

# The Impending Retirement Crisis

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In recent years, numerous significant economic and demographic shifts have made it increasingly difficult for individuals to save for retirement. Today, a retirement crisis is looming as millions of Americans are financially unprepared to continue to support their current lifestyle throughout their years in retirement. In fact, according to the National Retirement Risk Index, nearly one-half of all working-age households in America will be unable to afford the same lifestyle after retirement that they have been enjoying prior to retirement. While various trends have contributed to this lack of financial preparation, there are solutions that offer hope.

In order to develop solutions that can help mitigate the negative effects of the impending retirement crisis, it is important to understand the problem at-hand. One significant metric to consider is the household wealth-to-income ratio over the past few decades. Data collected from 1983 to 2013 reveals that the amount of wealth relative to income has remained surprisingly constant over the past three decades. At surface-level this trend may appear to be a positive sign, but in reality a variety of economic and demographic shifts over the past three decades have made it necessary for households to save more in anticipation of retirement. However, as indicated by the historic wealth-to-income ratios, the lack of increased levels of savings by American households presents a major problem.

So why exactly have retirement income needs increased? The first factor to consider is the demographic factor of increasing life expectancies. In 1960, the average sixty-year-old male was expected to live thirteen more years. Today, that number has increased to twenty, meaning the average length of an American male's time in retirement has increased by seven years. This trend of rising life expectancies also pertains to females, and since the retirement period has become longer, on average, for all Americans, it is important for savings to increase accordingly.

Another factor to take into consideration is that over the past few decades, medical costs such as premiums, deductibles, and co-payments have become significantly more expensive for individuals in

retirement. Even though Medicare offers retirees health insurance coverage, statistics show that medical expenses amount to approximately twenty percent of retirement income.

The rising need for additional retirement income, however, is only one part of the problem. Another dynamic to the retirement crisis is a decrease in the amounts provided by the major sources of retirement income: Social Security and employer-sponsored retirement plans.

With regard to Social Security, perhaps the most significant development has been the gradual increase of the Full Retirement Age (FRA) from sixty-five to sixty-seven. The result of this transition has been lower monthly payouts to individuals who retire at sixty-five and fewer years of payouts for individuals retiring at sixty-seven years old. Additionally, Social Security benefits are growing more slowly than Medicare premiums. This has made it increasingly difficult for retirees to afford Medicare. Finally, current law mandates that personal income tax apply to individuals' Social Security benefits. Specifically, Social Security recipients with an income greater than \$25,000 and married couples whose income totals more than \$32,000 are subject to personal income taxes on up to eighty-five percent of their Social Security benefits.

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The other major source of retirement income for Americans is employer-sponsored retirement plans. Historically, a mere fifty percent of working-age Americans in the private sector have been involved in employer-sponsored programs. Not only does this mean that those who are not involved are more likely to rely solely on Social Security benefits in their years of retirement, but even those participating in employer-sponsored retirement plans are facing difficult trends. The overwhelming shift from defined benefit (pension) plans to 401(k)s has been problematic because of the participants' insufficient level of contributions to 401(k)s. Specifically, employee contribution rates, on average, have not sufficiently met their retirement needs. In fact, only ten percent of employees with retirement programs make the maximum contribution allowed. Additionally, an average of 1.5 percent of the total value of individuals' 401(k)s are lost every year "when participants cash out as they change jobs, take hardship withdrawals, withdraw funds after age 59½, or default on loans." Ultimately, the ineffectiveness of 401(k)s has resulted in less retirement income for participants and thus made it even harder for retirees to live comfortably.

Despite the unfortunate situation many working-age Americans will face upon retirement, there are steps that can be taken now to ensure a more financially secure retirement. In fact, the solutions are not only in the hands of policymakers, but are also in the hands of the working-age individual in the midst of a retirement crisis.

First, working-age Americans should consider working longer, perhaps even to the age of seventy. By delaying their retirement, individuals reap the benefits of increased monthly Social Security benefits. For every year an individual delays their retirement, monthly Social Security benefits during retirement increase by approximately eight percent. Moreover, opting to retire at the age of seventy as opposed to sixty-two results in a seventy-six percent increase in monthly benefits. Though retiring at a later age increases one's retirement income significantly, not everyone will be capable of working to the age of seventy. Therefore, another solution for individuals is to save more.

While saving is not always easy given households' different spending needs, it is a habit that can help alleviate the financial difficulties that often arise upon retirement. Contributing the maximum allowed to employer-sponsored retirement plans, as well as to IRAs, can provide a working-age individual with \$23,500 of additional savings if less than fifty years old to as much as \$30,500 for those over fifty each year.

Ultimately, the impending retirement crisis in America presents a major challenge to millions of working-age Americans. Despite the unfortunate circumstances that exist today, it is important for these at-risk individuals to take action. Whether this means working longer or saving more, individuals should consider all options in order to enjoy a more comfortable and financially-stable retirement.

(This article was adapted from *Falling Short: The Coming Retirement Crisis and What to Do About It*, by Charles D. Ellis, Alicia H. Munnell, and Andrew D. Eschtruth.)