

The New Retirement— Emerging Issues Affecting Financial Security

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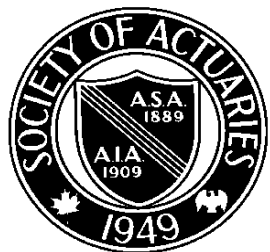
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AMERICAN ACADEMY *of* ACTUARIES

Retirement World Today - Context

- Decline in employer sponsored DB plans and retiree health
 - More individual responsibility, DC plans
 - Long service employees often have good benefits: DB, DC and retiree health
- Low savings rates
- People want and need to work longer, return to work
- Difficult policy environment and greater welfare costs for US taxpayers
- Big questions about future of retirement security



Background

- The actuarial profession has focused on Post-Retirement Needs and Risk
 - More work is needed about use of assets and understanding of post-retirement period
- Concern that too much individual responsibility may lead to bad outcome for many
- Response to post-retirement risk is key



Findings presented from two studies

- **Retirement Plan Preferences Survey**
 - Sponsored by SOA, Academy
 - Mail survey of retirement plan participants (790 workers and 600 retirees) conducted by Mathew Greenwald & Associates
- **2003 Risks and Process of Retirement Survey**
 - Sponsored by SOA
 - Telephone survey of 604 Americans ages 45-80 conducted by Mathew Greenwald & Associates and Employee Benefit Research Institute (EBRI)



Key Messages

- Retirement plan participants are very concerned about regular income security
- Pre-retirees are much more concerned about retirement security than in 2001
- People do not assess and manage risk well
- The emerging pattern of phasing into retirement is likely to increase
- People tend to express a preference for the type of employer-provided retirement plan they already have



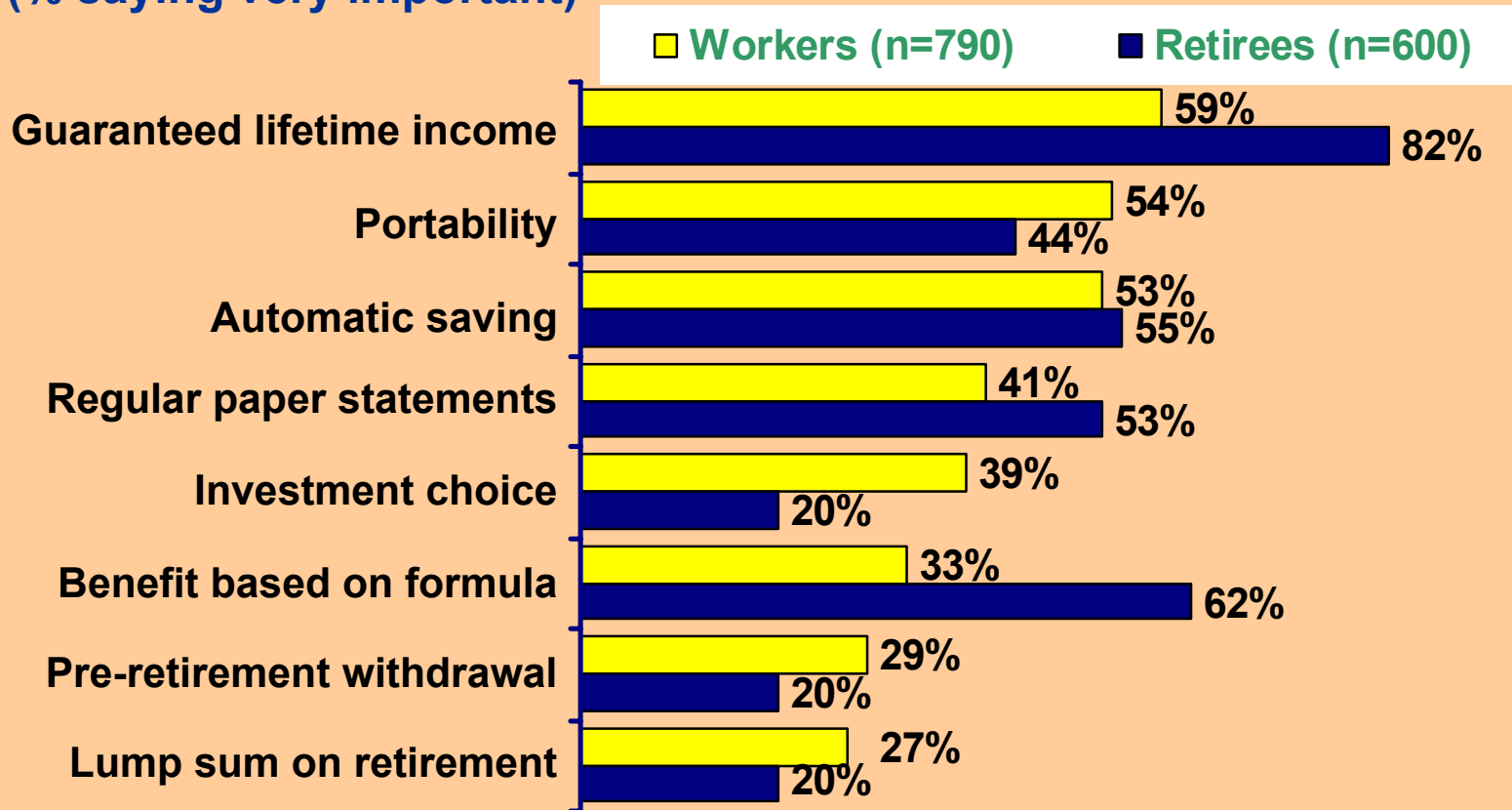
Key Messages

- Retirement plan participants are very concerned about regular income security



Lifetime income is top rated retirement plan feature, particularly for retirees.

