Article from:

# The Actuary Magazine

April/May 2010 – Volume 7 Issue 2

# Retirement

# SURVEY SAID

## LESS CHANGE THAN EXPECTED

2

3

4

BY ANNA M. RAPPAPORT

**MANY PEOPLE were recently surveyed about their perception of retirement risk. The top answers are in the article below.**

The Society of Actuaries has had an active program of research on retirement issues for many years. About 15 years ago, a number of SOA members became concerned that not enough attention was being focused on the post-retirement period and how resources are managed after retirement. As a result, a multifaceted approach to understanding post-retirement risks, including a series of biennial surveys focusing on public knowledge about post-retirement risk, started in 2001. This article provides perspective on the results of the 2009 survey and how the results relate to the four prior surveys.

The 2009 survey was fielded in July, 2009 and the survey instrument was developed in the spring of 2009. During that period, the economic crisis dominated public thinking about retirement and how it might affect planning for retirement and actions with regard to retirement. Understanding the implications of the economic crisis on risk management and perception was a major focus of the 2009 survey. The move to promote for health care reform was also an important agenda item in national public policy, and while it was not a specific focus of the survey, results need to be interpreted considering that health care is an important issue for retirees and preretirees, and that health care reform potentially will change the options available to them.

## CONCLUSIONS DRAWN ABOUT THE RESULTS

The oversight group to the study working with Ruth Helman, the lead researcher on the project from Mathew Greenwald & Associates, formulated several important conclusions as they thought about the study results:

- Misperceptions still exist after more than 20 years' experience with 401(k) plans and IRAs. Employee education has not had a big impact on these misperceptions.
- It is unclear if the economic downturn will lead to better management and planning.
- Longer-term risk management is very difficult for individuals, as is longer-term planning.
- Few workers are prepared for the risk of a sudden and unplanned early retirement. Yet over the long

run more than four in 10 workers retire before they planned to.

- There is a low appetite for guaranteed income products and a persistent feeling that people can do it on their own.
- Widows and the very old will continue to be vulnerable.
- A strong retirement system must include programs that work effectively for individuals who do not have personal initiatives to build savings and use them well.
- Education is important, but it should not be the primary strategy to address misperceptions and gaps in knowledge, since there are limits on what it can accomplish.

## MY OBSERVATIONS ABOUT THE RESULTS

Even though respondents indicated that the financial crisis had indeed affected how well prepared they were for retirement, the 2009 survey did not show any major changes in the way the public views and plans for retirement. This was very surprising to me. When asked about what actions they had taken to manage risk, however, a higher percentage of the retirees than in prior years indicated that they had taken actions such as reducing spending. To sum up, it seemed that the crisis had impacted and worsened the financial status of retirees; they had already tried to cut back spending and made some other changes, but their view about how to manage risk had hardly changed.

**THE 2009 SURVEY DID NOT SHOW ANY MAJOR CHANGES IN THE WAY THE PUBLIC VIEWS AND PLANS FOR RETIREMENT.**

As in prior years, preretirees were much more concerned about risk than retirees. Preretiree perceptions also seem to be more subject to change based on economic circumstances than those of retirees. From 2001 to 2003, there were several adverse events including the September 11th terrorism attacks and bad market conditions. In reaction, risk perceptions of preretirees increased significantly, and then reverted back to 2001 levels. From 2007 to 2009, market conditions were very difficult, but there was not the same move in risk perceptions as in 2001 to 2003. However, both preretirees and retirees did become more concerned about inflation risk between these latest two surveys. Inflation has superseded health care risks as the top concern of both retirees and preretirees. Six in 10 retirees (58 percent *very* or *somewhat* concerned) and seven in 10 preretirees (71 percent) express concern that the value of their savings and investments might not keep pace with inflation.

While paying for health care and long-term care remain in the top three concerns, overall there was some drop-off in concern about paying for health care. This may have been related to the effort to reform health care financing.

Some of the biggest concerns among the actuaries working on these surveys are that there are gaps in knowledge, not enough focus on risk management, and too short a planning horizon. Nothing about the new results changes these concerns from my perspective.

