

Retirement Behavior and the Global Financial Crisis

Jason J. Fichtner, John W.R. Phillips, and Barbara A. Smith

September 2011

PRC WP2011-10

Pension Research Council Working Paper

Pension Research Council

The Wharton School, University of Pennsylvania

3620 Locust Walk, 3000 SH-DH

Philadelphia, PA 19104-6302

Tel: 215.898.7620 Fax: 215.573.3418

Email: prc@wharton.upenn.edu

<http://www.pensionresearchcouncil.org>

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Abstract

Recent economic conditions have vastly changed the retirement landscape. Declines in assets as well as high unemployment changed the retirement plans of many Americans. Shocks to employment and wealth have likely influenced retirement behavior. This chapter provides a survey of the current literature on the influence of employment and wealth shocks on retirement and then makes use of administrative records on benefit applications to provide a preliminary analysis of changes in early retirement (age 62) claiming resulting from the recent economic downturn and implications. Since early claiming can have long lasting implications for retirement well being, we address how Americans learn about their retirement options.

Jason J. Fichtner

George Mason University

jfichtne@gmu.edu

John W.R. Phillips

National Institute on Aging

john.phillips@nih.gov

Barbara A. Smith

Social Security Administration

barbara.a.smith@ssa.gov

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Jason J. Fichtner and John W.R. Phillips

The financial crisis that began in 2008 resulted in a great and unanticipated loss of wealth for millions of people. The US stock market, as measured by the broad S&P 500 index, fell 56.7 percent from a peak on October 10, 2007 to a bottom on March 9, 2009.¹ Housing prices plummeted and unemployment rose quickly to double-digits. General confidence in the financial system was greatly weakened. Though the broad stock market has recovered much of its losses, housing prices remain low. Unemployment is still high, with unemployment rates for workers age 55-64 averaging 7 percent for the years 2009-2010 compared to 3 percent for the period 2005-2008 (BLS, 2011). Survey research suggests financial wealth declined by 15 percent for the median household as a result of the 2008 financial crisis (Shapiro, 2010).

These economic conditions have vastly changed the retirement landscape for millions of Americans, and have likely influenced retirement behavior. This chapter begins by providing a survey of the current literature on the influence of employment and wealth shocks on retirement. Next, we analyze administrative records from the Social Security Administration (SSA) on benefit applications to document the changes in retirement patterns resulting from the recent economic downturn and consider implications for retirement security. Given the importance that social security benefits play in the retirement security of millions of Americans, and the possibility that the financial crisis is affecting retirement decision, the chapter then addresses how SSA helps Americans prepare for retirement.

The effects of wealth and employment shocks on retirement behavior

The global financial crisis of 2008 and the resulting recession were notable for the speed at which the decline in financial markets, housing, and employment occurred. Also notable was the wide-spread nature of the economic crisis, affecting all ages and walks of life. According to data from the Health and Retirement Study (HRS), about 28 percent of HRS households reported that they had been affected ‘a lot’ by the financial crisis, 46 percent responded they had been affected ‘a little’, and only 26 percent reported not having been affected (Hurd and Rohwedder, 2010).

A sudden and unplanned drop in wealth and income can have significant effects on retirement behavior. Younger or middle-aged workers have more than a decade before retirement, and so they still have time to recover financial losses. Those post-retirement or near retirement are more limited in their ability to attain or maintain a secure retirement. For those current retirees, sudden declines in wealth from housing assets and financial portfolios might force immediate changes in consumption. For those near retirement, a financial crisis might also change the timing of retirement.² A financial shock, such as steep drops in the value of stock prices, investment portfolios, and housing assets might cause a delay in retirement plans, as a sudden loss in wealth causes people to remain in the workforce longer than planned and rebuild retirement saving (Bosworth and Burtless, 2010).

