What Factors are Associated with Generational and Gender Differences in Objective Retirement Income Adequacy

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Introduction

Retirement research often finds Americans fall short of achieving retirement income adequacy (RIA). However, many of these studies simply projected growth of existing assets without considering additions to and growth of savings when predicting RIA (see Kim and Hanna, 2013). Prior research also did not adequately considered gender and generation differences in achieving retirement income adequacy. This study investigates change in the effect of gender on RIA over time. This study also compares RIA of Baby Boomers (Boomers, born 1946 to 1964), and Generation X (Gen X, born 1965 to 1981)(Dimock, 2019).

Literature Review

Women's labor force participation has increased substantially since the 1970s. Today, the majority of women age 25-54 are employed. Women's earnings have increased over time as well, contributing to a decline in the gender wage gap. Although women's retirement plan access tends to lag men's, rise in their employment rates has likely increased access to workplace retirement plans as compared with past decades. Further, women's greater earning power today may make saving retirement easier than it was a few decades ago. In other words, while a gender gap in RIA is likely to exist, it is expected to be smaller in more recent years.

Boomers and Gen X experienced many of the same economic conditions, although the conditions affected them at different points in their lifecycle. There was, for example, steep inflation during the early 1980s, the 1990s stock market boom, and the Great Recession only a decade ago. The first major retirement plan change in the U.S. occurred when most Boomers were adults but Gen X were still youth. The Employee Retirement Income Security Act (ERISA) of 1974 introduced deferred compensation (DC) plans and individual retirement accounts (IRAs). The Taxpayer Relief Act of 1997 established Roth IRAs and Coverdell Education Savings Accounts, widening retirement savings options for households outside employer-sponsored plans. Boomers were first to experience the quick decline in defined benefit (DB) plans in favor of a growing number of DC plans, which decisively shifted the burden of retirement savings from employers to employees. Gen X was the first generation to benefit from availability of IRAs, Roth IRAs, and DC plans during their entire time in the labor market.

Two theoretical perspectives are helpful in the study of retirement planning. Life course theory (White, Klein, & Martin, 2015) encourages consideration of the decision-making context and recognizes that individuals make decisions based on past life experiences. Regarding retirement planning, it is reasonable to expect that younger generations learn from observing grandparents and parents. The life-cycle theory of consumption and savings (Ando & Modigliani, 1963) posits that individuals and families change spending and saving patterns over the course of the life cycle, providing understanding of ways financial decisions made across the life cycle can affect RIA.

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Economic conditions are a primary consideration when comparing generations' RIA, particularly given variability in the U.S. economy since the end of WWII. The 2012 Institute for Economics & Peace (IEP) report highlighted the economic consequences of war on the U.S. economy. World War II (WWII) generated a booming GDP growth rate of more than 17% with the stock market rising past its pre-WWII level. GDP growth continued increasing through the Korean War, though inflation was more than 5%. However, a brief recession that set in after the end of the war was triggered by a lack of increase in investment although military spending was still high (IEP, 2012).

Real estate is a common source of retirement wealth. However, postponement of college graduates' first home purchases due in part to high student loan debt delays amassing home equity (Mishoury & O'Sullivan, 2012). The percentage of U.S. households with debt decreased from 74% in 2000 to 69% in 2011, but median debt during that period increased by 37% (Vornovytsky, Gottchalck, & Smith, 2011).

Gender is also a key factor in retirement planning. Employment decisions and stable labor market participation facilitate RIA and confidence in expected retirement income. But, due to family caregiving responsibilities, employment gaps are more common for women (Blau & Kahn, 2000; Heckman, 1974), which can reduce objective RIA. Women who leave the work force during childbearing years may ultimately experience lower lifetime wages (Blau & Kahn, 2000), leading to lost earning power and reduced resources for retirement investment. Retirement planning knowledge is lower among females (Hopkins & Littell, 2015). Fisher and Yao (2017) found a difference in risk tolerance by gender. Research indicates women tend to be less risk tolerant than men, posing a threat of low investment growth when combined with lower wages of women as as compared with their male counterparts. Neelakantan (2010) found that women's risk tolerance, on average, is 10% lower than men's risk tolerance, accounting for a 51% reduction in lifetime wealth accumulation when considering the wage gap.

