How Is the Economic Turmoil Affecting Older Americans?

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The slumping stock market, falling housing prices, and weakening economy have serious repercussions for the 94 million Americans age 50 and older who are approaching retirement or already retired. Retirement accounts lost about 18 percent of their value over the past 12 months, and between January 2007 and May 2008, housing prices fell from 4 to 20 percent depending on where seniors live. Older Americans have little time to recoup the values of their homes, 401(k) plans, and individual retirement accounts—all important parts of their retirement nest eggs. More and more older Americans are working to bolster their retirement incomes, but the rising unemployment rate, now 6.1 percent, limits their prospects. This fact sheet examines the impact of the ongoing economic turmoil on retirement savings, home values, and retirement decisions.

The Retirement Policy Program addresses how current and proposed retirement policies, demographic trends, and private-sector practices affect the well-being of older individuals, the economy, and government budgets.

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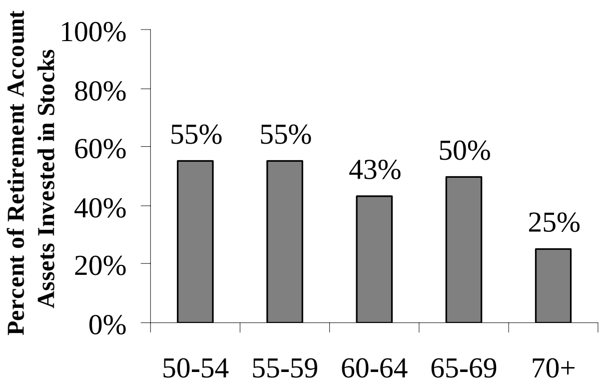
How Does the Financial Turmoil Affect Older Americans' Retirement Savings?

The stock market lost 27 percent of its value between September 30, 2007 and September 30, 2008, a roughly $7 trillion drop. The loss has reduced the retirement savings of many Americans, particularly older adults.

How Much of Older Adults' Retirement Accounts Is Invested in Stocks?

- Forty-nine percent of households ages 50 and older own retirement accounts. Seventy-nine percent of these accounts include stock holdings.
- The typical retirement account of households ages 50 and older invests 50 percent of its assets in stocks. However, households ages 70 and older hold much less in stocks, reducing their exposure to market fluctuations (figure 1).[1]

Figure 1. *Median Exposure to Stocks in Retirement Accounts, Households Ages 50 and Older with Retirement Accounts, by Age Group, 2004*



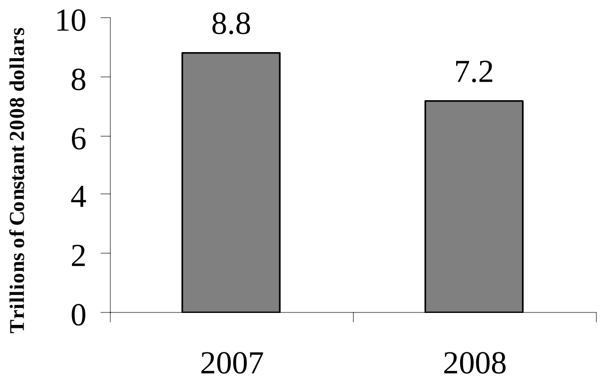
Source: Authors' calculations using the 2004 Survey of Consumer Finances.

How Much Have Retirement Accounts Fallen?

- During the past 12 months (from September 30, 2007, to September 30, 2008), retirement accounts have lost $1.6 trillion, 18.3 percent of their value (figure 2).[2]
- Households age 50 and older held $5.1 trillion in retirement accounts, which is 71.5 percent of all retirement account assets, on September 30, 2008.

[1] Some households also hold stocks outside of retirement accounts.
[2] Investor losses might be slightly higher, because IRS Form 5500 filings indicate that annual contributions to defined contribution plans exceed withdrawals by about 10 percent. This difference, however, amounted to less than 1 percent of assets in 2005 and 2006.