Research using the HRS data for 2008 and 2009 highlights the immediate impact of the financial crisis on retirement behavior (Hurd and Rohwedder, 2010).³ For those working in 2008, the authors compared data between the two survey years and found that in the 2009 HRS Internet survey, the average probability of those working past age 62 was 61.7 percent, up from 58.2 percent in the 2008 HRS. For those working in 2008, the average probability of working past age 65 increased from 38.6 percent to 46.4 percent (Hurd and Rohwedder, 2010). Thus these

results suggest that many are planning on working longer and retiring later as a result of the financial crisis, due to their sizeable losses in assets. These households responded in several ways: they reduced spending and with that increased saving, they intend to work longer, and anticipate bequeathing less. Data from the Federal Reserve support Hurd and Rohwedder's finding, reporting that since the financial crisis, the personal saving rate has trended upward from around 1 percent to around 6 percent (Glick and Lansing 2011). All else equal, a negative financial shock dictates that workers nearing retirement increase income and saving by remaining in the workforce or reduce planned consumption in retirement.⁴

The loss of a job can also affect retirement behavior. As Bosworth and Burtless (2010: 22) note: 'At ages past 60 and especially past 65 ... reduced employment levels caused by a weak job market very quickly translate into reduced labor force participation rates.' An employment shock, such as a sudden loss of a job and a labor market with high unemployment might hasten the decision on both when to retire and when to begin receiving social security benefits. As noted earlier, the unemployment rate for workers aged 55 to 64 has almost doubled during the recent recession. Also, older workers who lose their jobs are likely to have longer durations of unemployment than are younger workers. According to recent data from the U.S. Bureau of Labor Statistics, nearly half of workers aged 55 or older had been unemployed for 27 weeks or longer compared with 28 percent of workers aged 16 to 24 and 41 percent of workers aged 25 to 54 (BLS, 2010). And a Congressional Research Service study (CRS, 2007) found that older workers who are unemployed have a higher incidence of withdrawing from the labor market. When they do so, obvious sources of income are pensions and social security benefits. According to some studies, unemployment among older workers contributes significantly to the probability of retirement. All of these impacts will be amplified in the current recession. Though

the decision to start receiving social security benefits is often seen as being contemporaneous with retirement, electing to receive benefits is not necessarily a predictor of retirement or leaving the workforce (Bosworth and Burtless, 2010). In actuality, the decision on whether to stop work can be completely independent from the decision to begin collecting Social security benefits. For example, a worker might choose to completely exit the workforce and retire while delaying receipt of social security benefits, to take advantage of higher monthly benefit amounts that accrue the later one waits to claim (up to age 70). Or a worker might decide to elect retirement benefits as early as 62, receiving a smaller monthly benefit, yet continue to work full or part-time for continued income support.

The net effect of a financial crisis and recession on retirement behavior is ambiguous. While some workers will delay retirement, others will exit the workforce earlier due to job loss. Thus the decision to begin social security retirement benefits is intuitively correlated with leaving the workforce, but not necessarily. Accordingly, we might expect recessions to lead to an increase in those electing to begin receiving social security retirement benefits.

Researchers have long recognized the role social security benefits play in securing a dignified and secure retirement (Burkhauser et al., 2009). Social Security retirement benefits provide income security for millions of Americans, with 64 percent of all beneficiary units relying on social security for 50 percent or more of their income, and 34 percent relying on social security for 90 percent or more of their income (SSA, 2010*b*). Yet, because of the relatively larger importance of social security benefits for households at the lower end of the income and wealth distribution, the financial crisis has affected these retirees less (Hurd and Rohwedder, 2010).

Data to study the retirement and saving effects due to the global financial crisis of 2008 are just beginning to become available, so additional research is necessary to fully understand the story of how retirement behavior has changed as a result of the shocks to wealth and employment of the past few years.

Are people electing to claim social security benefits early due to the financial crisis? A preliminary look.

A relatively stable percentage of workers have elected to claim social security retirement benefits as soon as they become available, over the years (Muldoon and Kopcke, 2008). Annual data show that the percentage of those claiming retirement benefits at age 62 has been relatively constant since the last major reforms in 1983 (Figure 1). Yet these data do not accurately reflect the trends in claiming behavior by age, since they present claiming by calendar year, not by birth year or cohort (Muldoon and Kopcke, 2008).

