Center for American Progress

Keep Calm and Muddle Through

Ignoring the Retirement Crisis Leaves Middle-Class Americans with Little Economic Control in Their Golden Years

By Christian E. Weller and David Madland August 2014

Introduction and summary

Every American has his or her own vision of what retirement should look like.[1] It is clear, however, that everyone shares one view in common: They all want to control their own economic destinies when retired. They want to remain productive in some form as they age. They want to continue to work, albeit with more flexible schedules and possibly for different employers. They want to volunteer; they want to take care of family members and friends who need help, such as aging parents, grandchildren, and sick relatives or neighbors; and they want to start their own businesses, an action that would give their tremendous experience a new platform for innovation and economic activity.[2] These hopes and aspirations require a lot of savings, as people of retirement age typically also want to stop working full time for an employer and a regular paycheck—the stage known as career employment.

However, people want to be sure that they can pay their bills before they pursue their aspirations and goals. They still need to pay for housing, health care, utilities, food, and other necessities after their paychecks stop coming, often for uncertain and potentially extended periods of time. One estimate suggests that people will need hundreds of thousands of dollars in savings just to pay for health care.[3] Most people find daunting the amount of savings necessary to maintain just their standards of living in retirement, never mind the extra money they would need to save to start a business.

The academic research on retirement income adequacy—whether people have enough money to retire—comes to varied conclusions. Much of it finds that a large minority, and possibly even a majority, of households will not have enough money set aside for retirement.[4] That is, people will have to cut back on their dreams, their consumption, and their time in retirement, perhaps by working in their current jobs longer than they had anticipated. In fact, studies that conclude that the overwhelming share of households are adequately prepared for retirement rest heavily on the assumption that retirees can and will make adjustments to their standards of living by working longer, spending less, and gaining access to public assistance.[5] Put differently, assuming that households want to be in economic control of their retirement identifies a serious savings shortfall, while elevating "muddling through" as a guiding principle for retirement policy leaves only a small share of retirees with serious savings shortfalls.

Unsurprisingly, retirement worries rank as one of Americans' top economic concerns.[6] This suggests that people prefer to have a good sense of financial control over how their retirement will look than to muddle through by relying on government assistance and help from friends and family members, working odd jobs, and cutting back on critical consumption such as health care. Policymakers have recently taken notice, putting forward proposals to improve retirement income security by, for example, boosting Social Security benefits. This would make it easier for people to save, as well as lower the costs of saving.[7]

A review of the research reveals the following:

- **Muddling through retirement papers over a growing crisis.** Older households use a number of different approaches to compensate for inadequate savings. They rely on public assistance programs; benefit from the generosity of family and friends; stay in unsuitable jobs due to ailing health and other reasons; and cut their consumption of basic necessities, leading to hardships. These approaches allow older households to make ends meet, but they also do nothing to address the growing shortfalls of retirement savings.

- **Inadequate savings could slow economic growth.** Inadequate savings could translate into less consumption and contribute to slower economic growth. If older workers get locked into unsuitable jobs, productivity may be lowered to the extent that it is below where it otherwise would be for employers. Lower productivity growth also means less economic growth. Moreover, by getting locked into unsuitable jobs, older workers are not pursuing employment and volunteer opportunities better suited to their needs and skills. These unpursued opportunities are losses to the economy and society and possibly slow economic growth even further.

- **Wealth growth has not kept pace with the need for more wealth.** Wealth-to-income ratios—which set the amount of total household assets minus debt relative to households' current income and are key indicators of retirement preparedness—have not markedly risen over the past three decades. The need for wealth, meanwhile, has clearly grown. People are expected to live longer, Social Security benefits are scheduled to grow more slowly as the full-benefit age rises from age 65 to age 67, and financial and labor-market risks have increased. Households need more money than in the past to cover these additional costs and maintain their standards of living in retirement, but wealth-to-income has not noticeably and consistently grown along with household incomes during this time. That is, today's near retirees will likely have to make more ad hoc adjustments, muddling through their retirement more than previous generations of near retirees.

- **Few people feel confident about their retirement prospects.** Most people do not feel very confident about their ability to maintain a previous standard of living in retirement or to pay for basic expenses for more than two decades. In 2014, only 18 percent of preretirees felt very confident that they would have the resources necessary to maintain their standards of living after they retired. This lack of confidence indicates that many households worry about losing control over their economic security in retirement.

- **Most households are at risk of having to scale back their living expenses in retirement.** Under somewhat optimistic assumptions, an estimated 53 percent of working-age households in 2010 were not expected to have enough future income from Social Security; defined benefit, or DB, pensions; and private savings to maintain their standards of living in retirement. This calculation, however, assumes that retirees will convert all of their home equity to cash through reverse mortgages. Allowing for more realistic, pessimistic assumptions quickly increases the shortfalls in retirement savings.

- **Retirement savings shortfalls vary expectedly across subpopulations.** Nonwhite households, single women, and households with less education are much more likely than whites, single men, and households with more education to be inadequately prepared for retirement.

- **Painting a much rosier picture of retirement preparedness assumes that retirees will somehow muddle through retirement.** Much smaller retirement income shortfalls typically assume that workers will somehow cut spending when retired, that people will delay or abandon their retirement plans, and that many households will rely on public assistance and help from friends and family members.

- **Policy can strengthen retirement preparedness.** Previous generations were better prepared for retirement than current generations in part because today's working-age households have not increased their savings enough to compensate for slower growth in Social Security benefits, disappearing defined benefit pension, or DB pensions, and rising financial risk exposure. Policymakers should make it easier for people to save, strengthen savings incentives, and help households better manage their investments.

The share of inadequately prepared households rose from 31 percent of working-age households in 1983 to 53 percent in 2010. This again reflects the fact that wealth to income has not measurably increased as the costs of retirement have gone up for all households. Indeed, the data show that most households struggle with and worry about getting ready for a retirement that allows them to retain economic control over their lives. Giving up that control and instead deciding to rely on public assistance, delay or abandon postretirement plans, and curtail living standards is one option to make the retirement crisis disappear. However, a preferable alternative first step would be to help more people save more money and keep more of that money for retirement. CAP has already proposed a number of ways this could happen in previous work, including through more efficient tax incentives,[8] new low-cost, low-risk savings vehicles,[9] and better disclosure of the fees and risks associated with retirement savings.[10] Although the growing retirement crisis requires large, decisive, and comprehensive efforts, each small step taken will help address the crisis. Hoping that future retirees will somehow manage to muddle through is not an acceptable path forward.

The Center for American Progress is a nonpartisan research and educational institute dedicated to promoting a strong, just and free America that ensures opportunity for all. We believe that Americans are bound together by a common commitment to these values and we aspire to ensure that our national policies reflect these values. We work to find progressive and pragmatic solutions to significant domestic and international problems and develop policy proposals that foster a government that is "of the people, by the people, and for the people."

Center for American Progress

1333 H STREET, NW, 10TH FLOOR, WASHINGTON, DC 20005 • TEL: 202-682-1611 • FAX: 202-682-1867 • WWW.AMERICANPROGRESS.ORG