Figure 2. *Accumulations in Retirement Accounts, 2007 and 2008*

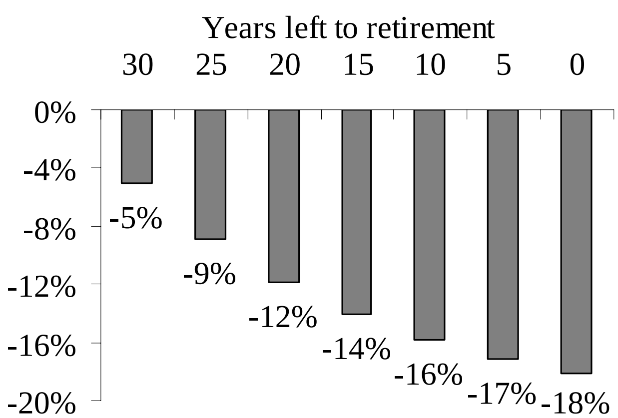


Source: Authors' calculations using data from the Board of Governors of the Federal Reserve System (2008).
Note: Estimates are for September 30 of each year, expressed in constant 2008 dollars.

How Are Different Age Groups Affected?

- An 18 percent loss disrupts retirement plans more for households nearing retirement than for those with many years before retirement, because younger households have more time to recover (figure 3). Consequently, people are commonly advised to reduce their stock holdings as they near retirement.

Figure 3. *Effect of an 18 Percent Decline in Retirement Accounts on Final Balance, by Years to Retirement*

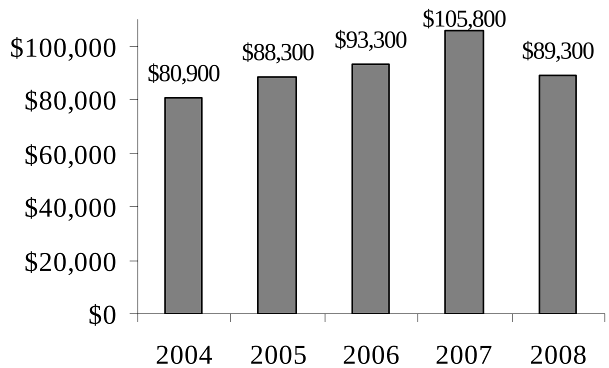


Source: Authors' illustration.
Note: Assumes a contribution rate of 10 percent of salary from age 30 to age 65 and a real rate of return on retirement assets of 5.5 percent, the expected long-term real return on a balanced portfolio.

How Much Do Households Hold in a Typical Retirement Account?

- The financial turbulence of the past year wiped out the gains from the 2005 to 2007 period. Today, the typical household age 50 and older with a retirement account holds a balance of $89,300, not enough to replace one year's pre-retirement income (figure 3).[3]

Figure 4. *Median Retirement Account Accumulation, Households Age 50 and Older, 2004 to 2008*



Source: Authors' calculations using data from the 2004 Survey of Consumer Finances and Board of Governors of the Federal Reserve System (2008).
Note: Estimates are for September 30 of each year, expressed in constant 2008 dollars. The starting point is the median account balance for households 50 and older in 2004. The calculations assume households hold a portfolio of 50 percent stocks and 50 percent in fixed-income instruments (which was the median allocation for the typical household ages 50 and older in 2004). Households are assumed to rebalance their portfolios at the end of the third quarter of each year to the 50-50 allocation. Annual changes are estimated using the gains/losses in stocks and bonds from the Flow of Funds Table L118c (defined contribution plans). Extrapolations to the third quarter are calculated using Table L118 (private pension plans) and the Russell 3000 index.

[3] A typical household age 50 to 59 with a retirement account has an income of $95,000.

How Will the Decline in Home Prices Affect Older Adults' Retirement Nest Eggs?

The drop in housing prices since 2007 could hurt older adults who count on home equity as an important part of their retirement nest eggs. Primarily affected will be those who plan to or need to tap into this asset to help finance retirement.

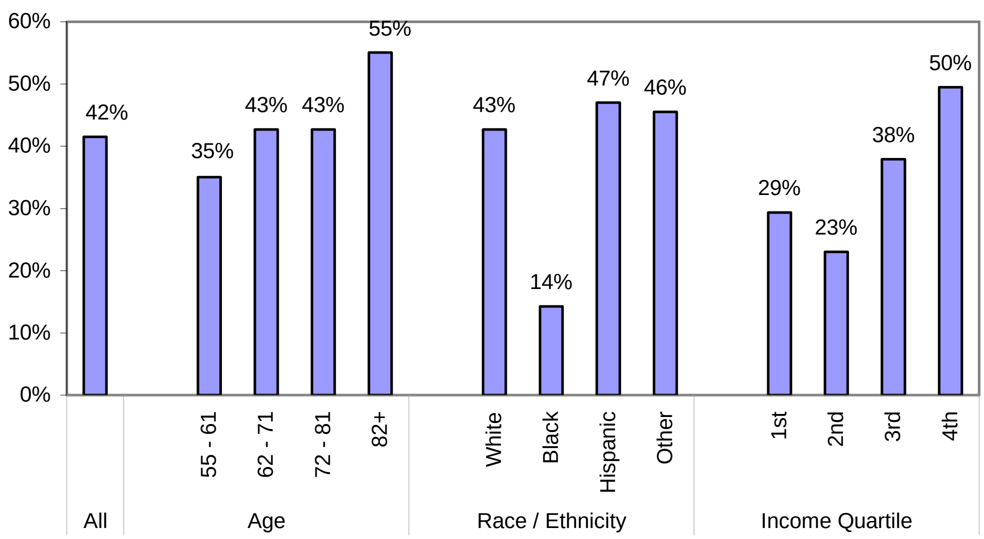
Does home equity represent a large share of older adults' wealth?