Figure 1 here

A more accurate way of assessing claiming behavior of 62-year olds is to look at the percentage of each birth cohort that claims at age 62; for example, the percent of people born in 1946 that claim benefits at age 62 when first becoming eligible in 2008. Using cohort data, comparisons can be made across birth years to see if those born in the 1920s have different claiming behaviors than those born in the 1930s and the early 1940s. Using the Continuous Work History Sample (CWHS), we calculated claiming patterns at age 62 for cohorts born between 1913 and 1947. Note, those born in 1913 first become eligible for reduced social security retirement benefits at age 62 in 1975, while those born in 1947 become eligible in 2009. These calculations are shown in Figure 2.

Figure 2 here

For both men and women, there is a clear decrease in the percentage claiming at age 62 beginning in 1997, for the cohort born in 1935. Due to the spousal benefit,⁵ the claiming pattern for women is, not surprisingly, consistent for those born between 1913 and 1938. As more women began to devote more time in the paid labor force, the percentage of those claiming benefits at 62 began to decline steadily, reaching a low of 36 percent in 2007 at the peak of the last economic expansion. Men, who have traditionally had more consistent employment patterns, display a time series increase benefit receipt at age 62, corresponding to the 1983 social security reforms. For men born in 1920, 41 percent elected to receive benefits when they turned age 62 in 1982. A pronounced three percentage point increase occurred in 1983, as 44 percent of men born in 1921 elected to start receiving retirement benefits at age 62. The fraction of men taking early retirement benefits then trended upward from 1983 through 1993, reaching a peak of 49 percent. Beginning in 1997, the trend started to reverse, and there was a decline in the percentage of men claiming at age 62, reaching a new trough of 34 percent in 2007 (those born in 1945).

Did the financial crisis of 2008 result in an increase in those electing to receive early retirement benefits at age 62? While correlation is not causation, a preliminary analysis of the data do support the thesis that, in response to financial shocks and increases in unemployment, more people will elect to begin taking social security retirement benefits as soon as eligible. In 2007, the year before the recession, 33.5 percent of fully insured⁶ men chose to begin retirement benefits at age 62, while 36.3 percent of fully insured women began benefits at age 62. These figures increased for the 1947 birth cohort who turned 62 in 2009 when the recession hit a low point, as 35.8 percent of fully insured men started receiving benefits and 38.9 percent of fully

insured women followed suit. Similar patterns exist when the data are disaggregated by race, as shown in Figure 3.

Figure 3 here

We conducted a similar analysis by state, to test whether states with higher unemployment rates also exhibited higher percentages of early claiming behavior at age 62. We use US Bureau of Labor Statistics data on state-level unemployment in 2009 and claiming information from the Continuous Work History Sample. The national unemployment rate was about 9.2 percent in 2009, and in that year, state-level unemployment varied from 4 to 13 percent. As Figure 4 shows, higher unemployment in a state was correlated with a higher incidence of claiming at age 62 in 2009. This is computed for the age-eligible population which is fully-insured for benefits. A simple linear regression shows a positive relationship between unemployment and age 62 retirement claims.⁷

Figure 4 here

How social security helps retirement preparations

A preliminary analysis of the data supports the thesis that more people will elect to begin taking social security retirement benefits as soon as eligible, due to financial shocks and increases in unemployment as a result of the global financial crisis. Recognizing the unique role the SSA plays in the financial security of millions of Americans, and to better help people prepare for retirement in a post-financial crisis world, in 2009 the Agency undertook a special initiative to develop and refine print, web, and other products to better inform the public about retirement planning options and the importance personal saving contributes to a dignified and financially secure retirement (SSA, 2011a).

The SSA's decision to promote financial literacy drew from research that found differences between how much people expect to receive in social security benefits when they retire, and what they actually receive. For example, only 19 percent of workers can correctly identify the age at which they will be eligible for full benefits from social security (EBRI, 2011). Further, the 2011 Retirement Confidence Survey (RCS) found that current workers are half as likely to expect social security to provide a major share of their income in retirement (33 percent) as current retirees are to say social security makes up a major share of their income (68 percent). However, EBRI (2011) found that 60 percent of those all 65 + received at least three-quarters of their income from social security in 2009.⁸ Additionally, although people are living longer, a significant fraction of workers continues to take social security benefits at age 62 even though this may permanently reduce monthly benefits. Also influencing the SSA's decision to move forward with a special initiative to encourage saving was research linking financial literacy and saving behavior, indicating that the less financially literate are also least likely to plan for retirement (Lusardi 2011; Lusardi and Mitchell, 2006, 2007, 2008, 2009).

