Four Views of Retirement Preparation

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What fraction of the American population is (or will be) adequately prepared for retirement?

a. 50%
b. 65%
c. 70%
d. 80%
e. 95%
f. All of the above

Welcome to the retirement security debate in America!
A time-value-of-money problem

All adequacy models are, in the end, a time-value-of-money problem, projecting today into the future.

- **POPULATION**: There are usually two (or segments thereof)
- **DATA**: Some very good; some surprisingly bad
- **FORECAST METHODOLOGY**: Many plausible assumptions; a few heroic
- **MEASURE OF OUTCOMES**: Relative v. absolute
Four papers, four questions

**Working-age Americans**

1. (NRRI) Will working-age Americans be ready for retirement at age 65?
   …40+ year forecast

2. (EBRI) Will working-age Americans have enough to pay for living expenses and health care through retirement?
   …70+ year forecast

**Older Americans**

3. (H&R) Do older Americans have enough to finance their current standard of living for the rest of their lives?
   …+30+ year forecast

4. (S&S) Have older Americans made economically reasonable tradeoffs between savings and consumption throughout their lives?
   …+70 year forecast
Semi-heroic assumptions

**All studies**
- The forecast horizons involved suggest caution in interpretation

**NRRI**
- Beautiful data on wealth – but not so much on savings
- So how to predict future wealth?
- An imperfect answer: “Your (grand)father’s retirement”

**S&S**
- Beautiful lifecycle model – taking Social Security lifetime earnings, estimating “optimal” future wealth, and comparing with actual
- Conclusion: most Americans optimize the choices they’ve faced
- But is playing well with the cards you are dealt—is that what we mean by retirement security?
One other major assumption – how we spend in retirement

Pragmatists View

I need to maintain my standard of living in retirement

Economists View

I should spend a bit more today and less tomorrow – given the risk of dying
Two different views

- Conventional view
- Lifecycle model

Optimal retirement spending (real $$) vs. Age
Working-age Americans: two models, one result (with rounding)

Source: NRRI, EBRI estimates with rounding.
Older Americans – two models, somewhat varied results

Source: H&R, S&S estimates with rounding.
Sensitivity analysis—relaxing the outcome measure

NRRI +
EBRI +
H&R +
S&S +

Source: estimates with rounding (author calculations)
What to conclude?

1. **At least 50% of Americans are (or will be) prepared for retirement**
   - We can reject the hypothesis that “most or all Americans are ill prepared”
   - Who are these households?
     - Higher income and better educated
     - Access and use of workplace retirement plans
     - Better planning skills (low discounters)
   - All of these characteristics contribute to ability to accumulate private savings/benefits, which is a precondition of retirement security in the U.S.
What to conclude?

2. At least 20% of Americans are ill-prepared for retirement

• The formal range of estimates is probably anywhere from 5% to 35%. Let’s use 20% as a naïve estimate.

• Who are these households?
  – Low income and lower levels of education
  – No access or limited use to workplace retirement plans
  – Perhaps those with low planning skills

• Financial vulnerability in one’s working years persists into retirement (Haveman, Holden, Wolfe, Romanov, 2007)

• One common point of agreement is that, for this group, improving adequacy is likely to come through public programs
What to conclude?

3. The question remains—what about the other 30%?

• Are they ill-prepared, fully prepared—or something in between?

• Who are these households? Certainly lower income and education

• Questions remain about the interplay of income, education, retirement plan access and planning skills
  – Will recent innovations in private DC design reach this group?
  – Is there sufficient coverage?
  – What is the relative reach of private v. public action to improve adequacy?
A final observation

• Let’s move beyond “bi-polar” characterizations of retirement security

• It’s better to think in a more differentiated way—especially given wide differences in lifetime incomes, education, planning skills, and the resultant accumulation of private wealth

• More attention should focus on defining the size of the ill-prepared and partially prepared groups, and the relative role that private versus public resources should be expected to play
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