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Retirement: Key Facts and Positions
Adequacy of 401(k) plans to meet retirement needs

Data from ICI and other sources shows that, if utilized correctly, 401(k) and other defined contribution (DC) plans—when combined with the other elements that make up America's retirement system—can help form the basis for a comfortable retirement.

The 401(k) system is helping Americans achieve a secure retirement.

- 401(k) plans are a key component of a U.S. retirement system that relies upon a number of complementary components—Social Security; homeownership; employer-sponsored retirement plans, including both DC and defined benefit (DB) plans, private-sector as well as government; contributory and rollover individual retirement accounts (IRAs); and other savings. In retirement, different households will depend on each of these components in differing degrees, depending on lifetime income, work history, and other factors.

- Research indicates that the U.S. retirement system has successfully provided generations of Americans adequate retirement resources.

    - Research shows that workers have accumulated sufficient resources to maintain their standard of living in retirement.

    - Analysis of the transition into retirement shows that most households maintain both consumption and after-tax income at the same level in the first years after retirement as when they were working.

    - Moreover, studies that examine households later in retirement find that, on average, retirees maintain sufficient wealth to generate as much income as they could early in retirement.

- The research also shows that retirement outcomes have been improving over time.

    - Academic analysis has found that successive generations of Americans have reached retirement wealthier than previous generations.

    - Assets specifically earmarked for retirement are now at record levels. Adjusted for inflation and population growth, retirement assets have increased nearly sixfold since 1975.

    - The poverty rate among individuals aged 65 or older has declined from nearly 30 percent in 1966 to 9 percent in 2011.

- Americans across the income distributions depend on employer plans and IRAs. Data from the Survey of Consumer Finances (SCF), conducted by the Federal Reserve Board, show that accrued benefits and asset accumulations in public and private employer-sponsored DC and DB retirement plans and IRAs (which are funded largely by rollovers from DC and DB plans) constituted a resource for about 80 percent of near-retiree households in 2010.

- There has been a shift from DB plans to DC plans in the private sector. However, the share of all workers approaching retirement with resources from employer plans and IRAs has stayed fairly constant at around 80 percent since 1989.

- Recent research shows that, on average, in 1998 the present value of DB plans benefits had represented 59 percent of employment-based retirement accumulations (the total of DB, DC and IRA balances) of near-retirees (aged 57 to 62), while assets in DC plans and IRAs represented 41 percent. For near-retirees in 2010, the balance had shifted to 47 percent in DB benefits and 53 percent in DC and IRA assets. This shift from DB to DC was associated with an 8 percent increase in overall accumulations, in inflation-adjusted dollars.

- A number of studies have concluded that the majority of workers who have access only to DC plans during their working careers will be better off than if they had access only to DB plans, even when taking into account the risks faced by participants in either type of plan (for example, the investment risk faced by workers in DC plans and the job turnover risk faced by workers in DB plans).

    - Comparing typical DB plans with typical 401(k) plans in the SCF data, under a variety of possible labor market and investment return scenarios, a Dartmouth study concluded that "generally, 401(k) plans ... are as good or better than DB plans in providing for retirement."

    - In an analysis of data from the University of Michigan's Health and Retirement Study (HRS), using both detailed descriptions of retirement plans and the actual work histories of individuals, economists from MIT, University of Chicago, Dartmouth, and Harvard projected that retirement resources will be higher on average with private-sector DC plans than they would be with private-sector DB plans.

Three key elements make the 401(k) a success today.

- **Portability**

    - Americans are a mobile workforce, and it's not unusual for them to move from job to job—even career to career. That puts a premium on retirement benefits that are portable—that can travel with a worker throughout his or her lifetime.

- **Ownership**

    - 401(k) owners own actual assets—not a promise of future benefits.

  - 401(k) participants have full rights to their own contributions and the investment earnings on those, subject only to the tax rules that encourage workers to preserve their savings for retirement.

  - While owning and investing one's own assets brings risk, the design of 401(k) plans helps limit the impact of investment shocks and mitigate risks. Workers invest paycheck-by-paycheck (enabling them to take advantage of dollar-cost averaging) in accounts that tend to be diversified.

- **Innovation**

  - Employers can use automatic enrollment to get more workers into plans—a key innovation that uses workers' inertia to boost, rather than depress, saving.

  - They can use auto-escalation of workers' contribution rates to increase savings rates.

  - Employers can choose to offer and workers can choose to invest in target date funds—innovative funds that allocate savings between stocks and bonds based on workers' retirement horizon, and rebalance those holdings as markets move and savers age. These funds provide diversification, keep 401(k) participants exposed to growth assets as part of a balanced portfolio, and help them rebalance in a timely and disciplined manner.

  - Such recent developments in 401(k) plans have helped these investors avoid over-reaction to the financial crisis—overreaction that could hurt their retirement security decades from now.

  - Innovation also has created new services for participants—for example, daily balances, web-based retirement-planning tools, and call centers.

Retirement is a complicated issue that can be hard to measure.

- Today's 40-year-olds are the first cohort of workers who will spend their full career in a 401(k)-based system. Though it's hard to make predictions, participants are committed to the value and benefits provided by the system, according to a recent survey conducted by ICI, America's Commitment to Retirement Security: Investor Attitudes and Actions, 2013.

- Saving is really a lifecycle issue. The focus on formal retirement savings typically occurs later in a working career, so households are more likely to focus on saving for retirement as they near retirement age and as their income increases. For example:

  - In 2010, only 14 percent of households younger than 35 reported that retirement was their primary savings goal, compared with nearly half of households aged 50 to 64.

  - Younger households typically are focused on other goals: one-third of households younger than 35 reported that saving for education, a home, or other large purchase was their primary saving goal.

- Looking at the percentage of all workers who have access to retirement plans at their employers at any single point in time understates the share of the population who will reach retirement with work-related retirement benefits. Distinct "snapshots" of coverage rates in any given year do not offer meaningful information for purposes of assessing the retirement system as a whole.
    - Many young workers, low-wage workers, or part-time workers are more concerned with saving for a rainy day, to purchase homes, or to fund education than they are with saving for retirement. That said, young workers do not remain young throughout their working careers, and many low-wage and part-time workers do not remain low-wage and part-time throughout their careers. Many workers who do not have access to employer-sponsored retirement plans today *will* have access to a plan—either through their own employers or their spouses' employers—before they retire.

For more key facts and positions on retirement, please see http://www.ici.org/retirement.