How important is each in a retirement plan?
(% saying very important)



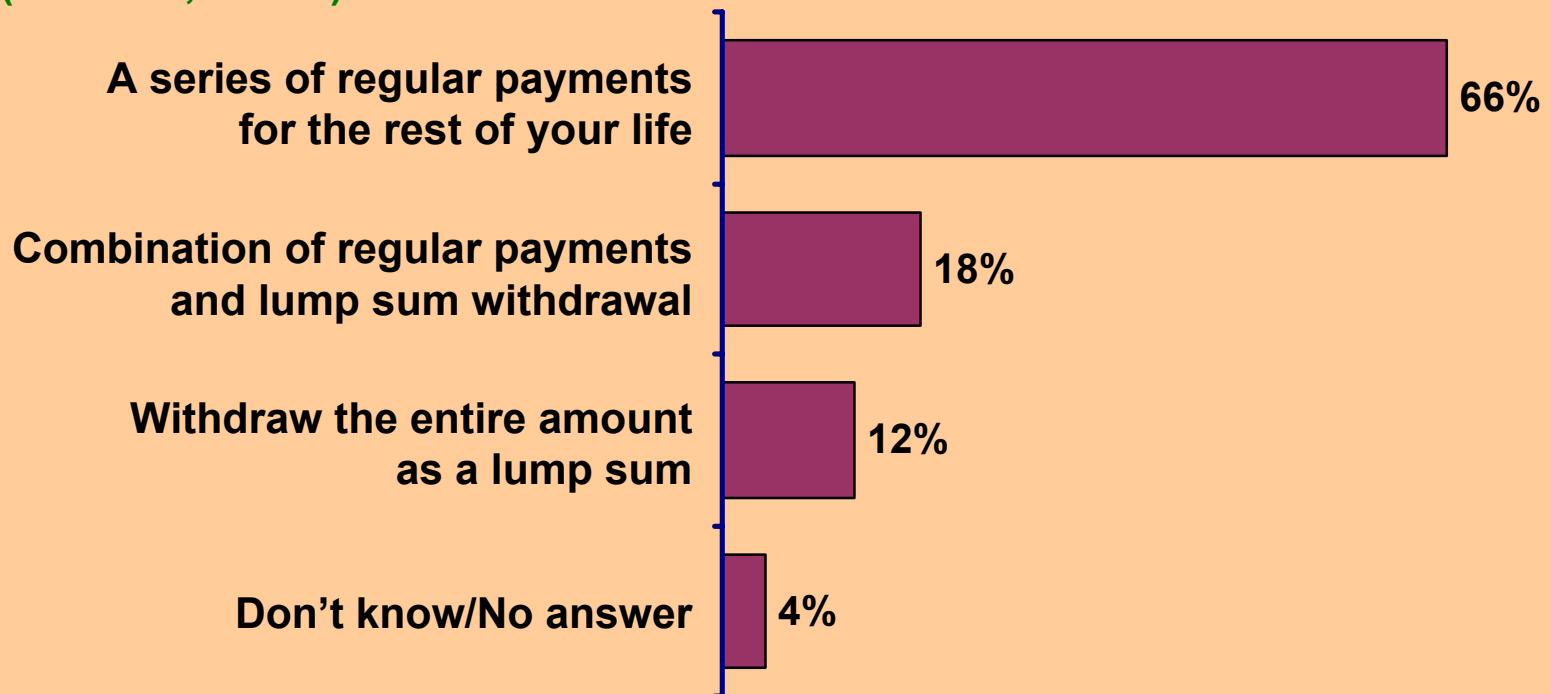
SOA/Academy, Retirement Plan Preferences Survey



Most workers want to take their plan payout as regular payments.

Which of the following best describes how you would like to receive your money at retirement from an employer's retirement plan(s), given that each choice is of equal value?

(Workers, n=790)



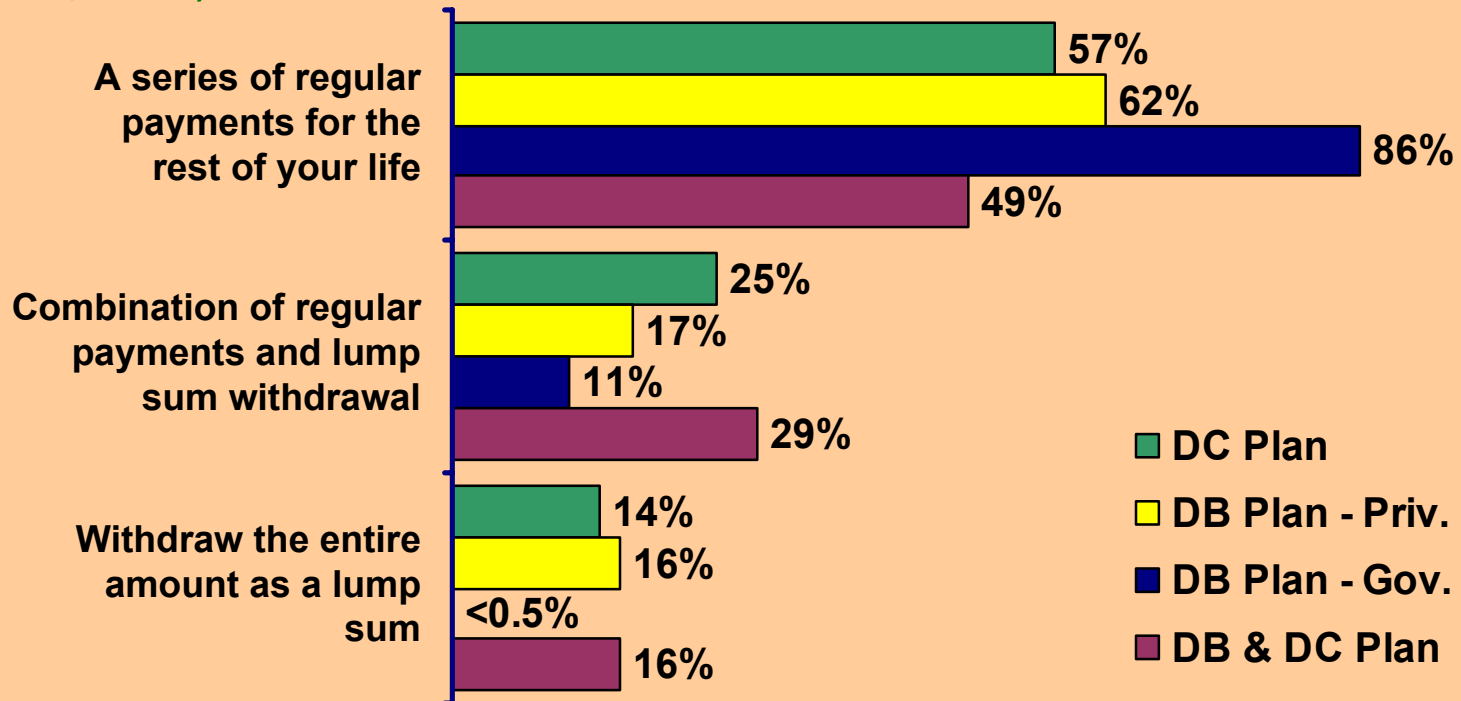
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Even DC plans should offer life annuity options.