In the last two years, I have become very concerned about focus on home equity in retirement planning and the importance of home equity. Other SOA research shows that for middle Americans nearing retirement age, nonfinancial assets, primarily home equity, account for about 70 percent of assets (excluding the value of pensions and Social Security). The new survey asks respondents about their use of home equity as part of their retirement plan. The results show that while home equity may be used to finance retirement when all other options are exhausted, few plan to use equity in their home to finance their retirement. Just one in 10 retiree (11 percent) and two in 10 preretiree (20 percent) homeowners plan to use any of their home equity to help finance their retirement. Only 6 percent of retirees report they have already tapped into their home equity.

While actuaries have often been concerned that retirement ages need to adjust to increasing life spans, and while there have been recent modest increases in labor force participation rates at higher ages, nothing in the study indicates a real change in expectations about retirement ages. As in prior years, preretirees expect to retire at much higher ages than retirees. The majority of retirees in this study report they retired before the age of 65 (80 percent), with one-third having retired before the age of 55 (28 percent). However, half of preretirees indicating that retirement applies to them say they expect to retire at age 65 or later (51 percent). As in the prior studies, a sizeable proportion of preretirees state that retirement will not really apply to them (29 percent). Many of these preretirees say they will never be financially able to retire (31 percent) or they will choose to continue working (23 percent).

Other research has indicated that many people do not focus well on the long term, so the planning horizon has become a major concern. This study indicates that retirees look a median of just five years into the future when making important financial decisions. Preretirees have a slightly longer median planning horizon of 10 years.

Defined benefit plans are in decline but they remain important to today's retirees and those people who will be retiring in the near future. While similar proportions of retirees and pre-retirees received or expect to receive income or money from defined benefit plans (61 percent of retirees, 58 percent of preretirees), significantly more preretirees receive or expect to receive money from an employer's retirement savings plan, such as a 401(k) (42 percent of retirees, 76 percent of preretirees). The percentage receiving money from defined benefit plans seems high to some people who are focused on how the retirement system is changing, but for today's retirees, it makes sense. It is consistent with findings presented at the 2009 Social Security retirement research conference based on analysis of the Health and Retirement Survey.

## RISK MANAGEMENT FINDINGS FROM THE 2009 STUDY

Risk management was an area of major focus for the 2009 study. Retirees and preretirees continue to try to protect themselves against financial risks by decreasing debt, increasing savings, and cutting back on spending. Eight in 10 retirees (81 percent) and nine in 10 preretirees (90 percent) indicate they have eliminated or plan to eliminate all of their consumer debt, while eight in 10 have paid off or plan to pay off their mortgage (77 percent of retirees and 80 percent of preretirees). Three-quarters of retirees (75 percent) and almost nine in 10 preretirees (85 percent) say they save or intend to save as much as they can. Large majorities also say they have or intend to cut back on spending (68 percent and 78 percent).

Most retirees and preretirees purchase products to help ensure they can pay for adequate health care. Three-quarters of retirees (76 percent) and preretirees (74 percent) indicate they have or plan to purchase health insurance to supplement Medicare or participate in an employer-provided retiree health plan. Retirees and preretirees also recognize the role their own behaviors play in managing health care risk. Virtually all (93 percent each) report they maintain or plan to maintain healthy lifestyle habits, such as a proper diet, regular exercise and preventative care. Some of the oversight group members think that people say they are more active in maintaining health than they actually are. A special report to be issued later in 2010 will focus on risk management and the findings of the 2009 survey.

## ADDING SOME PERSPECTIVE AS WE THINK ABOUT THE ECONOMIC CRISIS AND THE RESULTS

It has been well documented that the economic crisis had a significant impact on personal retiree wealth, and particularly 401(k) balances by early 2009. That does not mean the impact will be long-lasting, but for some who changed direction, it will be. In this study, two-thirds of retirees (66 percent) and eight in 10 preretirees (79 percent) report the recent stock market and economic downturn has affected their financial concerns about retirement. Similar proportions of retirees (63 percent) and preretirees (77 percent) also say their finances have been negatively impacted by the downturn. Both retirees and preretirees say the downturn has made them feel as though they need to save more money (49 percent of retirees, 72 percent of preretirees), do a better job of managing their finances or planning for retirement (51 percent, 61 percent), and go back to work or work longer (23 percent, 64 percent). Nevertheless, it is unclear if the economic downturn will lead to actual changes in behavior, or better retirement management and planning. While retirees and preretirees may feel they need to make these changes, few appear to have made plans to do so. For example, the proportions of retirees and preretirees who plan to save as much money as they can and work

**… NOTHING IN THE STUDY INDICATES A REAL CHANGE IN EXPECTATIONS ABOUT RETIREMENT AGES.**

longer are statistically unchanged from their 2007 levels. And despite the economic downturn, the study saw few measurable changes in attitudes and behaviors between 2007 and 2009.

