices during their

Figure 8. Median Own Pension Wealth among Pension Owners at Age 70, by Birth Cohort (000s, $2010)



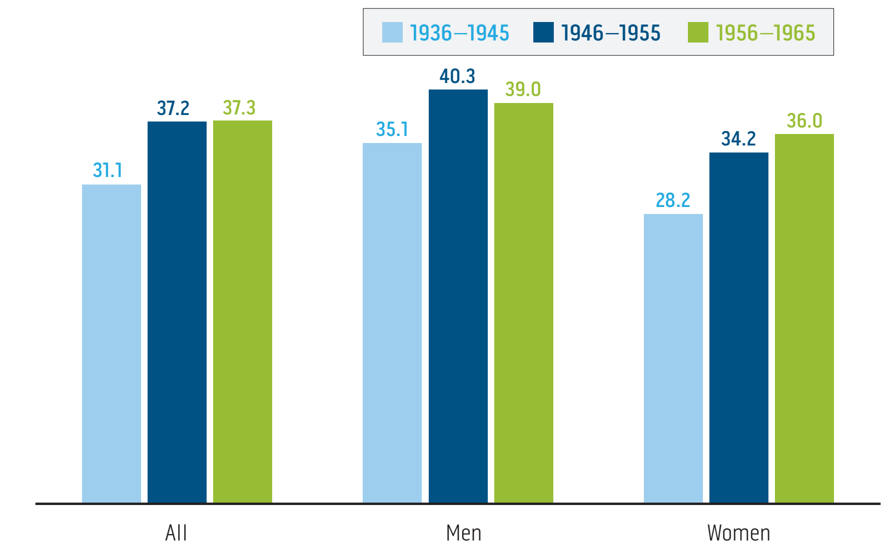
Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Figure 9. Median Per Capita Financial and Housing Wealth among Owners at Age 70, by Birth Cohort (000s, $2010)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Note: Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Figure 10. Median Annual Per Capita Family Income at Age 70, by Birth Cohort, Based on Annuitized Measure (000s, $2010)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Notes: The annuitized income measure includes earnings, Social Security, defined benefit pensions, Supplemental Security Income, and the annual income from an annuity valued at 80 percent of financial assets and retirement accounts. Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

careers, while late boomers were affected more by the housing bust since 2006.[26] Projected median per capita housing wealth increases from $93,500 for pre-boomers to $114,500 for early boomers, and then drops to $96,000 for later boomers. The predicted equity decline for late boomers also reflects trends in increased borrowing against homes prior to retirement.

Will These Resources Be Adequate?

Will boomers have enough to retire comfortably? Some analysts unequivocally conclude that the majority of boomers will have too little, while others argue that many boomers are saving too much.[27] Others conclude that retirement income security will gradually erode, and Gen Xers (born between 1966 and 1975) will be less likely than today's retirees to have enough retirement income to maintain their preretirement standard of living.[28]

The answer depends on assumptions about future retirement-income resources and the amount needed to maintain preretirement living standards. Projected retirement income depends on retirement ages; growth rates for pension, financial, and housing assets; the use of home equity as an income stream; assumptions about how Congress will handle Social Security underfunding; and assumptions about whether retirees annuitize their pension and financial assets. The amount of retirement income required, typically called a replacement rate, depends on expenditure estimates. A 75 percent replacement rate is often used as an adequacy rule of thumb, assuming that spending declines in retirement, especially since retirees do not pay payroll taxes or save in retirement accounts.[29] Others argue that retirees need at least as much income as they had before retiring to cover rising medical costs (as prices and health care use increase).[30]

We use two measures to predict future retirement income. The first, a traditional measure, counts income retirees receive from their financial assets (interest, dividends, and rent) plus money withdrawn from retirement accounts (based on historic withdrawal trends and required minimum distributions) and cash income (earnings, Social Security, and pensions). The second measure assumes that retirees receive the income generated by annuitizing 80 percent of their retirement and financial assets in addition to cash income. The annuitized measure is higher because it assumes that retirees draw down most of their assets during retirement (except for home equity), leaving just 20 percent of their savings.[31]