Which of the following best describes how you would like to receive your money at retirement from an employer's retirement plan(s), given that each choice is of equal value?

(Workers, n=790)



SOA/Academy, Retirement Plan Preferences Survey



Comments

- US Federal public policy does not adequately encourage regular lifetime income
- Individual indication of awareness often not linked to action; people do not do what they say
- Nor is it clear that people understand retirement income management options well
- Need better understanding of what is viewed as regular lifetime income



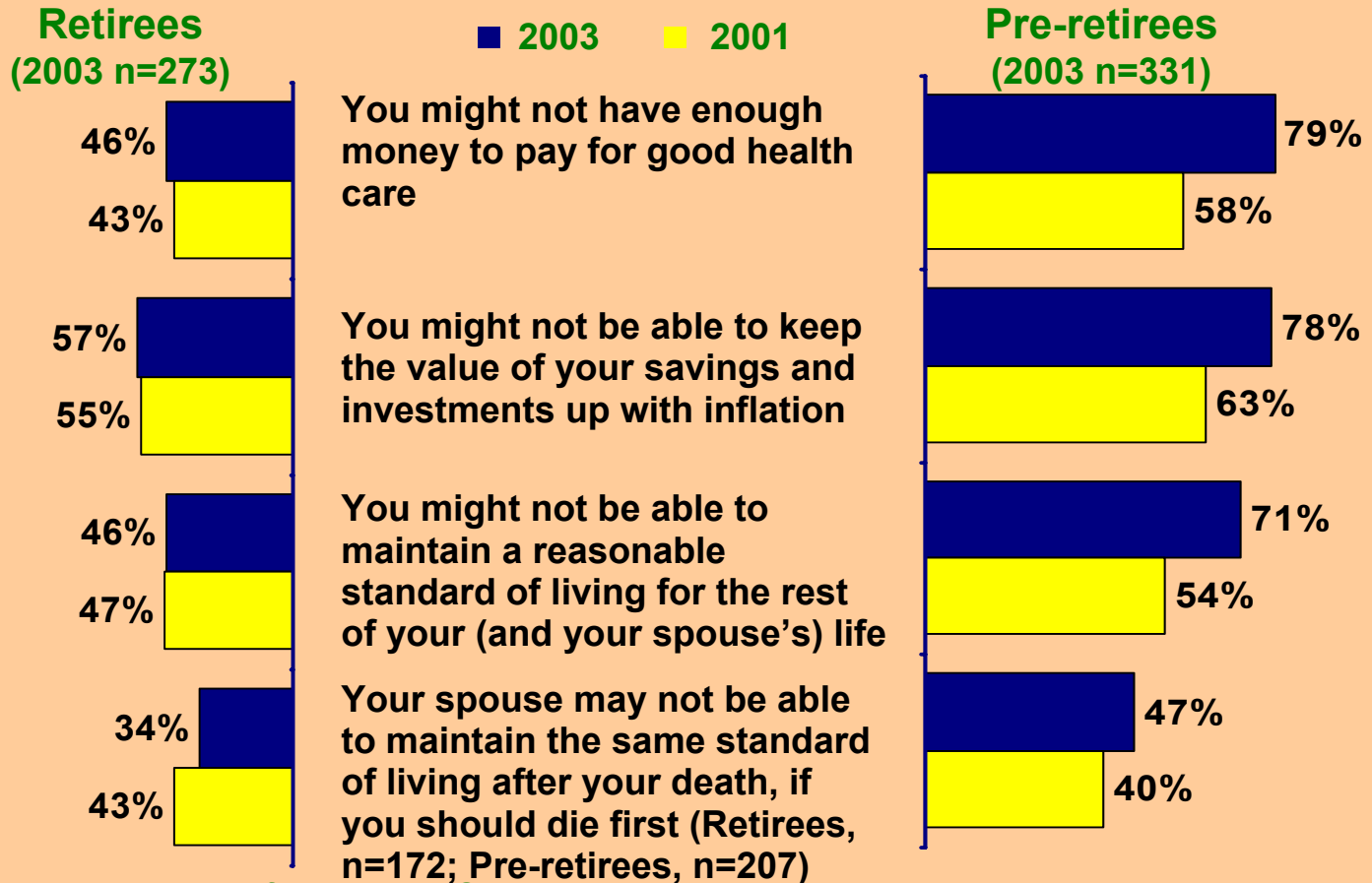
Key Messages

- Retirement plan participants are very concerned with regular income security
- Pre-retirees are much more concerned about retirement security than in 2001.



Pre-retirees, not retirees, are more concerned about risks than in 2001.

How concerned are you that...? (% very or somewhat concerned)



SOA, 2003 Risks and Process of Retirement Survey

Comments

- Events of the last three years have focused pre-retirees on risk
 - Health care costs
 - Disappointing investment markets
 - Terrorism
- Retirees are somewhat insulated from these risks
 - Medicare
 - Employer sponsored benefits (DB and health)



Key Messages

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- People do not assess and manage risk well.