The SSA's first initiative was to improve the Social Security Statement with modest changes to the content and language; it also changed the order in which benefit projections were displayed, to focus attention on the full retirement age instead of the early retirement age (age 62). The Statement was sent to all working Americans age 25 or over, and it provided a personal record of the earnings and taxes paid, along with an estimated benefit of what the worker might receive in the future when electing to begin receiving benefits. Approximately 150 million Statements were mailed in 2010. Research has shown that the introduction of the Statement in 1995 had a significant impact on increasing workers' knowledge about social security benefits (Mastrobuoni, 2009).⁹ Surveys commissioned by the SSA also found that those respondents who

stated they had received a Statement were better informed than those who did not recall receiving one. Additionally, the Social Security Advisory Board recognized that the Statement is the ‘most direct and important means of communicating with the public’ about social security benefits (SSAB, 2009).

Along with the modest content and language changes in the Statement, the SSA also created two one-page, double-sided inserts to accompany the Statement. The first insert, entitled ‘Thinking of Retiring?’ was included in Statements sent to workers age 55+, beginning in October 2000. It addressed important topics including the reduction in benefits that occurs if one elects to begin benefits before the full retirement age, the role of survivor and spousal benefits, and the fact that the decisions to stop work and begin collecting benefits are independent. The insert also provided information on how workers could go to the SSA’s website and use online tools to estimate retirement benefits.

The second insert, issued in February 2009, was designed for workers aged 25-35. Entitled ‘What Young Workers Should Know About Social Security and Saving,’ it informed younger workers that social security is a form of social insurance that provides disability insurance along with retirement benefits, and it stressed the importance of personal saving to a financially secure retirement. Additionally, the insert informed its young readers that social security benefits are designed to replace approximately 40 percent of income in retirement, but financial planners suggest that retirees will need to replace 70-80 percent of pre-retirement income to have a secure retirement. Accordingly, individuals will need to make up the difference with personal saving or pensions.

An additional one-page, double-sided information pamphlet was also created to address one of the most important questions people ask the SSA, namely ‘What is the best age to start

receiving retirement benefits?’ The document entitled ‘When to Start Receiving Retirement Benefits’ stresses that when to begin benefits is a very personal decision and that no simple answer is correct for everyone. This document indicated that monthly benefits vary substantially, depending on the age one begins receiving benefits. It also noted that retirement may be longer than most people expect, and it highlighted that one’s decision about when to begin benefits might also affect the benefits a person’s family is eligible to receive. Finally, it also explained how continuing to work after receiving benefits is treated. This document was distributed to all SSA field offices (approximately 1,300) and it is available on the agency’s website.¹⁰

The SSA also supported an extramural program of research on retirement, including several interdisciplinary projects on financial literacy, decision making, and behavior change. The research goals were learn the most effective ways to help foster retirement and other saving strategies at all stages of the life cycle, to help low and moderate income populations successfully plan and save for retirement and other life events, and to improve understanding of Social Security's programs. The goal was to have the findings inform Social Security’s efforts (statement, web, program design, etc.) as well as spill-over to other relevant areas such as employer sponsored retirement programs.

Several of the financial literacy projects have produced promising results. For example, an innovative study used the American Life Panel to experiment with different ways of framing monthly benefit information, to inform people that delaying claiming leads to a higher monthly benefit (Brown, Kapteyn, and Mitchell, 2010). The authors held constant the factual information presented but varied how the information was presented to highlight the financial gains of delaying or claiming. That study found that framing information strongly shaped respondents’ expected claiming ages.

Unfortunately, due to the tightening of federal budgets in 2011, the Social Security Administration curtailed its efforts in the financial literacy domain. Moreover, the agency suspended the mailing of the Statement to workers, and cut back on research support for financial literacy projects (Astrue, 2011).

