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BOOK REVIEW

Remaking Retirement: Debt in An Aging Economy

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Reviewed by Anna M. Rappaport, FSA, MAAA

INVESTMENTS & WEALTH INSTITUTE®

Remaking Retirement: Debt in an Aging Economy

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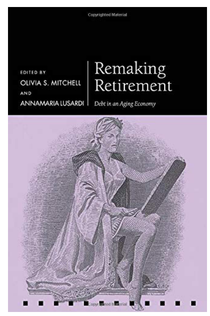
Editor's note: Remaking Retirement: Debt in an Aging Economy, *edited by Olivia S. Mitchell and Annamaria Lusardi, is a compendium of research studies sponsored by the Pension Research Council at The Wharton School.*



Debt is a major financial problem for many Americans. Personal debt has increased over time, and more individuals are entering retirement with significant debt. Debt can take several different forms, including mortgages, reverse mortgages, medical expense obligations, credit card debt, and many more. As people near and transition into retirement, they must make several decisions linked to debt. This book provides a multi-faceted look at different aspects of this issue, including the growth and importance of debt, the amount and types of debt held by older persons, the patterns of debt and payments by age, the link between debt and bankruptcy, and the international picture. Responding to recent trends in debt, the book focuses most heavily on the older populations, yet it also includes information about borrowing and debt repayment throughout the life cycle. This volume also includes projections indicating that the next cohort of retirees will be worse off than the current group. This tome should be central to the work of financial advisors, because debt affects financial planning, when people can afford to retire, and a variety of other retirement decisions. The research studies provide data and analysis that should be very helpful in giving advisors new perspectives and a bigger picture as they think about clients and their debt. Although the volume was written before COVID-19, the concerns it raises persist and have intensified for some population segments.

Below, I discuss several chapters that I believe are of greatest relevance to advisors.

PERSPECTIVES ON RESEARCH ON DEBT AND RETIREMENT SECURITY

Personal debt has grown significantly in the older population, and retirement experts increasingly are concerned about the impact of growing debt on retirees. The decline of defined benefit plans, coupled with rising medical costs, a shift to fewer jobs with good benefits, and longer periods of retirement, are all contributing factors to greater challenges for retirees.

DEBT OVER THE LIFE CYCLE

Personal debt varies over the life cycle. For instance, millennials have taken on a great deal of student loans, while mortgage debt is the largest for members of Generation X. Retirees today are far more likely to have mortgage debt than in the past. Interestingly, the volume finds some student-loan debt for all generations, including loans taken out for themselves, or for a child or grandchild. One chapter, "The Graying of American Debt," reports on differences in debt by age groups, and another, "Paying it Back: Real-World Debt Service Trends and Implications for Retirement Planning," looks at debt repayment by age group.

OLDER ADULTS' DEBT BY INCOME, RACE, AND ETHNIC GROUP

The chapter titled "The Risk of Financial Hardship in Retirement: A Cohort Analysis," focuses on the types of debt held by age and racial and ethnic groups. For example, 37 percent of older adults hold home mortgages. By income, 18 percent of those with incomes less than $35,000 held home mortgages versus 52 percent of those with incomes greater than $75,000. Credit card debt and other forms of expensive debt are held by 25 percent of older Americans. By income, 25 percent of those with incomes under $35,000 held such debt compared with 16 percent of those with incomes over $75,000. Twenty-one percent of whites have such debt, 38 percent of African Americans, 25 percent of Hispanics, and 13 percent of Asians do so. These data are derived from the 2015 National Financial Capability Study.

DEBT AND RETIREMENT DECISIONS

In another chapter, "Is Rising Household Debt Affecting Retirement Decisions?" the authors report that debt levels have risen over time, so that more people are holding debt as they near retirement age. As a result, debt pressure has increased peoples' probability of working and led to later retirement; it also influences when people claim Social Security benefits. The authors found that credit card debt had a bigger influence on work and retirement decisions than mortgage debt. They also point out that customs with regard to mortgage debt have changed over time, because people today tend to refinance their mortgages, rather than paying them off by the time they retire (as was traditional in the past).

A FOCUS ON BAD OUTCOMES FOR RETIREES

The rising fraction of older Americans with mortgages, the increasing amounts of those mortgages, and the growing pattern of foreclosures is the subject of the chapter entitled "Mortgage Foreclosures and Older Americans: A Decade after the Great Recession." Although older individuals did better than younger ones, they still had many problems. For instance, of families age 75 and older, 6.3 percent had mortgage debt in 1989, a figure that rose to 26.5 percent by 2016. Foreclosures were higher for sub-prime mortgage holders and for non-white borrowers.

Bankruptcies and foreclosures represent growing problems for retirees, as discussed in the chapter "Financial Distress Among the Elderly: Bankruptcy Reform and the Financial Crisis." Using data from the 2005 bankruptcy reform and the financial crisis, the authors conclude that neither event explains the pattern of filings. In particular, the percentage of total bankruptcy filings by the elderly increased from 6 percent in 2000 to 12 percent in 2018; corresponding numbers for foreclosures are 6.8 percent and 11 percent. Nevertheless, the elderly are less likely to encounter these situations compared with the younger population.