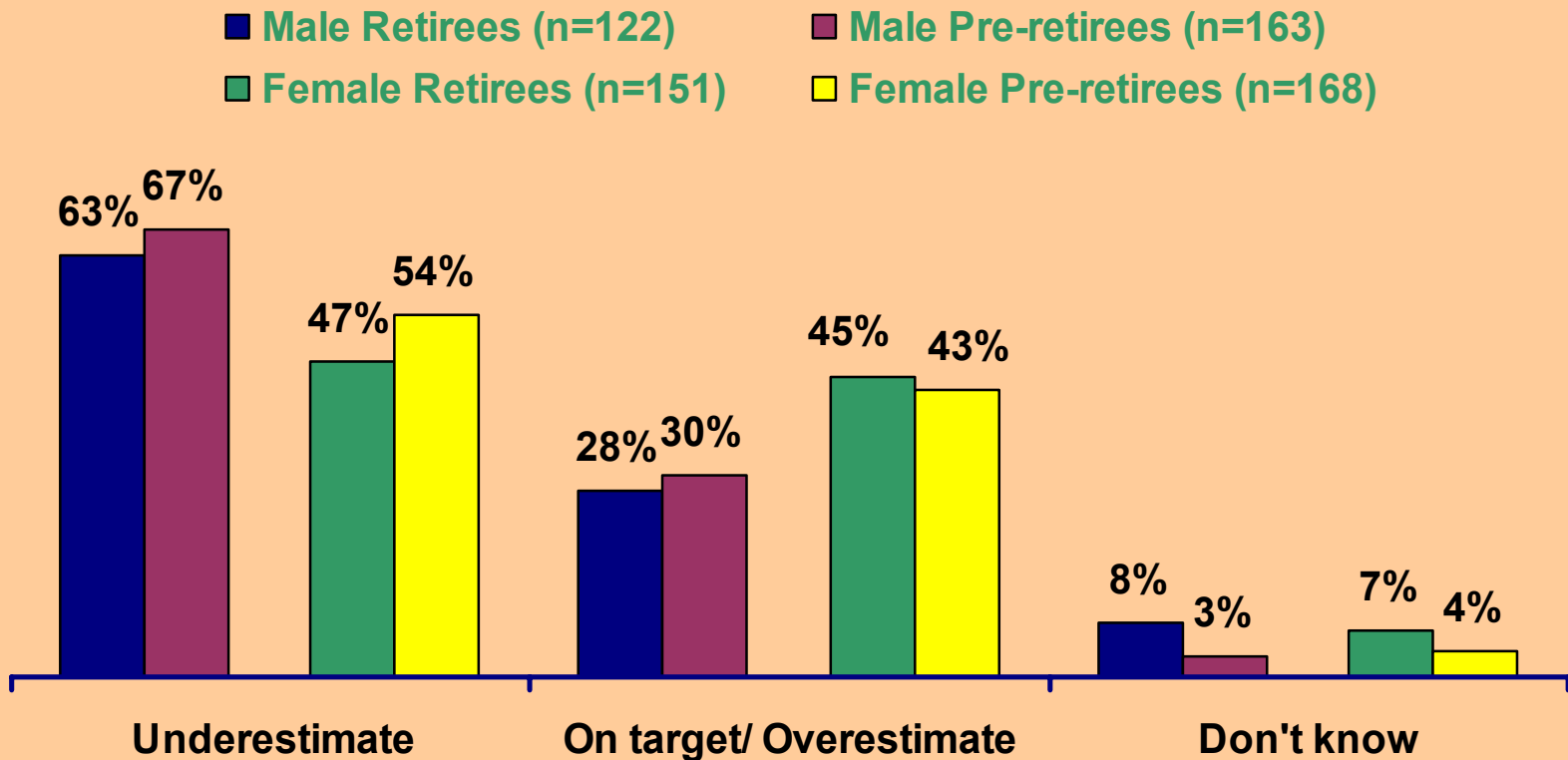
Knowledge and Understanding of Longevity Risk

- Preferences survey shows people prefer regular monthly income, but this is not supported by choices often made
- Seems to be little focus on variability of life span
- Retirement planning software generally asks for expected date at death
- Outliving assets not a major concern and very incomplete understanding of longevity risk protection
- We believe the public overvalues lump sums compared to regular lifetime income



Half or more underestimate life expectancy at age 65.

Until what age do you think the average 65-year-old male/female can expect to live?

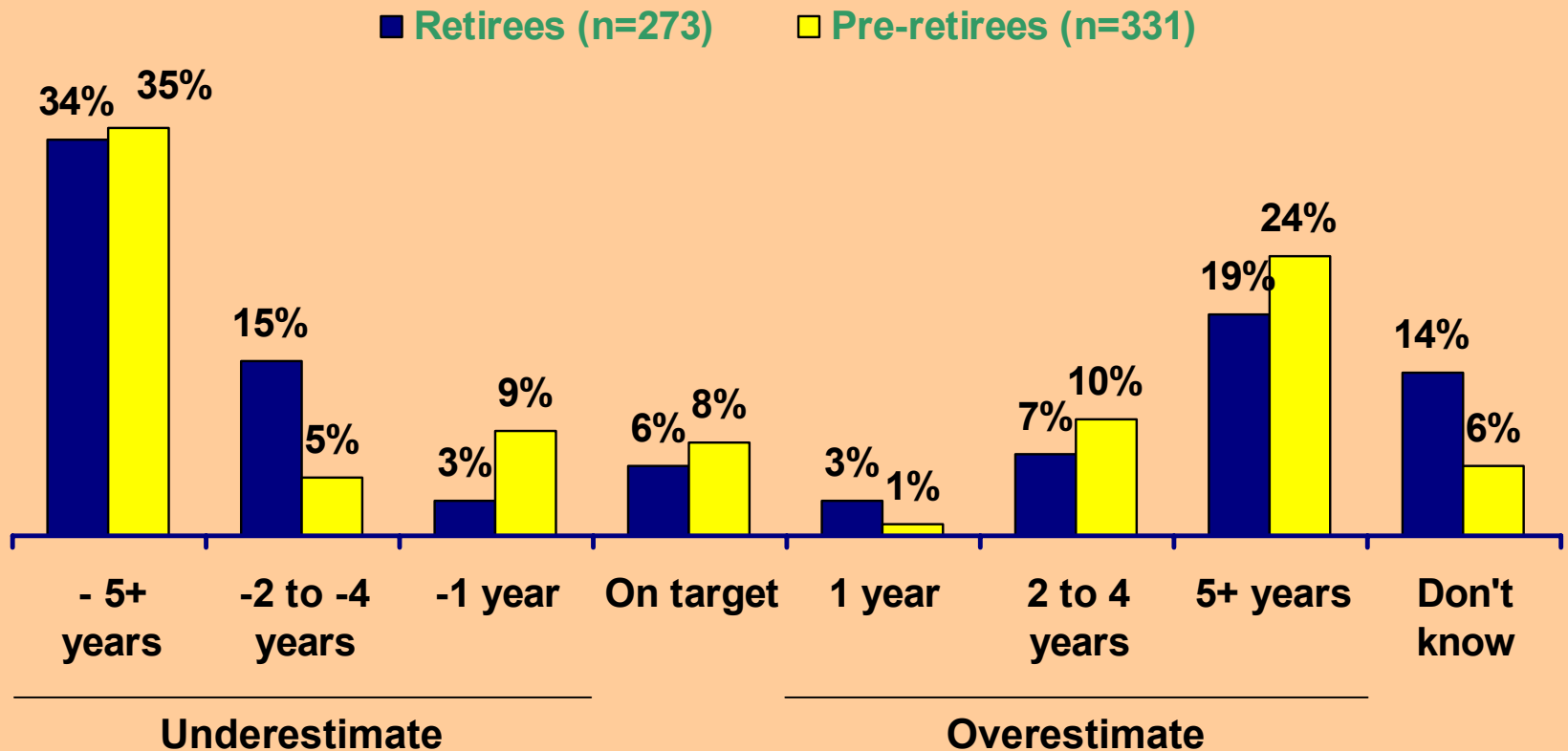


SOA, 2003 Risks and Process of Retirement Survey



Half may underestimate personal life expectancy.