One of the frequent comments made during and after the worst part of the economic crisis is that people will need to work longer, and that it will be vital for people to retire later. I also heard anecdotally from diverse sources that people who could were postponing retirement, and that companies had seen a real slowdown in retirements. As discussed above, the retirees retired quite early, and preretirees plan to retire much later than the retirees. The 2009 and 2007 surveys asked questions about what the impact of delaying retirement for three years would be/would have been. The two studies show similar results with the 2009 study showing a modestly greater impact, indicating that most people underestimate what the impact of retiring later would be. However, overall respondents strongly understand the importance of continuing employer health benefits. It is also widely believed that many people will not be able to afford to retire. Presently, over the long term, about four in 10 end up retiring before they planned to, often due to job loss, health and family issues. It is unclear whether the aftermath of the economic crisis will be later retirement, and the 2009 risk survey provides no evidence that it will be.

**ONE OF THE FREQUENT COMMENTS MADE DURING AND AFTER THE WORST PART OF THE ECONOMIC CRISIS IS THAT PEOPLE WILL NEED TO WORK LONGER. …**

Unlike the 2009 Risk Survey, other studies showed big shifts in confidence with regard to retirement issues. The 2009 EBRI Retirement Confidence, for which the fieldwork was done in January, showed a big drop in confidence. The SOA's study done with LIMRA and INFRE, "What a Difference a Year Makes," for which the field work was done in April, also showed a big difference. However, this study and the EBRI Health Confidence Study for which the field work was done mid-year, did not show such changes. How can this be explained?

The Yale University School of Management publishes a "crash confidence index," for individuals and institutions which shows "confidence that there will be no stock market crash in the succeeding six months. …" (*http://icf.som.yale.edu/confidence.index/CrashIndex.shtml#data*). According to this data, confidence was very low from November 2008 to May 2009, and by July, individual confidence was up a great deal.

On his Web site, Yale economist Robert Shiller offers us insights on the topic of confidence:

> "Unemployment, GDP, manufacturing statistics—what's the best way to tell that we're headed into an economic recovery? According to Yale economist Robert Shiller, the answer might lie less in the metrics we use to measure economic production than it is in our own minds.
>
> "In a *New York Times* column, Shiller says that supposedly key economic indicators like unemployment or retail sales figures aren't causes of a recovery, but symptoms of one. 'For a fuller explanation, look beyond the traditional economic links and think of the world economy as driven by social epidemics, contagion of ideas and huge feedback loops that gradually change world views,' he writes. 'These social epidemics can travel as swiftly as swine flu: both spread from person to person and can reach every corner of the world in short order.'
>
> "When stocks fall, he says, stories pop up in the media about the declines, 'remind[ing] people of longstanding pessimistic stories and theories. These stories, newly prominent in their minds, incline them toward gloomy intuitive assessments.' That leads to more negative news stories, which leads to further declines, and the cycle continues, he says. The same thing happens, in the opposite direction, when stocks are rising." (*http://theguruinvestor.com/2009/09/01/shiller-the-recoverys-in-our-minds-not-our-metrics/*)

I was very puzzled at first by the results of the survey, particularly when looked at together with the earlier work, but this explanation seemed to make a lot of sense to me.

The risk survey report and related reports can be found at: *www.soa.org.* A

**Anna M. Rappaport, FSA, MAAA,** of Anna Rappaport Consulting, chairs the Society of Actuaries Committee on Post-Retirement Needs and Risks and is a past president of the Society of Actuaries.

The Risk Survey is conducted for the Society of Actuaries by Mathew Greenwald & Associates with assistance from EBRI.