AN INTERNATIONAL PERSPECTIVE

Research from the International Monetary Fund indicates that added household debt leads to slower output growth, higher unemployment, and greater probability of future banking crises. In the chapter titled "Understanding the Macro-Financial Effects of Household Debt: A Global Perspective," the authors discuss analysis of evidence from 80 countries. In advanced economies, the median debt ratio rose from 52 percent of gross domestic product (GDP) in 2008 to 63 percent in 2016. In emerging market economies, the median debt ratio increased from 15 percent to 21 percent of GDP over the same period. Another international perspective is offered in the chapter "Household Debt and Aging in Japan." Here the authors report that the United States is not the country with the most debt. In fact, Canada and the United Kingdom have relatively more personal debt, while Italy has relatively little. Japan and the United States are in the middle. Four of these nations have a higher ratio of household liabilities to assets than does the United States.

OTHER RESEARCH ON DEBT AND ITS SIGNIFICANCE

The Society of Actuaries (SOA) report "Financial Risk Concerns and Management Across the Generations" focuses on what people say about how important debt is in managing their finances (SOA 2018). This report is one of a series of studies analyzing a 2018 survey of the U.S. public by generation; this survey relied on self-reports by 2,001 individuals, across income levels. In the retired generations (early boomers and silents), 63 percent said they had debt, and 14 percent said that their level of debt was complicating their ability to manage their finances. By contrast, 77 percent of the millennials said they had debt and 34 percent said debt was complicating their ability to manage their finances. For Gen X, the figures are 83 percent and 26 percent. For the early boomers, they are 74 percent and 17 percent.

A new SOA survey in 2021 found that peoples' concerns about debt have now worsened, in part due to COVID-19. About half of millennials (48 percent) now say that debt is complicating their finances. Debt is also a problem for Gen Xers (35 percent), but it is a much smaller issue for late boomers (20 percent), early boomers (16 percent), and the silent generation (14 percent). The newer study also reported that 27 percent of millennials and Gen Xers have experienced a negative impact on their level of debt since the COVID-19 pandemic began. This is true for two in 10 late boomers, 14 percent of early boomers, and 11 percent of the silent generation.

OVERVIEW OF ISSUES TODAY

Household debt has become an increasingly important concern to older households in the past three decades. Debt, of course, can be good or bad for any individual household, depending on how it is managed. Debt has enabled a much better life for some families, helping them to get education supportive of a good career, helping them to buy an affordable house, or helping them to establish a good business. Nevertheless, for others, it has become a major problem leading people to become over-extended. Student loans have become particularly troublesome for those who were unable to complete their programs, and for some who enrolled in online programs. Moreover, the same people having trouble with debt can also have difficulty budgeting and managing day-to-day expenses. SOA research on financial management across the generations found a consistent top priority of meeting day-to-day expenses (SOA 2018, 2021).

COVID-19 also has had a major impact on families, disrupting employment, leading people to draw down savings, and in some cases, to take on new debt. Thus far, the biggest challenges linked to the pandemic have confronted the younger generations, not retirees. Yet with the ending of mortgage forbearance programs, the elderly also may soon be affected.

Employers and advisors have recognized the importance of helping employees with day-to-day money management and the wide use of debt. This has prompted the development of financial wellness programs, as well as a move from retirement education and planning to a broader financial wellness focus. Such programs incorporate a variety of different options and will continue to evolve as employers seek to help employees do a better job of managing their own finances. For advisors, there are business issues in deciding how much focus to place on debt and how to weave debt issues into their practices.

ACTION STEPS AND TIPS FOR ADVISORS

Areas for action:

- Debt reduces net worth and debt repayments boost regular spending. Debt should be a factor in deciding whether an individual can afford to retire and how much adjustment might be required in the post-retirement standard of living.
- When clients hold debt, advisors have multiple opportunities to help them figure out how to manage this debt effectively. In particular, advisors can help identify alternative paths for repayment and/or reorganization of the debt and lay out new options for clients to consider.
- Potential responses to substantial debt that is not easily affordable in retirement include retiring later, reducing expenses, and working post-retirement.
- Housing is a major asset for many Americans, and often housing has a mortgage. Refinancing mortgages has been common in the past 20 years, and many people who have been in their homes for a long time still have significant mortgage balances. Advisors should help clients evaluate whether the client's house is affordable and, if so, whether and how soon the mortgage should be repaid.
- Debt is a major issue for the financially fragile. Managing debt is critical for financial stability, enabling people to save for retirement.
- Credit card and some other types of debt carry very high rates of interest. It is therefore essential to encourage clients to repay their high interest-rate debt and not to allow it to keep building.
- Reverse mortgages are a way to use housing equity to help finance retirement.

Planning issues:

- Can I afford to retire?
- How do I manage high-cost debt?
- Should I pay off the mortgage and other debt before retirement?
- Should I take a reverse mortgage?
- Can I negotiate down unexpected medical expenses that led to unexpected debt?
- Am I responsible for debt because of cosigning loans with other family members?
- Should I put money into my 401(k) plan at the same time I am incurring new credit card debt?
- Should I put money into my 401(k) plan versus paying down credit card and other high-cost debt?

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