- In 2006, 77 percent of adults age 55 and older owned a home and 41 percent owned a home with no debt (Zedlewski, Cushing-Daniels, and Lewis 2008).
- Home equity (home value less mortgage debt) made up 29 percent of private wealth of adults age 57 to 61 in 2004 (Mermin 2008).

How has housing wealth changed for older adults?

- Despite big recent declines in home values, older adults have enjoyed a huge boon in housing values. Between 1998 and 2006, the inflation-adjusted median home equity for adults ages 55 and older increased by 41.5 percent (figure 5).

Figure 5
Inflation-Adjusted Growth in Median Home Equity: 1998-2006
Homeowners Ages 55 and Older



Source: Zedlewski, Cushing-Daniels, and Lewis (2008), based on Health and Retirement Study (HRS) data.
Notes: Includes all HRS home-owning households headed by an adult ages 55 and older.

- On average, home prices fell 3.9 percent across the United States from January 2007 to May 2008 (Office of Federal Housing Enterprise Oversight 2008), though the more oft-cited Standard and Poor's Case-Shiller Index indicates that home prices in 20 select metropolitan areas fell 16.7 percent over the same period.[4]

What is the importance of home equity in retirement?

- Historically, most retirees do not use housing wealth to finance living expenses in retirement (Venti and Wise 2004), but recent declines in retirement accounts (see page 2) may force more older adults to do so.
- Only 6 percent of homeowners age 50 to 65 report that they plan to use home equity to finance ordinary living expenses in retirement (Munnell, Soto, and Aubry 2007).
- If all homeowners age 62 and older took out reverse annuity mortgages (RAMs) and chose a lifetime annuity option, their median annual retirement income would increase by 18 percent based on 2006 home values (figure 6). A 10 percent home price decline would reduce this gain to 16 percent.

Figure 6
Potential Median Change in Income from Reverse Annuity Mortgages
Homeowners Age 62 and Older, 2006

Source: Zedlewski, Cushing-Daniels, and Lewis (2008), based on Health and Retirement Study (HRS) data.
Notes: Includes all HRS home-owning households headed by an adult age 55 and older.

[4] The OFHEO index covers the entire country but only includes houses financed with mortgage loans of $417,000 or less (representing about three-quarters of U.S. homes). The Case-Shiller Index focuses on larger cities, excludes 13 states, and includes subprime loans. The Case-Shiller Index weights transactions by value so it is particularly sensitive to changes in the most expensive homes and in the highest-priced markets.

- The potential for home equity to improve retirement security varies dramatically depending on age, race, and income level (figure 6). Black households have relatively low home-equity values and thus little to gain from RAMs. Also, gains increase with age because there is a shorter payout time for the annuity.

Are reverse annuity mortgages a good way to shore up retirement incomes?

- The downsides to using home equity to help finance retirement are the high administrative cost of taking out a loan (about 18 percent of the loan value for a 62-year-old) and the need to repay reverse annuity mortgages plus compounded interest when a senior wants to move.
- Seniors need better information about the pros and cons of these mortgages and other options for tapping into home equity. Seniors have not been immune to the subprime mortgage crisis; adults age 50 and older were 28 percent of all delinquencies and foreclosures by the end of 2007 (Shelton 2008).