Conclusion

The financial crisis that began in 2008 resulted in substantial and unanticipated job loss and loss of wealth for millions of people. Many Americans responded by reducing consumption and increasing saving. Moreover, based on a preliminary analysis of the data, it also seems that some will elect to receive retirement benefits at age 62, reversing the pre-crisis trend to file at later ages. Further research will be required to confirm this trend.

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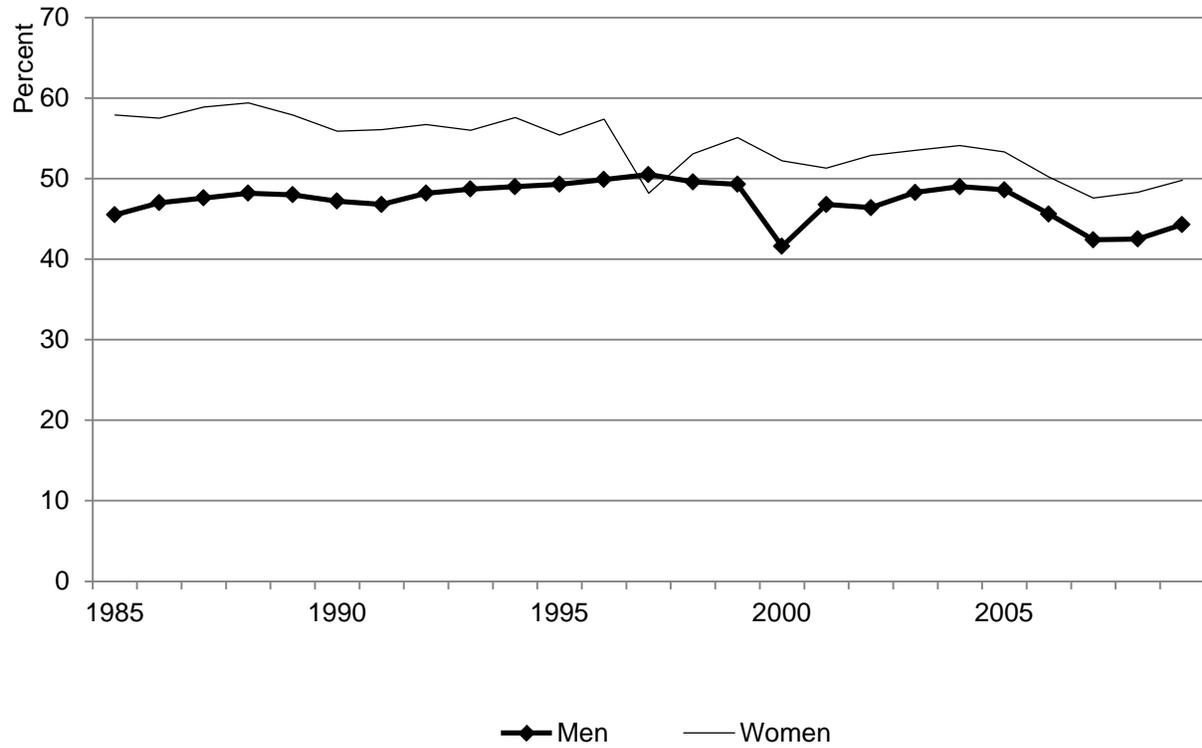


Figure 1. Percent of social security benefits awarded at age 62 over time. *Source:* Derived from Table 6.B5., SSA (2010a).

