Retirement News Highlights
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Buck Up, Boomers. You're Still Better Off Than Your Parents.

By Allison Schrager | Bloomberg
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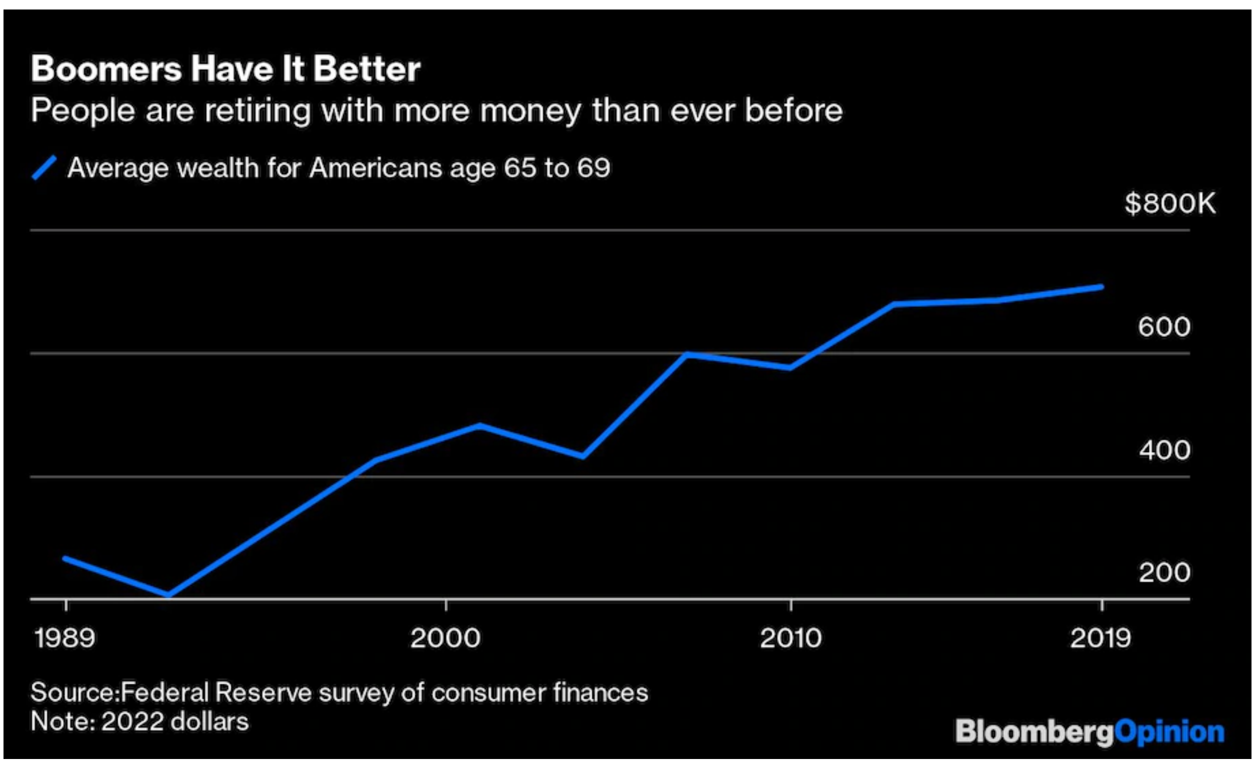
This is a hard time to retire. The market is down 7% from last year and the rate of inflation has risen to 8.5%. Both are brutal to your bottom line when you're on a fixed income. But buck up! As bad as things seem, odds are you are in better shape than your parents or grandparents were. And if they got through retirement comfortably, so will you.

If there were a golden age of retirement, it would be now. For most of human history, people worked until they were physically unable, and then spent the remainder of their lives either poor or dependent on family. This changed in the early to mid-20th century, when many economically developed countries adopted various pension programs that paid income through retirement. The U.S. pays Social Security benefits and also offers tax incentives for employers to offer retirement plans.

It's tempting to idealize the 1960s and '70s, when companies mainly offered traditional pension plans that paid a stable income until you died. But taking on all the market and longevity risk of workers was expensive for employers. Once companies were required to adequately fund their pensions to account for that risk, most dropped them. A notable exception is the public-sector employers who follow different accounting standards (that don't account for risk) and still offer traditional pensions.



But even at their peak, only about 38% of private-sector workers had a defined benefit plan, and many of them were higher earners, leaving most Americans to fend for themselves. When cheaper solutions became available — as in, defined contribution plans such as a 401(k) — retirement benefits became more common. In 2019 about 57% of U.S. workers had some form of a retirement plan.

Greater access to retirement accounts means people are retiring with more money than before. The figure below plots the average financial asset balance of Americans between age 65 and 69 from 1989 to 2019. This includes all retirement accounts, pension plans, bank accounts, stock portfolios and any other financial assets. Of course, many people still don't have access to retirement accounts through their jobs, or don't have extra income to save. But most retirees have a lot more money than they used to.

More money translates to more income in retirement. One study looked at the IRS records of 5% of retired Americans and estimated that income grew 10% to 12% for 70-year-olds in 2011 compared with 2000. Among 80-year-olds, income was about 5% higher in 2016 over 2010 at the median of the income distribution and 8% higher at the 75th percentile, but 0.8% lower for the bottom 25th. Overall, the data show people have more or almost the same income than previous cohorts of retirees.

Our government benefits are also worth much more now. When interest rates fall, as they have over the last 30 years, the value of low-risk income like Social Security increases. True, medical costs have risen, but that also reflects that health care has gotten much better at keeping us alive and improving our quality of life. Medicare has also become more generous: Consider, for example, the creation of the prescription drug benefit in 2003.

It's also true you can expect to live longer in retirement and that means your money has to last longer. But isn't that a good problem to have? You're probably healthier, too, than previous retirees at your age, which means you can do part-time work years into retirement if you need to improve your financial situation.

Before you get too confident, though, I have to add this caution: Retirement these days isn't easy. When you're living longer and don't want to run out of money before you dance your last dance, figuring out how much you can safely spend each year is a very difficult problem — especially when markets are volatile and inflation is high and unpredictable.

To make matters worse, the current conventional wisdom, such as the 4% rule or spending your Required Minimum Drawdown, would suggest you should pare back spending in an economy like we're having now. But that's easier said than done when your money will buy less with inflation at 8.5%, and many retirees are feeling ready to travel and socialize after years of pandemic isolation.

In finance, any strategy that forces you to cut spending at the worst possible time is considered a failure. Yet for some reason millions of retirees are advised to follow a strategy that does exactly that. So if you want to do better and don't want to buy an annuity with your savings, you need to be more strategic.

Divide your spending into wants and needs. Finance your needs (housing costs, food) with stable, inflation-protected income like Social Security or inflation-adjusted bonds. Then finance your wants based on how your risky assets are performing (a good investment choice would be cheap, well-diversified stock funds) and balance those decisions with your personal situation. If this is the year you feel you really need to take a vacation with your grandkids, so be it. You can at least rest assured that while you splurge, you've got your needs financed with low-risk assets, so you know you'll be OK in the future.

Defined contribution plans like your 401(k) have taken a lot of flak over the years, but they're the main reason many retirees will be better off compared with previous generations. That means that boomers enter retirement richer than previous generations but burdened with a very complex risk problem: how to spend that money. So if you want to fret about your retirement, fret about that — in times like these, the problem is harder to solve than ever.

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