Health care costs are a growing concern. Wallace, Haveman, & Wolfe (2016) found that married couples who experienced a health shock saw small declines in wealth that eventually grew to larger declines in wealth of up to 12% over time. Munnell, Hou, & Sanzenbacher (2018) report an intact household of two adults and two children live on 100% of the household's combined resources, but separation of this same household requires 120% of resources. Shin & Kim (2017) found that single women experienced a higher rate of wealth depletion (28%) from 1992 to 2014 than married women (14%). Given gender wage gap concerns, single female-headed households may see a far lower probability of achieving RIA.

Boomers are expected to be more pessimistic about RIA than Gen X and less likely to be prepared given Great Recession effects occurring close to their retirement transition. From a theoretical perspective, we expect these generations learned to adjust spending and saving in order to recover, from an objective point of view. Research indicates that women often demonstrate lower risk tolerance, spend less time in the workforce, and experience lower earnings (Blau & Kahn, 2000; Fisher & Yao, 2017; Heckman, 1974), all of which could lead to being less optimistic about their retirement preparedness and being objectively less prepared than their male counterparts.

It is expected that individuals will make retirement planning decisions to improve their outcome by learning from past behaviors (and economic times). Given a preference for consumption smoothing over the lifespan as well as various external factors addressed in the literature, we hypothesize that:

1. Women are less likely than men to meet or exceed the target for objective RIA.
2. The effect of gender on objective RIA is different for different years.
3. Gen X are more likely than Boomers to meet the target for objective RIA.
4. The effect of generation on objective RIA is different for different years.

Methodology

Data are from the 1989, 2001 and 2016 Survey of Consumer Finances (SCF), a triennial, cross-sectional survey of American households by the Federal Reserve Board. The sample includes those born between

1946 and 1964 (Baby Boom generation) and those born between 1965 and 1981 (Generation X) to assess effects of gender and generation across time. Sample is restricted to full time workers.

Objective RIA is measured by comparing retirement income replacement rate to target replacement rate (termed Retirement Income Replacement Rate or RIRR). If the household meets or exceeds the appropriate target income replacement rate, retirement income adequacy is met. RIRR is the ratio of post-retirement income (PostRI) to pre-retirement income (PreRI), where PostRI is the sum of expected income from Social Security retirement benefits and the income stream expected from the projected value of household net worth (Yuh, et al., 1998). Objective RIA equals 1 when RIAA ≥ 0.73.

Gender and generation are central explanatory variables of interest. Control variables include socioeconomic factors, demographic characteristics, economic expectations, and financial planning behavior characteristics. Socioeconomic measures include income, net worth, housing status, education level completed, and debt-to-income ratio. Demographic variables include race/ethnicity, marital status, the presence of children age 6 or under in the household, and self-reported health status. Economic expectations include expected retirement age and economic expectations in the next five years. Financial planning behavior characteristics are measured with inclusion four factors: (1) use of financial planner to make savings and investment decisions, (2) own an IRA, (3) participates in an employer-sponsored retirement plan, and (4) risk tolerance level.

The two logistic regression models for analysis include the following:

1. *Objective RIA = female + year + female*year + [socioeconomic factors] + [demographic factors] + [financial planning behavior factors]*
2. *Objective RIA = Boomer + year + Boomer*year + [socioeconomic factors] + [demographic factors] + [financial planning behavior factors]*

Results

The share of adults who met or exceeded target RIRR declined over time from 96% in 1989 to 84% in 2001 to 64% in 2016. The hypothesis of women being less likely to meet the target objective RIA was not supported. Women and men are equally likely to meet the target objective RIA and the effect of gender did not differ by year. However, Gen X was more likely than Boomers to meet the target RIRR, though the effect of cohort did not vary by year as expected.

Other factors that increase the likelihood of meeting the objective target include having young children in the household, being a renter, being in the lowest income tercile, and being in the highest net worth tercile. Factors that negatively affect the likelihood of meeting the target RIRR include identifying as Black/African American, being married, being in the highest income tercile or the lowest net worth tercile, planning to retire at any age, identifying as having no risk tolerance, and identifying one’s health as fair or poor.

Conclusion/Implications

Generational differences in objective RIA exist. Results indicate that Boomers close to retirement are far less prepared to meet their retirement income needs than Gen X. Gen X is more highly educated than prior generations, especially its women, and Gen X women participate in the labor force more than prior generations (Butrica, Smith, & Iams, 2012). Financial planners have an opportunity to help Gen X to remain on track for retirement, especially given the economic challenges of delayed parenthood and now COVID-19 and its potential lingering effects. Efforts to keep Gen X on track for successful retirement income adequacy may have social costs that could be further explored such reduced financial support for their Boomer parents or for their children’s college education.

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