Annuitized income projections at age 70 again show rising household income for women in each cohort (figure 10). Early boomer men will receive more income than their pre-boomer counterparts, but late boomers will receive less than early boomers. Although the gender gap in retirement income is shrinking, projected annuitized income for late-boomer men will still exceed that for women ($39,000 compared with $36,000). Overall, the projections indicate that early boomers will do better than their predecessors, but this trend will flatten between the early and late boomers. The traditional income measure presents a similar picture, although predicted incomes will be about $5,000 (13 percent) lower for all cohorts than if boomers annuitize assets (figure 11).

Estimating how many boomers will be able to replace 75 percent of their preretirement earnings depends on how the measure is constructed. With a replacement rate based on average earnings received between age 50 and 54, the annuitized income measure predicts that about 3 in 10 late boomers will fall short of a 75 percent replacement rate (figure 12). The traditional measure of retirement income finds that nearly 4 in 10 will be at risk. The replacement rate projections do not vary much between the pre- and late boomers. The projections also show that relatively few boomers receive enough income at age 70 to replace more than 150 percent of their preretirement income—22 percent of late boomers, compared with 26 percent of pre-boomers, according to the traditional income measure.

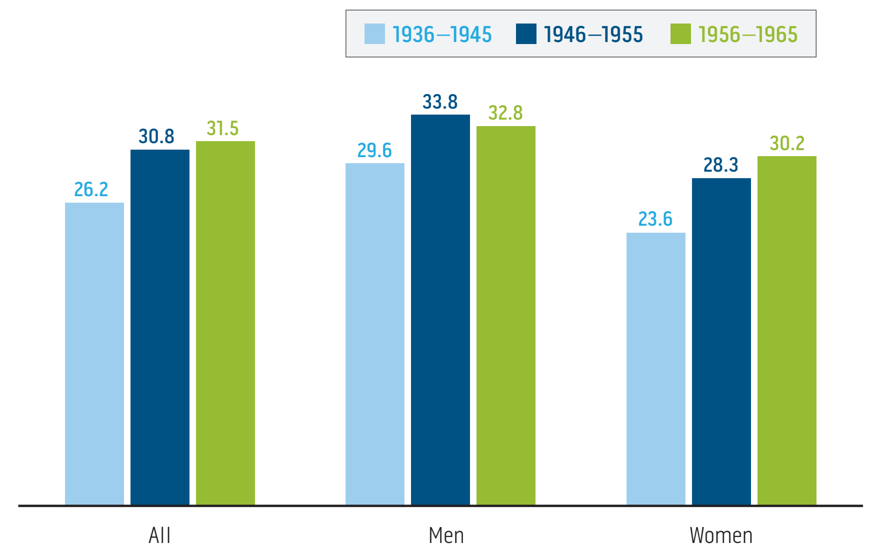
Projected replacement rates based on the top 35 years of lifetime earnings provide a somewhat rosier picture since earnings averaged over a lifetime are typically lower than those measured in the early fifties, when earnings generally peak. The predictions indicate that about a quarter of late boomers will not replace 75 percent of their average lifetime earnings using the annuitized income measure. Projections using the traditional retirement income measure show that 35 percent fail to reach 75 percent of average lifetime earnings. (See online appendix charts A.16 and A.17 at http://www.urban.org/publications/412490.html.)

Of course, a 75 percent replacement rate may not be sufficient in the future. If out-of-pocket health care costs continue to grow rapidly, older adults will need more resources to finance an adequate retirement income. Johnson and Mommaerts (2010), for example, project that the median ratio of out-of-pocket health spending to income for adults age 65 and older will rise gradually from 10 percent of income in 2010 to 15 percent in 2030.[32] This implies that boomers, especially those in the later cohort, will need to have at least 80 percent of their preretirement income to achieve the same living standard as their pre-boomer predecessors. Of course, these projections do not include the value of health care benefits received before or after retirement. Accounting for these benefits is very challenging.

