Managing the Nest Egg Through Retirement:

How Do US Households Manage Assets and Income in Retirement?

by

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Abstract: The US retirement system is comprised of several components that together accrue resources throughout households' working careers to provide for income, health care, and shelter in retirement. This paper investigates how households manage and rely on the multiple components as they progress through their retirement years using three data collections: The IRA Investor Database™, the Federal Reserve Board Survey of Consumer Finances (SCF), and the Health and Retirement Study (HRS). Specifically, this research explores not only how households are managing specific components of their retirement accumulations, but the role of Social Security wealth in households' evolving balance sheets as well. As part of this work, a measure of augmented wealth will be created for each household. Augmented wealth includes consistent measures of Social Security wealth and defined benefit (DB) pension wealth, in addition to usual household balance sheet assets (retirement accounts, net home equity, and other assets). By and large, the US system typically provides resources as people age so that they can maintain their standard of living. Nevertheless, there is a range of experiences in retirement and this research will document where challenges exist and contribute insights to help address these challenges.

Extended Abstract

In part because the US retirement system has multiple components, there has been debate as to whether each separate component of the system is performing adequately. While it is generally acknowledged that households rely to differing degrees on the specific components of the US retirement system, whether the components together succeed in supporting pre-retirement standards of living continues to be a matter of debate. Some studies have raised concerns that large percentages of the US population are saving and investing too little for retirement, these studies often emphasize risks of shocks to households (Munnell, Hou, and Sanzenbacher 2018). Other research suggests that Americans generally are on track to maintain their standard of living in retirement (Scholz, Seshadri, and Khitatrakun 2006; Brady 2016). Focusing on the evolution of wealth in retirement, recent research finds that households at risk of financial difficulty in late retirement typically experienced financial difficulty before retirement (Poterba, Venti, and Wise 2018).

In fact, a side effect of the diversity across households' use of retirement resource components is the challenge to determine whether the system *as a whole* is adequate. The challenge is not unlike the traditional parable wherein several blind people attempt to reconcile disparate facts about elephants, based on their limited and differing understanding of individual features of the elephant.[1] Much as in the parable, reconciling disparate facts about attributes of a complex retirement system requires a broader and comprehensive perspective.

This paper investigates how households manage and rely on the multiple retirement resource components as they progress through their retirement years using three data collections: The IRA Investor Database™,[2] the Federal Reserve Board Survey of Consumer Finances (SCF),[3] and the Health and Retirement Study (HRS).[4] The three datasets work together to offer this comprehensive perspective.

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[1] The folk tale, from India, describes how several blind men argue about the attributes of an elephant, because they each know and emphasize only a little of what the elephant is and so cannot picture it, in its entirety. The parable is used in many contexts to teach and promote understanding, consistent with the goal of the research here. For a specific version of the parable and an example of how the parable is used see US Peace Corps 2019.

[2] The IRA Investor Database is a proprietary database maintained by the Investment Company Institute (see https://www.ici.org/research/investors/database).

[3] See Bricker et al. (2017) for discussion of the most recent update of the SCF data; and https://www.federalreserve.gov/econres/scfindex.htm.

[4] See http://hrsonline.isr.umich.edu/ for a description of the HRS and research using the HRS.

With these data, it is possible to investigate vulnerabilities of aging individuals as they near retirement and age onwards from there. The IRA Investor Database™ contains annual panel data at the account level from 2007 forward covering individual contributions, rollovers from employer-sponsored retirement plans (whether defined benefit [DB] or defined contribution [DC]), and investment allocations in IRAs.[5] The SCF contains detailed data on household finances, using a triennial cross-section design that consistently spans 1989 to 2016. The HRS data serve as a great complement to the SCF, targeting the US population aged 50 or older, over 1992 to 2016, with a biennial panel design. The HRS collects data from a large set of cohorts, with emphasis on cohorts born between 1931–1965. These data include information on health and assets, along with self-reported subjective measures of well-being and health status that can enhance understanding of how elders experience retirement.

Most notably, the HRS includes estimates of employer-sponsored DB pension wealth and estimates of Social Security wealth for each household. Estimates of Social Security wealth have been generated by two similar methods, by two teams of authors including Kapinos, et al. (2016), and Fang and Kapinos (2016). Other members of these two teams, Fang, Brown and Weir (2016) have produced estimates of cohort changes in Social Security and DB pension wealth and use somewhat different Social Security wealth measures as a part of that work.[6] Employer-sponsored DB pension wealth also has been estimated by Gustman, Steinmeier, and Tabatabai (2010a, 2010b, 2014a, 2014b). Each of these measures of Social Security wealth and DB pension wealth differ in their assumptions, target population, and ability to represent the US population over time.[7] None cover the most recent cohort additions to

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[5] For more on The IRA Investor Database™, see Holden and Bass (2018) and Holden and Schrass (2018).

[6] The work of this team differs from the work of previous related teams in several ways. For example, their measures include impacts of disability insurance uptake and feature enhanced private pension wealth data, among other changes. Because some of these changes work in opposite directions, it is difficult to isolate the impact of each of them.

[7] For example, Kapinos et al. (2016); Fang and Kapinos (2016); and Fang, Brown, and Weir (2016) all use somewhat different imputation methods and different assumptions for estimating Social Security wealth. The first two sets of these authors offer Social Security wealth estimates at various claiming ages, and for couples and for individuals, whereas the third set imputes only early retirement benefits at age 62 and only based on own work history. This is problematic. Consider just the switch to an early claiming assumption for results from imputations. The 2010 HRS birth cohorts that the third set of authors targets (aged 51–56 in 2010) varies in distance from the full retirement age because the full retirement age changes from age 66 for those born in 1954 (age 51) to age 66 and 10 months for those born in 1959 (age 56). As a result, a relative discount of 21 percent to Social Security wealth is imposed on 1959 birth cohorts in the Fang Brown and Weir (2017) treatment, that would not be imposed under a full retirement age assumption. The significance of this assumption is hard for a reader to observe however, because the 1959 birth cohort estimates are embedded in aggregated results.

the HRS. None consider how Social Security wealth evolves. As part of this research paper, previous methods and sample analyses will be compared to help reconcile results, with the new analysis using more recent data to bring the research up-to-date for an expanded sample of households.[8]

In summary, this research has two related goals. A first goal is to provide robust estimates of Social Security and DB pension wealth for more households, over more recent time periods. The second goal is to use the robust estimates to observe the evolution of these and other household resources over retirement.

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As another example, Gustman, Steinmeier, and Tabatabai (2014b); and Fang, Brown, and Weir (2016) differ in their inclusion of disability insurance recipients as part of their sample for estimating Social Security wealth, while both address economic consequences of the Great Recession. Neither piece distinguishes health from economic shocks. One piece, Seligman (2014) targets Social Security wealth impacts from the Great Recession separating out health and economic shocks. Seligman (2014) does not mix measures of other savings components, but unfortunately also does not address stabilizing aspects of the US system outside of Social Security such as home ownership, thus it also offers a less than complete look at the US system's stabilization components.

This paper addresses each of these issues methodically and incrementally.

[8] Much of the variation in previous estimates is a natural consequence of the fact that building estimates of the value of each component requires employing assumptions about longevity, interest rates, wage growth, and career lengths. While the HRS contains data, both in the public and restricted samples, that are helpful for this purpose, many options for underlying estimation exist, which need to be carefully considered and documented.

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