Comparison of response from “And until what age do you think that you, yourself, can expect to live?” with actual life expectancy by age



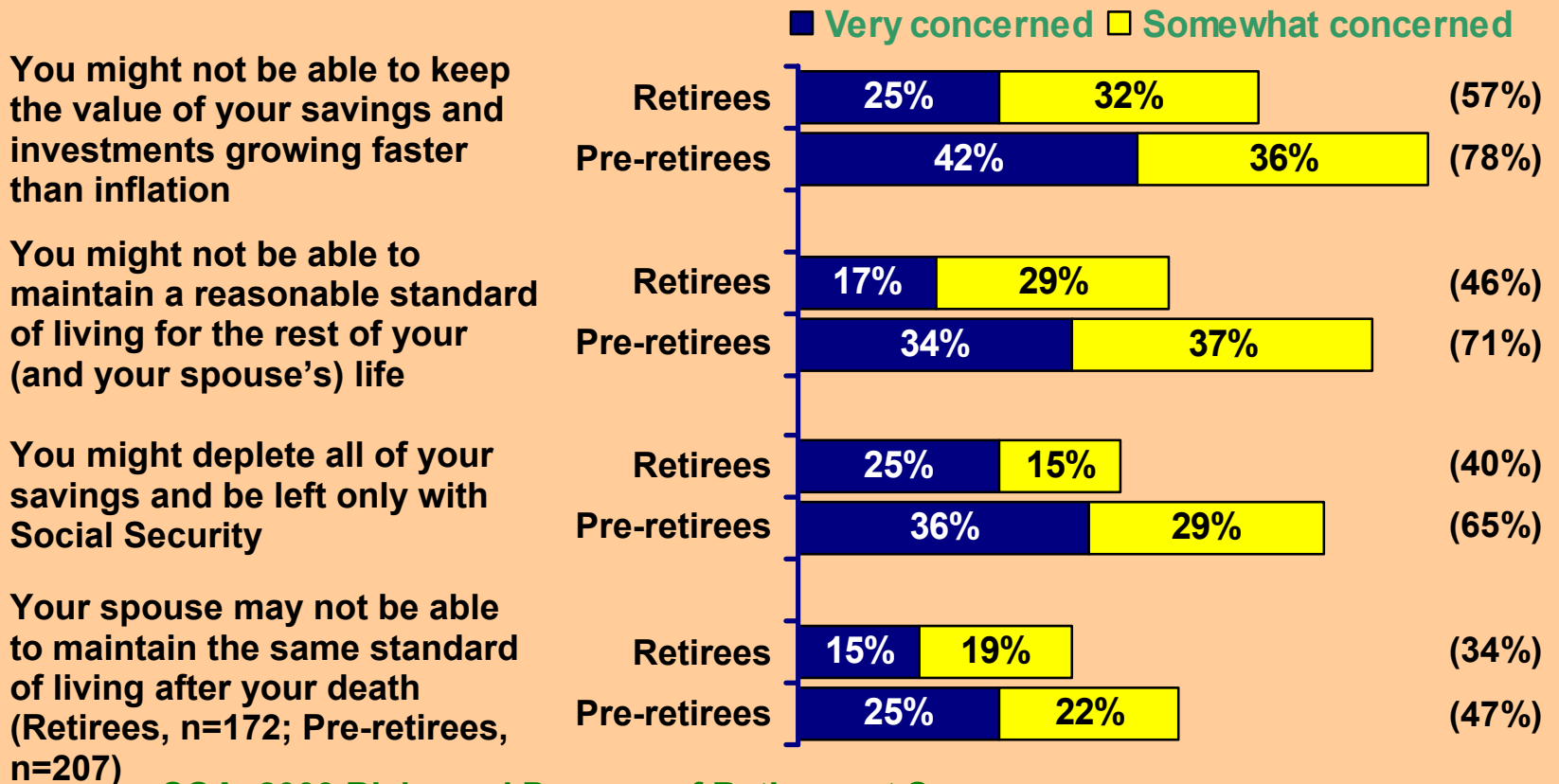
SOA, 2003 Risks and Process of Retirement Survey



Retirees' top concern is inflation risk.

How concerned are you that...?

(Retirees, n=273; Pre-retirees, n=331)