Summary and Implications

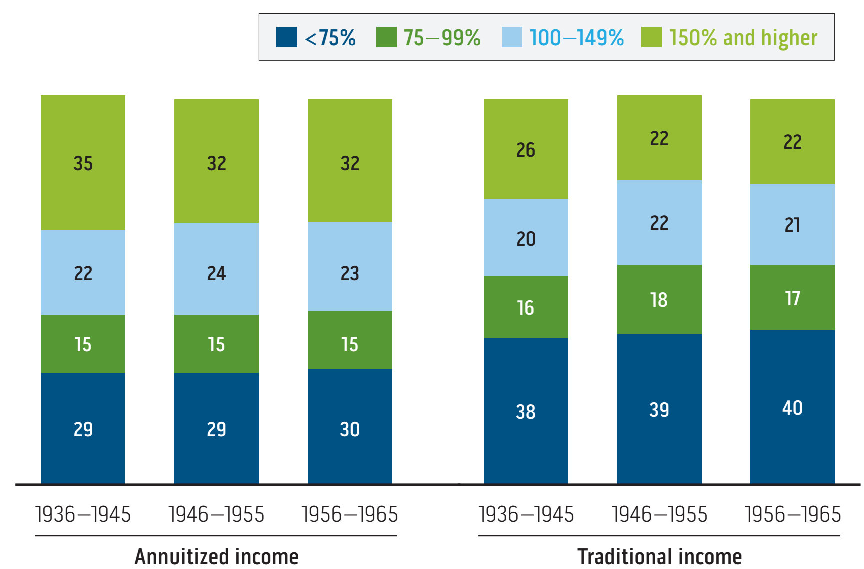
The growth in boomer women's employment and earnings will bear fruit in retirement. The projections show that the majority of boomer women will earn their own Social Security and will receive higher benefits than previous generations. Also, more will have their own pensions or retirement accounts, which will generally be worth more than earlier generations' accounts. These gains will help offset

Figure 11. Median Annual Per Capita Family Income at Age 70, by Birth Cohort, Based on Traditional Measure (000s, $2010)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Notes: The traditional income measure includes earnings, Social Security, defined benefit pensions, Supplemental Security Income, interest, dividends, rent, and occasional withdrawals from retirement accounts. Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

Figure 12. Distribution of Replacement Rates at Age 70, Based on Age 50–54 Earnings (%)



Source: Dynamic Simulation of Income Model 3, Run Number 834.
Notes: The replacement rate equals age-70 income divided by average annual earnings received from ages 50 to 54, both measured in constant 2010 dollars as adjusted by the change in the consumer price index. Projections use the Social Security trustees' 2011 intermediate assumptions (Board of Trustees 2011).

anemic growth in benefits for boomer men, who will have little more Social Security than their predecessors because of their stagnant wages and somewhat reduced labor market activity at earlier ages.

The shift in employer coverage from DB pensions to DC plans means that more men and women with coverage will retire on benefits subject to the volatility of stocks and bonds. Although risky, these accounts will bolster retirement income security if workers participate, assets are invested prudently, and financial markets provide positive long-term rates of return.

Although projected age-70 incomes will be higher for boomers than for their predecessors, the picture of retirement income security that emerges from these trends is worrisome. Counting regular cash income plus income generated from assets and periodic withdrawals from retirement accounts suggests that 4 in 10 late boomers will lack sufficient income at age 70 to replace 75 percent of what they earned between ages 50 and 54. An alternative measure that annuitizes most financial and retirement assets reduces the share that falls below the 75 percent target to 3 in 10. Measures of predicted retirement income adequacy based on earnings averaged over a lifetime—typically less than the average at ages 50 to 54—also paint a somewhat rosier picture. Despite the high share of boomers predicted to be ill-prepared for retirement, the picture is not much worse than for their predecessors.