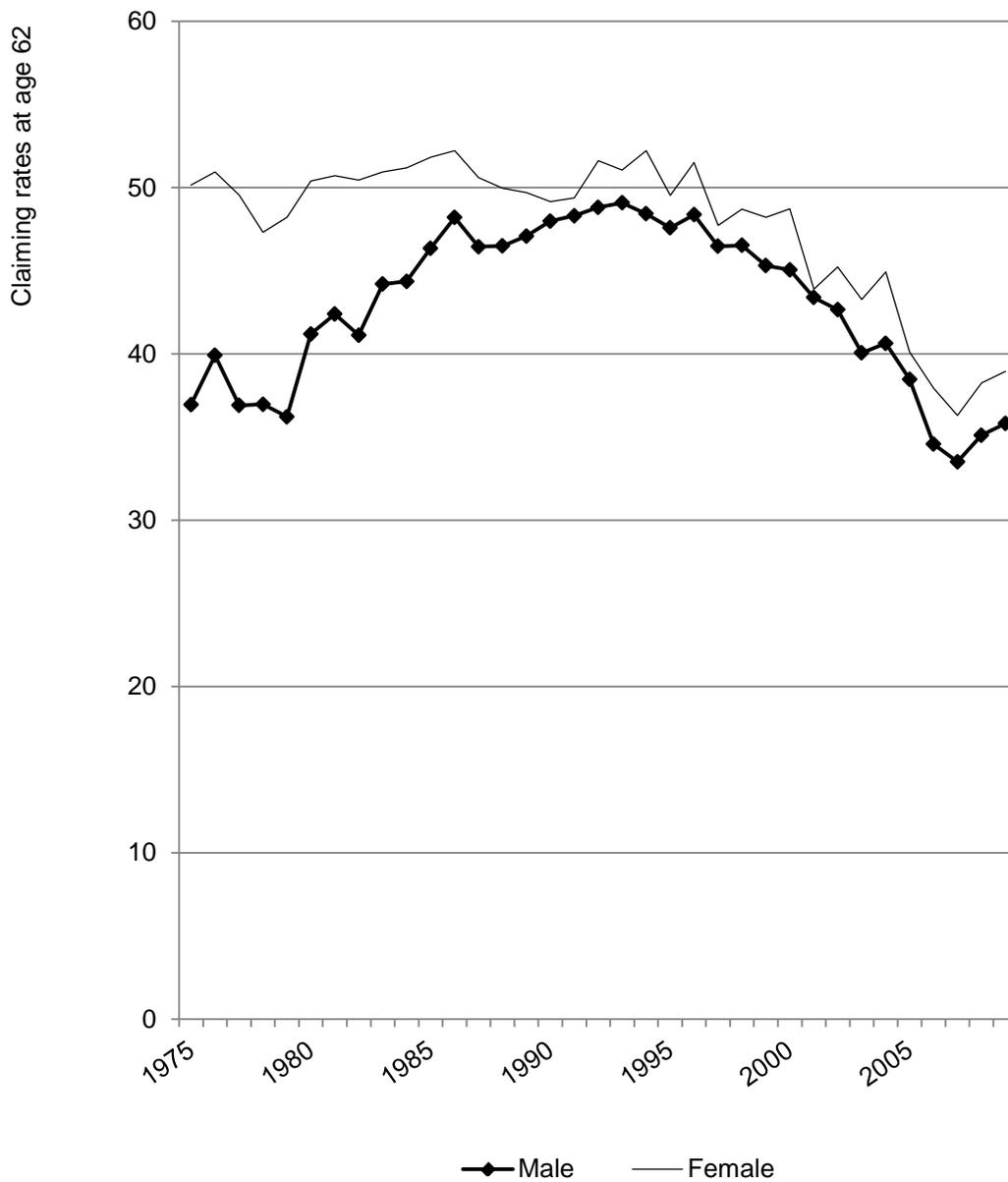


Figure 2. Percent of fully-insured workers who claim at age 62: cohorts born 1913-1947 by sex. *Source:* Authors' calculation based on SSA administrative data, Continuous Work History Sample.