SOA, 2003 Risks and Process of Retirement Survey

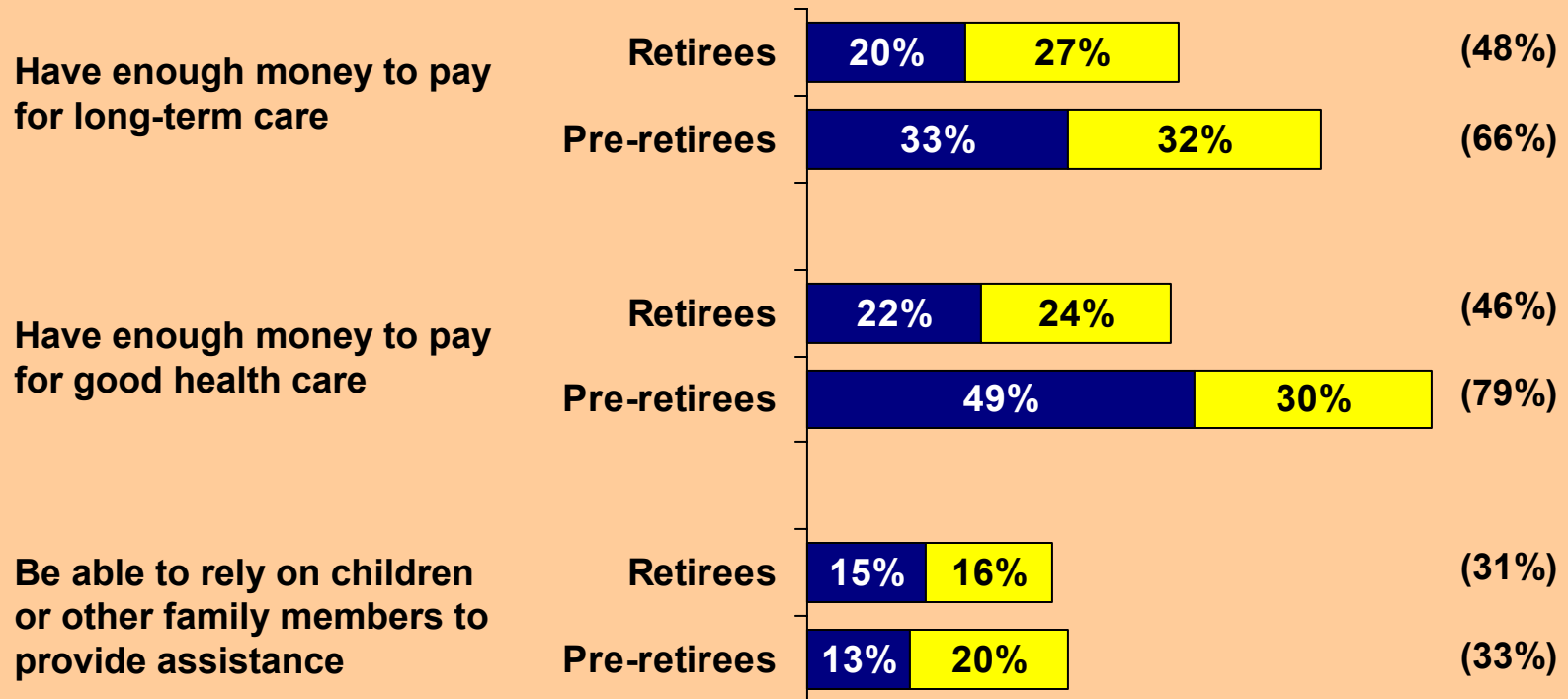


Pre-retirees are more concerned about health care risks than retirees.

How concerned are you that you might not...?

(Retirees, n=273; Pre-retirees, n=331)

■ Very concerned ■ Somewhat concerned



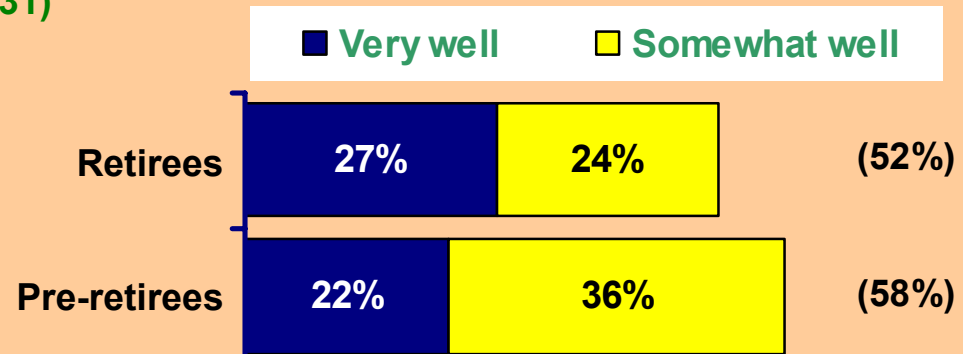
SOA, 2003 Risks and Process of Retirement Survey

Few turn to risk-reducing products to protect themselves.

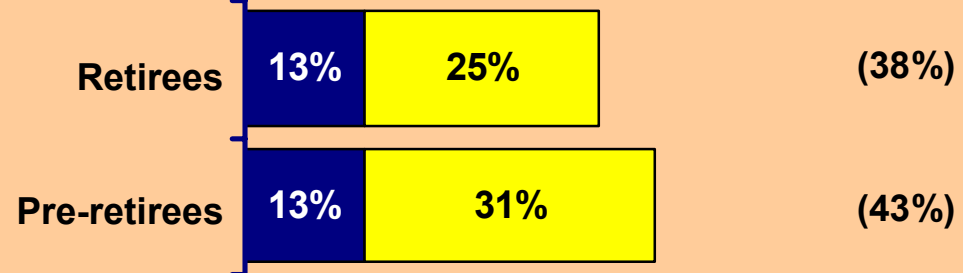
How well does the statement about managing money in retirement describe you (and your spouse)?

(Retirees, n=273; Pre-retirees, n=331)

I think it is a good idea to buy insurance to protect financially against things like the possibility of needing extended nursing care.



I think it is a good idea to buy annuities, because they protect people by paying a guaranteed income for life, no matter how long you live.



SOA, 2003 Risks and Process of Retirement Survey

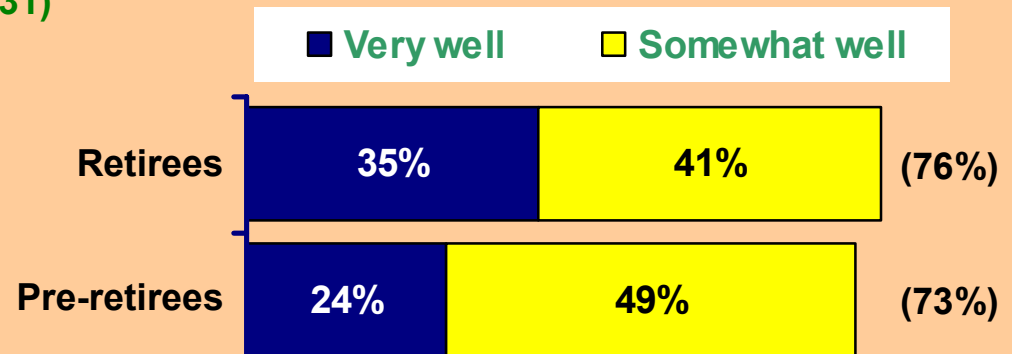


Instead, people try to reduce spending.

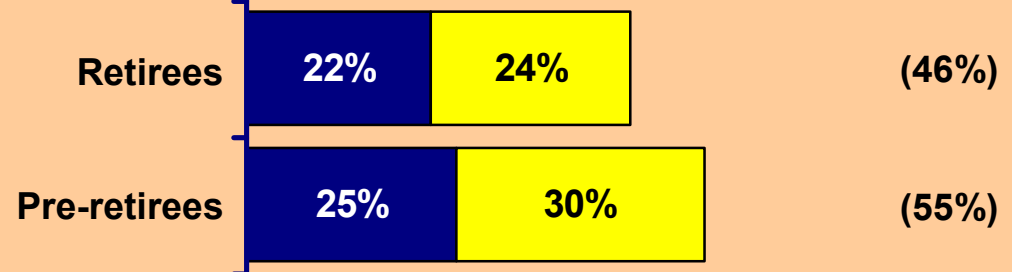
How well does the statement about managing money in retirement describe you (and your spouse)?

(Retirees, n=273; Pre-retirees, n=331)

I try to reduce unnecessary spending so that I can set aside as much money as possible to keep the value of my savings growing.