These predicted outcomes for the typical boomer mask significant differences across groups. Those with limited education will have less retirement income and will rely primarily on Social Security. Also the gap between the rich and poor is striking. For example, boomers in the top income quintile will accrue more than 100 times the financial wealth and 10 times the per capita annuity income held by those in the bottom income quintile.

How boomers really fare in retirement will hinge on several unknowns. How much will stocks and bonds earn over the coming decades? Will more boomers than we expect end up working well into old age? Will a significant share end up dipping into their housing wealth? Will Congress cut boomers' Social Security? And perhaps most important, how much will boomers need to spend on health and long-term care? One estimate suggests that out-of-pocket medical costs will consume 15 percent of income for the median boomer retiree, up from 10 percent for the pre-boomer retirees—which suggests that boomers will need more than their predecessors to enjoy a comfortable retirement. A benchmark of 75 percent of preretirement income may no longer be adequate.

The projections lead to some important policy implications:

- Boomers, especially those with limited education and income and those who are divorced, are widowed, or never married, will continue to rely primarily on Social Security. Policymakers need to ensure the system's long-term financial health.

- Boomers should be encouraged to work as long as they can. Policymakers and employers need to recognize the importance of jobs for older adults, promoting retraining and flexible work schedules that can accommodate their needs.

- Boomers should be encouraged to annuitize some of their retirement accounts and savings when they retire to boost their incomes and produce a guaranteed income stream until death. Policymakers should consider policies that make annuities more attractive and increase trust in these products.

- A significant share of boomers will reach age 70 with very little retirement income. Policy remedies such as modernizing the Supplemental Security Income program and boosting minimum Social Security benefits would help the most vulnerable retirees for modest cost.

- Whether boomers are better off than their predecessors, they will comprise a much larger portion of the total population, straining public resources to meet their needs. Remedies that address this fiscal strain must be mindful of the vulnerability of many older adults, especially those with limited education, widows, and other singles. ▪

Acknowledgments

This brief was funded by a generous grant from the Rockefeller Foundation. The authors are grateful to Serena Lei for editorial assistance, Janice Park for help with the graphics, and Barbara Butrica and Gene Steuerle for helpful comments.

Notes

1. Program on Retirement Policy (2011c).
2. For example, our projections show that 58 percent of individuals born between 1936 and 1965 who die between ages 56 to 69 have no more than a high school diploma, compared with 50 percent of those who survive to age 70.
3. National Center for Health Statistics (1985, 2011b).
4. Meara, Richards, and Cutler (2008); Waldron (2007).
5. National Center for Health Statistics (2011a).
6. Lakdawalla, Bhattacharya, and Goldman (2004); Martin et al. (2009).
7. Unpublished 2011 tabulations from SSA.
8. 2011 Technical Panel on Assumptions and Methods (2011).
9. Bureau of Labor Statistics (2011).
10. Between 2007 and 2011 participation rates for men and women fell slightly as unemployment surged and pushed some workers out of the labor force.
11. Program on Retirement Policy (2011a, 2011b).
12. Friedberg and Webb (2005).
13. Board of Trustees (2011). The trust fund is invested in government securities, and the drawdown in the fund will force the government to redeem these bonds, increasing pressure on the federal budget.
14. Bureau of Labor Statistics (2010); Pension and Welfare Benefits Administration (2001/2002).
15. In 2010, DB plans covered 79 percent of state and local government employees (Bureau of Labor Statistics 2010).
16. Butrica (2012).
17. Butrica, Zedlewski, and Issa (2010).
18. Butrica and Johnson (2010).
19. As explained in Smith (2012), the model accounts for recent market volatility and subsequently assumes real long-run rates of return of 6.5 percent for stocks, 3.5 percent for corporate bonds, and 3.0 percent for government bonds with standard deviations around these averages based on historic experience.
20. See online appendix tables A.6 through A.11 at http://www.urban.org/publications/412490.html for our detailed projections.
21. Case-Shiller (2011).
22. As explained in Smith (2012), financial assets and home equity projections are based on the experiences of recent cohorts documented in numerous datasets.
23. See Smith (2012). For example, lifetime earnings and unemployment spells affect wealth.
24. See online appendix table A.12 at http://www.urban.org/publications/412490.html.
25. While the use of reverse annuity mortgages has increased over the last decade, they are still relatively uncommon. The cost of taking out these mortgages, the lack of knowledge about them, and the requirement that they be repaid when holders vacate their houses all contribute to low adoption (Foote 2010). Before the mortgage crisis some older adults tapped into home equity through home equity loans, but these now are less commonly available.
26. Real housing prices more than tripled between 1987 and 2007 and then dropped about 30 percent (Case-Shiller 2011).
27. Scholz, Seshadri, and Khitatrakun (2006) conclude that fewer than 20 percent of households have less wealth than their optimal targets; Munnell, Webb, and Golub-Sass (2009) estimate that half of today's households will not have enough retirement income to maintain their preretirement living standards; and VanDerhei (2011) estimates that nearly half of early boomers will be at risk of having insufficient retirement income to pay for the basics, including uninsured health care costs.
28. Butrica, Smith, and Iams (2012).
29. See Scholz and Seshadri (2009) for a discussion of replacement rates.
30. VanDerhei (2011).
31. Some analysts also include the annuitized value of home equity in these calculations. We exclude home equity because historically few retirees have actually tapped into this wealth.
32. Out-of-pocket health spending includes premiums (Medicare and private), deductibles and copays, and miscellaneous spending. Johnson and Mommaerts (2010) use the Medicare trustees' 2009 intermediate assumptions (2.2 percent real growth between 2010 and 2020 and 2.9 percent from 2021 through 2030) to project costs.