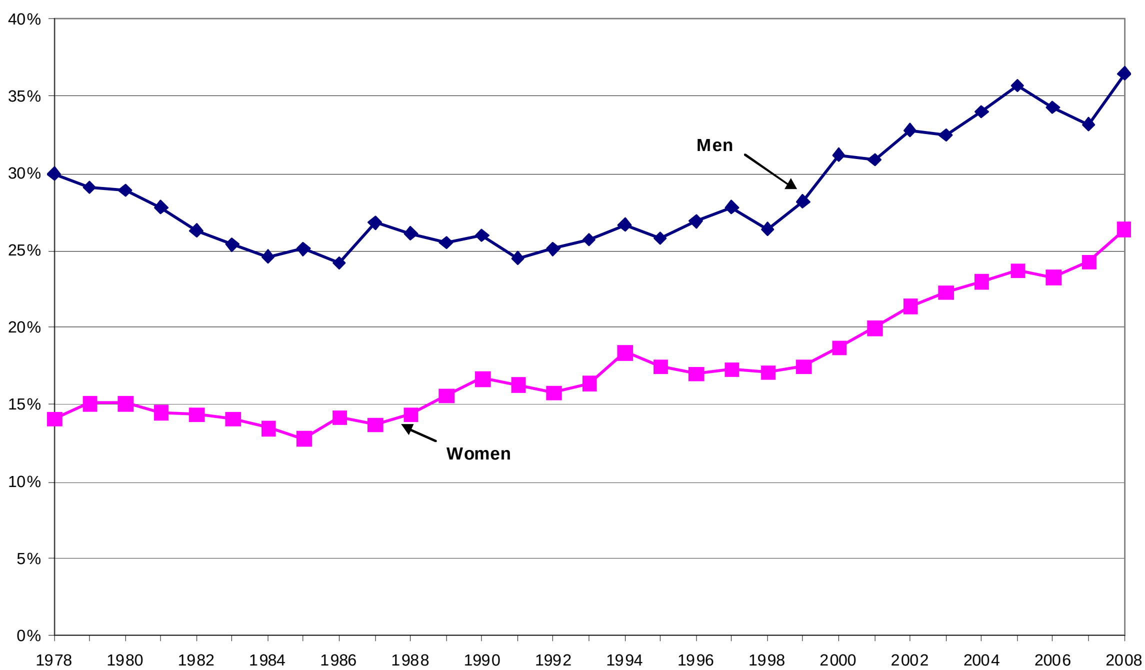
How Will the Financial Turmoil Affect Older Workers?

The plummeting value of retirement assets—housing, pensions, and other savings—could force more older adults to delay retirement and remain at work and could encourage some retirees to return to work. At the same time, contracting credit markets could weaken the labor market, limiting employment opportunities for older adults.

How will the financial crisis affect retirement decisions?

- The share of older adults working or looking for work is rising. Between August 1998 and August 2008, the labor force participation rate at age 65 to 69 increased from 26.4 to 36.5 percent for men and from 17.1 to 26.4 percent for women (figure 7). The housing and stock market slump will likely accelerate this trend.
- Many retirees may want to go back to work as their nest eggs disappear. In the 1990s and early 2000s, long before the current crisis hit, about a quarter of retirees returned to work (Maestas 2005).

Figure 7. Labor Force Participation Rates for Men and Women Ages 65 to 69, 1978-2008



Note: Estimates are for August of each year.
Source: BLS (2008b).

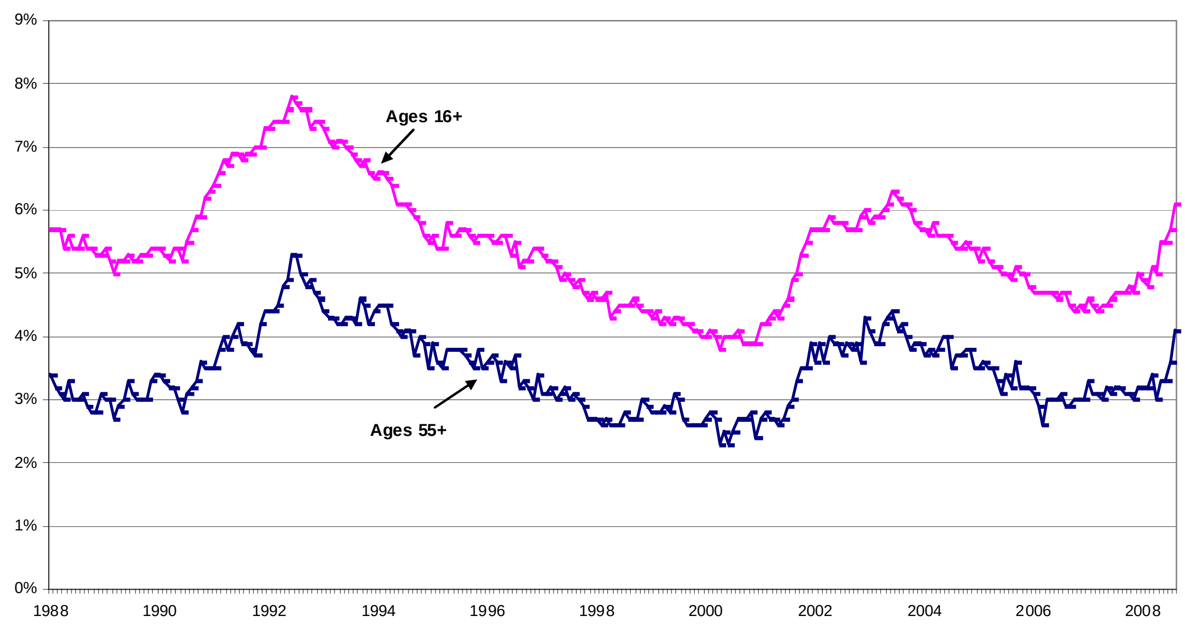
How will the credit crunch affect jobs?