I try to invest a considerable portion of money in stocks and stock mutual funds, hoping that in the long run their value will rise.

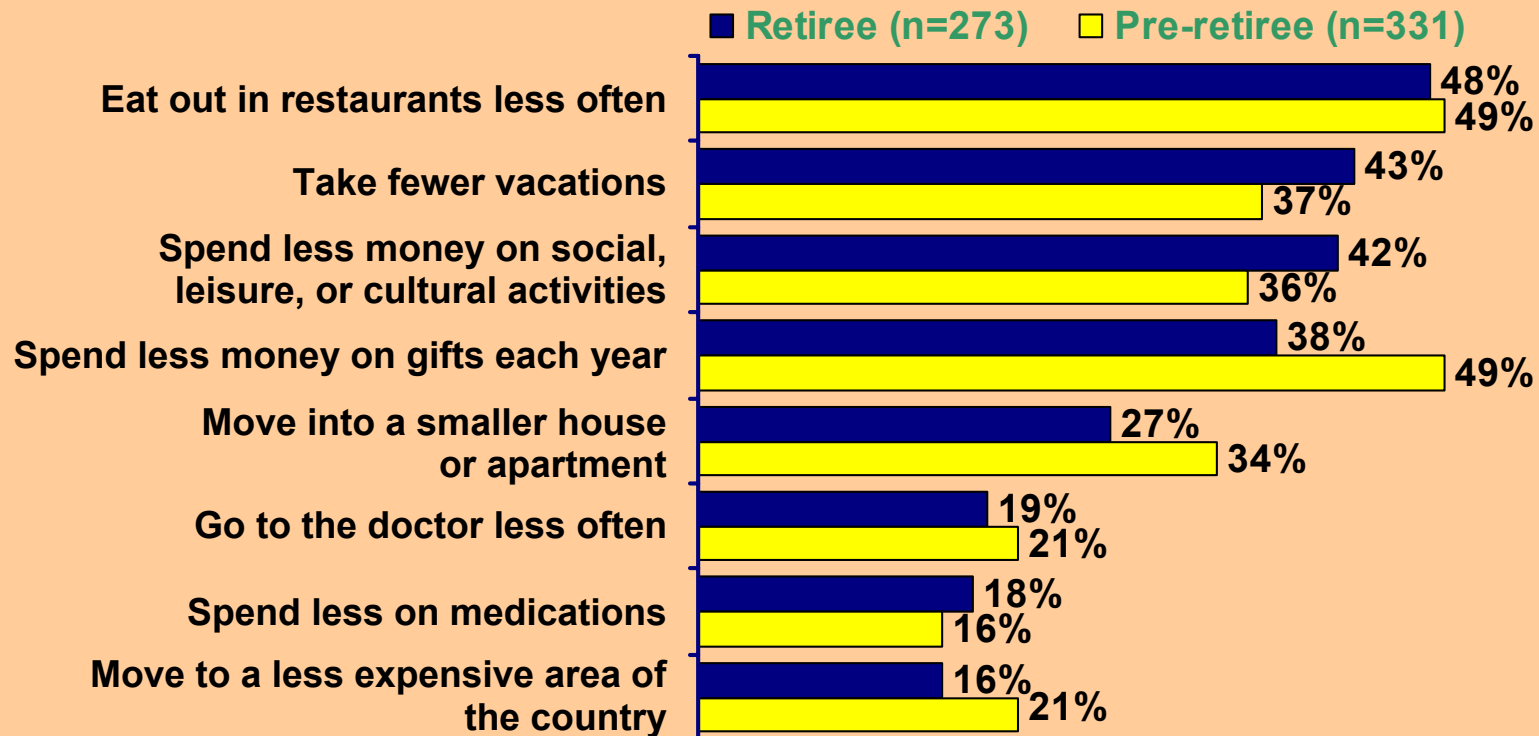


SOA, 2003 Risks and Process of Retirement Survey



If necessary, many think lifestyle reductions would be acceptable.

If you found yourself needing to reduce your living expenses, how acceptable would it be for you (and your spouse) to do each of the following? (% saying very acceptable)



SOA, 2003 Risks and Process of Retirement Survey



Comments

- Potential for many people to have financial problems in retirement
- Awareness of risk often does not drive action to manage the risk
- Decline in DB plans and employer-sponsored health care coverage makes individuals' gaps in risk management strategies more serious



Key Messages

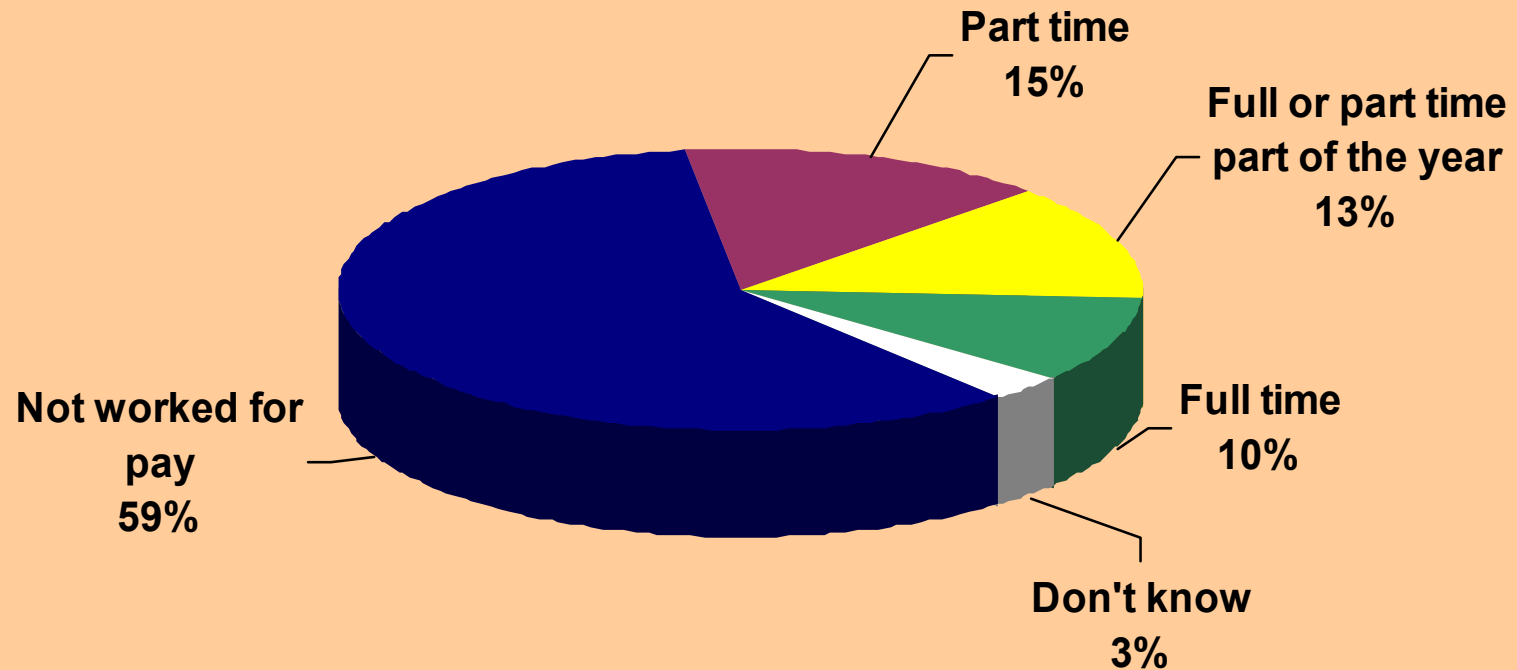
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- Pre-retirees are much more concerned about retirement security than in 2001.
- People do not assess and manage risk well.
- The emerging pattern of phasing into retirement is here to stay.