References

2011 Technical Panel on Assumptions and Methods. 2011. *Report to the Social Security Advisory Board.* Washington, DC: Social Security Advisory Board.

Board of Trustees. 2011. *The 2011 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds.* Washington, DC: U.S. Government Printing Office.

Bureau of Labor Statistics. 2010. *National Compensation Survey: Employee Benefits in the United States, March 2010.* Washington, DC: U.S. Department of Labor.

———. 2011. "Labor Force Statistics from the Current Population Survey." Washington, DC: U.S. Department of Labor. http://data.bls.gov/pdq/querytool.jsp?survey=ln. (Downloaded December 01, 2011.)

Butrica, Barbara A. 2012. "Retirement Account Balances." Washington, DC: The Urban Institute.

Butrica, Barbara A., and Richard W. Johnson. 2010. "Racial, Ethnic, and Gender Differentials in Employer-Sponsored Pensions." Statement to the ERISA Advisory Council, U.S. Department of Labor, June 30.

Butrica, Barbara A., Karen E. Smith, and Howard Iams. 2012. "This Is Not Your Parents' Retirement: Comparing Retirement Income across Generations." *Social Security Bulletin* 72(1): 1–22.

Butrica, Barbara A., Sheila Zedlewski, and Philip Issa. 2010. *Understanding Early Withdrawals from Retirement Accounts.* Washington, DC: The Urban Institute. Retirement Policy Center Discussion Paper 10-02.

URBAN INSTITUTE

Case-Shiller. 2011. "S&P Case-Shiller Home Price Indices." Standard and Poors Financial Services. http://www.standardandpoors.com/indices/sp-case-shiller-home-price-indices/en/us/?indexId=spusa-cash-pidff--p-us---. (Downloaded December 01, 2011.)

Foote, Bruce. 2010. "Reverse Mortgages: Background and Issues." CRS Report for Congress 7-5700. Washington, DC: Congressional Research Service.

Friedberg, Leora, and Anthony Webb. 2005. "Retirement and the Evolution of Pension Structure." *Journal of Human Resources* 40(2): 281–308.

Johnson, Richard W., and Corina Mommaerts. 2010. "Will Health Care Costs Bankrupt Aging Boomers?" Washington, DC: The Urban Institute.