- In September 2008, 6.1 percent of the labor force was unemployed (not working and looking for work), nearly a five-year high (figure 8).
- Partly because of the credit crisis, total nonfarm payroll employment has fallen every month since January 2008, a cumulative loss of 760,000 jobs this year through September (BLS 2008a).
- A continuing credit crunch will limit businesses' and consumers' ability to borrow, slowing economic growth and increasing unemployment.

Are older workers likely to lose their jobs?

- The unemployment rate for older adults consistently falls below the average for all adults (figure 8). In September 2008, 4.1 percent of adults age 55 and older were unemployed, compared with 5.2 percent of those age 25 to 54 and 13.2 percent of those age 16 to 24 (BLS 2008b). However, official statistics understate job loss at older ages because many older workers drop out of the labor force when they lose their jobs.
- Although few older workers are unemployed, many lose their jobs at some point late in their careers. Between 1992 and 2006, for example, 24 percent of full-time workers age 51 to 55 lost a job by age 65 to 69 because of a layoff or business closing (Johnson forthcoming).
- Unemployed seniors tend to spend more time out of work than their younger counterparts. In 2007, 24 percent of unemployed adults age 55 to 64 spent 27 or more weeks out of work, compared with 17 percent of unemployed adults age 25 to 34 (BLS 2008c).

Figure 8. Monthly Unemployment Rates for All Adults Ages 16 and Older and for Those Ages 55 and Older, Jan. 1988 to Sept. 2008



Source: BLS (2008b).

Will older adults find new jobs?

- Job losses this year have been concentrated in four industries: construction, manufacturing, retail trade, and professional and business services. The contraction of the retail sector will hit older workers hard because retail sales is the largest occupation for workers age 65 and older (Mermin, Johnson, and Toder 2008). Construction and manufacturing, by contrast, employ relatively few older workers.
- The financial services industry also employs many older workers. Although it has not shed many jobs yet this year, industry consolidation could cause substantial job losses in coming months.
- Historically, many workers become self-employed in their sixties, but the credit crunch could make it difficult for people to start and sustain small businesses. In 2006, 36.8 percent of employed men and 21.5 percent of employed women age 65 to 69 worked for themselves (Toder et al. 2008).
- Well-educated older workers face better job prospects than those with limited schooling. In 2006, 51.9 percent of men and 36.5 percent of women age 65 to 69 with college degrees were employed, compared with only 32.5 percent of men and 26.9 percent of women with no more than a high school diploma (Toder et al. 2008).

How does unemployment at older ages affect retirement income security?

- Unemployment at older ages can upend retirement planning. Most people save most in their fifties and sixties, when earnings tend to be high and childrearing expenses are winding down. Job losses reduce earnings that can be set aside for retirement and prevent people from contributing to their pensions or accumulating more Social Security credits.
- Median wages fall by 26 percent for older workers when they return to work after being laid off from jobs they held for 10 or more years (Johnson and Kawachi 2007).
- A job layoff in one’s fifties and sixties typically reduces total household wealth (excluding the value of future Social Security and pension benefits) by 21 percent for married people and 33 percent for single people (Johnson, Mermin, and Uccello 2006).
- On average, working an additional year increases annual retirement income by 9 percent (Butrica, Smith, and Steuerle 2006).

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