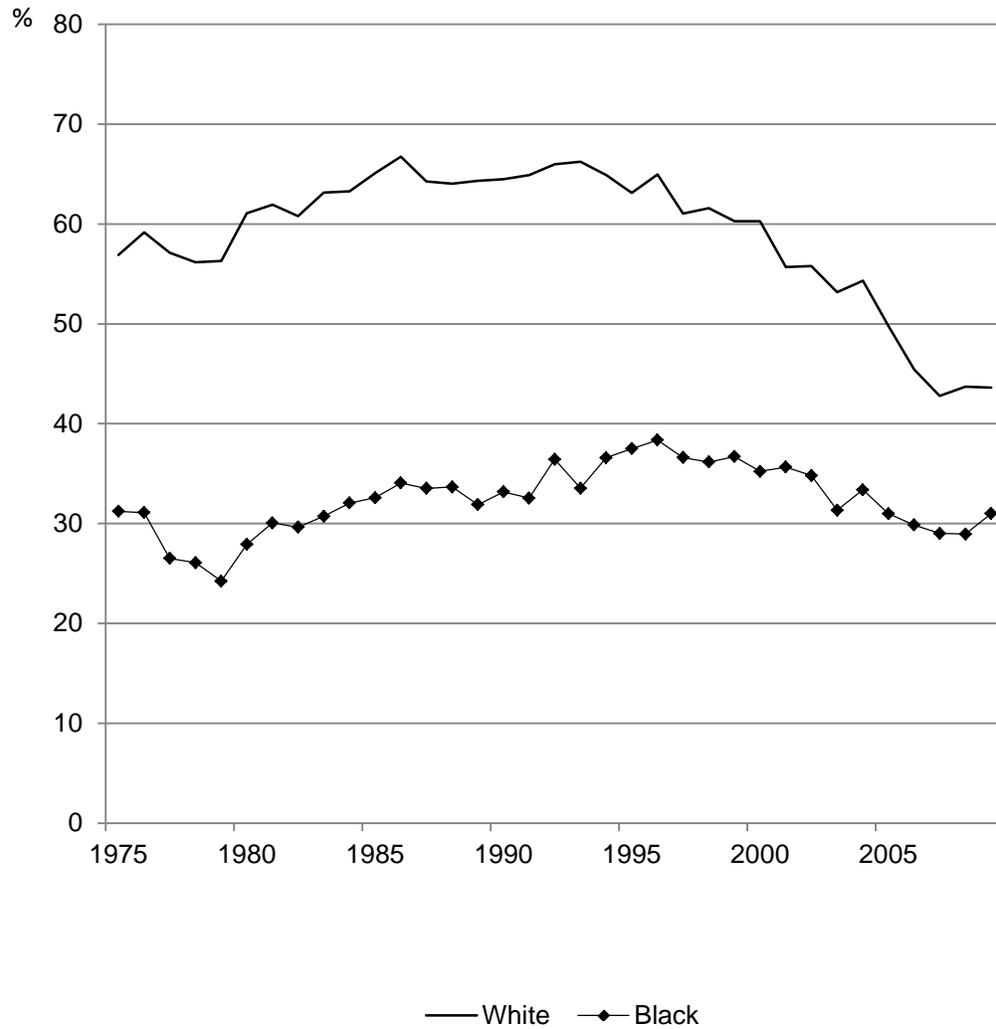


Figure 3. Percent of fully insured workers who claim at age 62: cohorts born 1913-1947 by race. *Source:* Authors' calculation based on SSA administrative data, Continuous Work History Sample.