Lakdawalla, Darius N., Jayanta Bhattacharya, and Dana P. Goldman. 2004. "Are the Young Becoming More Disabled?" *Health Affairs* 26(1): 168–76.

Martin, Linda G., Vicki A. Freedman, Robert F. Schoeni, and Patricia M. Andreski. 2009. "Health and Functioning among Baby Boomers Approaching 60." *Journal of Gerontology: Social Sciences* 64B(3): 369–77.

Meara, Ellen R., Seth Richards, and David M. Cutler. 2008. "The Gap Gets Bigger: Changes in Mortality and Life Expectancy, by Education, 1981–2000." *Health Affairs* 27(2): 350–60.

Munnell, Alicia H., Anthony Webb, and Francesca Golub-Sass. 2009. "The National Retirement Income Risk Index: After the Crash." CRR Issue in Brief Number 9-22. Chestnut Hill, MA: Center for Retirement Research.

National Center for Health Statistics. 1985. *U.S. Decennial Life Tables for 1979–81, United States Life Tables.* Washington, DC: Government Printing Office.

———. 2011a. "Health Data Interactive." http://www.cdc.gov/nchs/hdi.htm. (Downloaded December 1, 2011.)

———. 2011b. *United States Life Tables, 2007*. Hyattsville, MD: National Center for Health Statistics.

Pension and Welfare Benefits Administration. 2001/2002. "Private Pension Plan Bulletin: Abstract of 1998 Form 5500 Annual Reports." Washington, DC: U.S. Department of Labor.

Program on Retirement Policy. 2011a. "Female Labor Force Participation Rates by Age, 1948–2010." Washington, DC: The Urban Institute. http://www.urban.org/retirement_policy/datawarehouse/olderworkers.cfm.

———. 2011b. "Male Labor Force Participation Rates by Age, 1948–2010." Washington, DC: The Urban Institute. http://www.urban.org/retirement_policy/datawarehouse/olderworkers.cfm.

———. 2011c. "Number of Persons by Age, 1950–2050." Washington, DC: The Urban Institute. http://www.urban.org/retirement_policy/datawarehouse/population.cfm.

Scholz, John Karl, and Ananth Seshadri. 2009. "What Replacement Rates Should Households Use?" MRRC Working Paper 2009-214. Ann Arbor: University of Michigan Retirement Research Center.

Scholz, John Karl, Ananth Seshadri, and Surachai Khitatrakun. 2006. "Are Americans Saving 'Optimally' for Retirement?" *Journal of Political Economy* 114(4): 607–43.

Smith, Karen E. 2012. "Projection Methods Used in the Dynamic Simulation Model of Income (DYNASIM3)." Washington, DC: The Urban Institute.

VanDerhei, Jack. 2011. "A Post-Crisis Assessment of Retirement Income Adequacy for Baby Boomers and Gen Xers." Washington, DC: Employee Benefit Research Institute.

Waldron, Hilary. 2007. "Trends in Mortality Differentials and Life Expectancy for Male Social Security–Covered Workers, by Socioeconomic Status." *Social Security Bulletin* 67(3): 1–28.

About the Authors

Melissa M. Favreault is a senior fellow in the Urban Institute's Income and Benefits Policy Center.

Richard W. Johnson is a senior fellow in the Urban Institute's Income and Benefits Policy Center.

Karen E. Smith is a senior research associate in the Urban Institute's Income and Benefits Policy Center.

Sheila R. Zedlewski is an institute fellow; she directed the Urban Institute's Income and Benefits Policy Center for 20 years.

Program on Retirement Policy

http://www.retirementpolicy.org

The Program on Retirement Policy addresses how current and proposed retirement policies, demographic trends, and private-sector practices affect the well-being of older individuals, the economy, and government budgets.

URBAN INSTITUTE
2100 M Street, NW
Washington, DC 20037-1231
(202) 833-7200
paffairs@urban.org www.urban.org