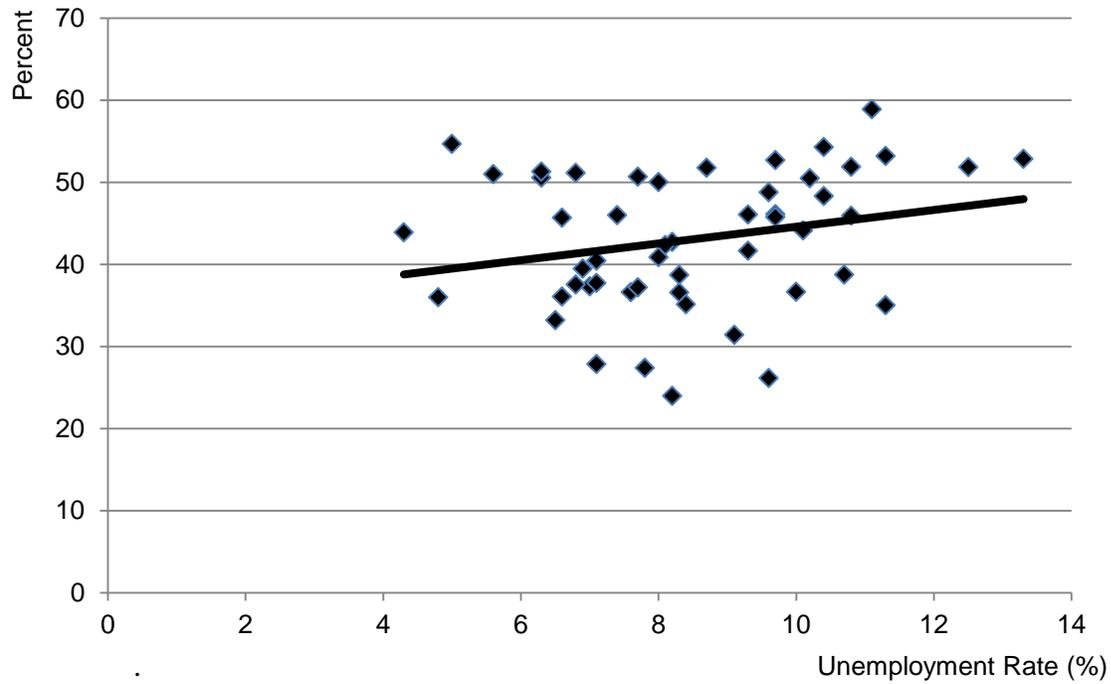


Figure 4. Cross-state unemployment rates and percent claiming (2009). *Note:* Percent claiming based on estimates of fully-insured at age 62. *Source:* Authors' calculation based on SSA administrative data, Continuous Work History Sample.

Endnotes

¹ Data from YahooFinance.com; S&P 500 index value at market close on October 10, 2007 was 1562.47. Index value at close on March 9, 2009 was 676.53. The National Bureau of Economic Research, the arbiter of the start and end dates of a recession, determined that the recession that began in December 2007 ended in June 2009, roughly coinciding with the peak and trough dates of the S&P 500 index.

² The timing of retirement can be affected by more than age, including accumulated saving, the availability of an employer-provided pension, the willingness or ability to continue working part-time in retirement, personal health, access to health coverage and general economic conditions.

³ Although the time between the 2008 HRS interview and a subsequent 2009 HRS Internet survey was insufficient to observe actual behavior, the data nonetheless can be used to shed light on retirement expectations.

⁴ For a theoretical model of this behavior, see Chai et al. (2012).

⁵ Spouses of Social Security retirement or disability benefits may also be eligible for benefit payments. Benefits can be paid to a spouse if he or she is age 62 or older; or at any age if he or she is caring for the primary beneficiary's child (the child must be younger than 16 or disabled and entitled to Social Security benefits on the primary beneficiary's record). Spouses may be eligible for a monthly benefit that is up to half of the primary beneficiary's retirement or disability benefit amount. For more information see SSA (2011*b*).

⁶ Individuals must be insured under the Social Security program before retirement, survivors, or disability benefits can be paid. Social Security considers the number of quarters of coverage earned to determine insured status. A quarter of coverage (QC), also called a 'credit,' is earned for a certain amount of work covered under Social Security, but no more than 4 QCs can be

earned in a given year. Generally one must be ‘fully insured’ to receive Social Security benefits, but other requirements may also apply. To be fully insured, a person needs at least one QC for each calendar year after turning 21 and the earliest of the following: (1) the year before one attains age 62, (2) the year before one dies, or (3) the year one becomes disabled.

⁷ In a simple linear regression of state-level unemployment and age-62 claiming, the relationship is significant at the 9 percent level.

⁸ Employee Benefit Research Institute (EBRI, 2010).

⁹ Prior to 2000, the Social Security Statement was known as the Personal Earnings and Benefit Statement (PEBES).

¹⁰ Examples of the Social Security Statement and the two inserts can be found online:

<http://www.ssa.gov/mystatement/statsamples.htm>. The document entitled ‘When to Start

Receiving Retirement Benefits’ can also be found online:

<http://www.socialsecurity.gov/pubs/10147.html>