Phased retirement already exists informally.

In the past 12 months, have you worked for pay . . . ?

(Retirees working only at a young age, sporadically, or never employed omitted, n=242)

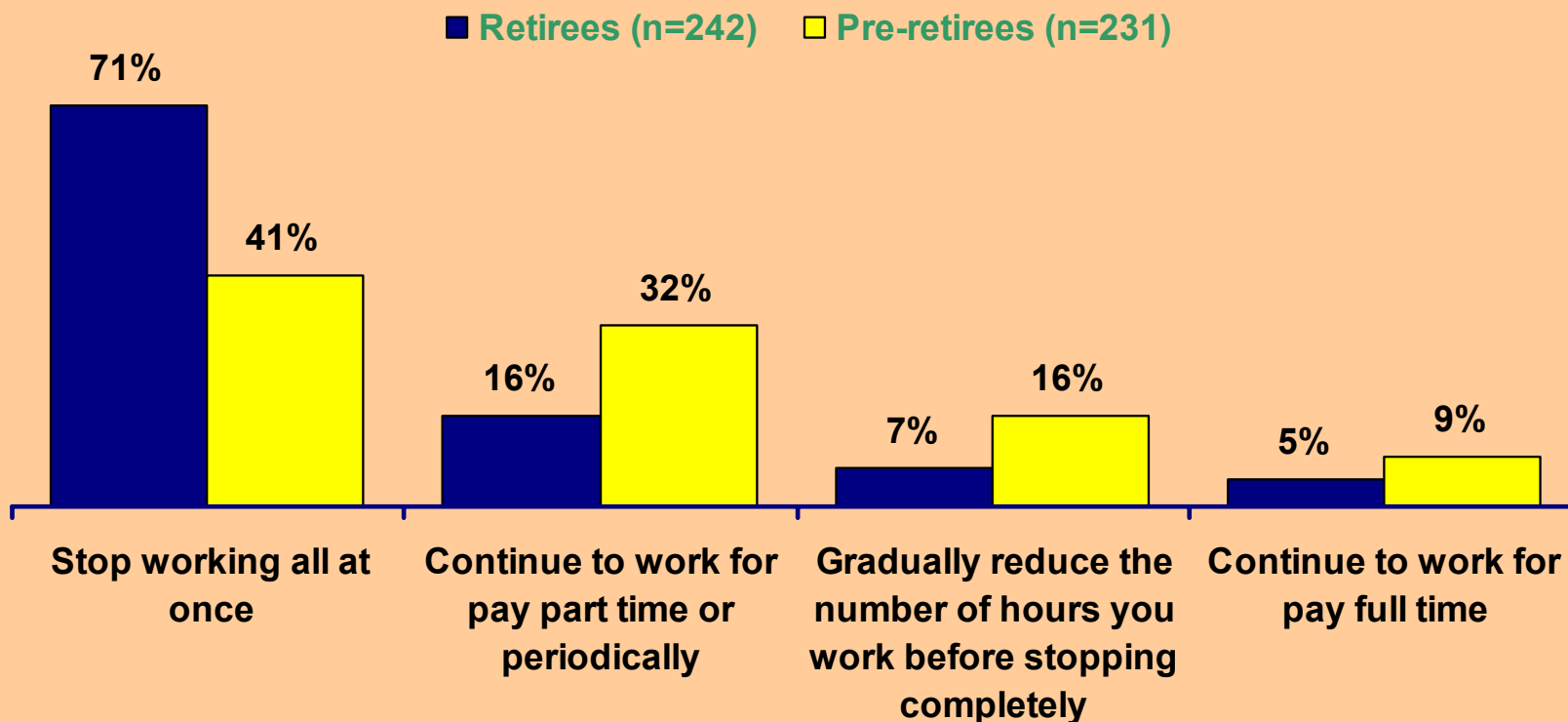


SOA, 2003 Risks and Process of Retirement Survey

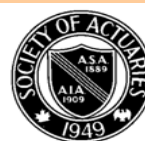


And phased retirement will increase in the future.

Which statement comes closest to describing how you retired/plan to retire from your primary occupation? (those working only at a young age, sporadically, never employed or never planning to retire omitted)



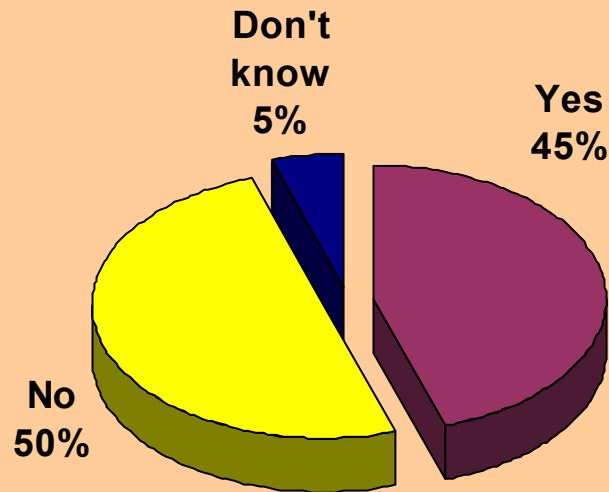
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Many would alter plans if they could collect their pension during phased retirement.

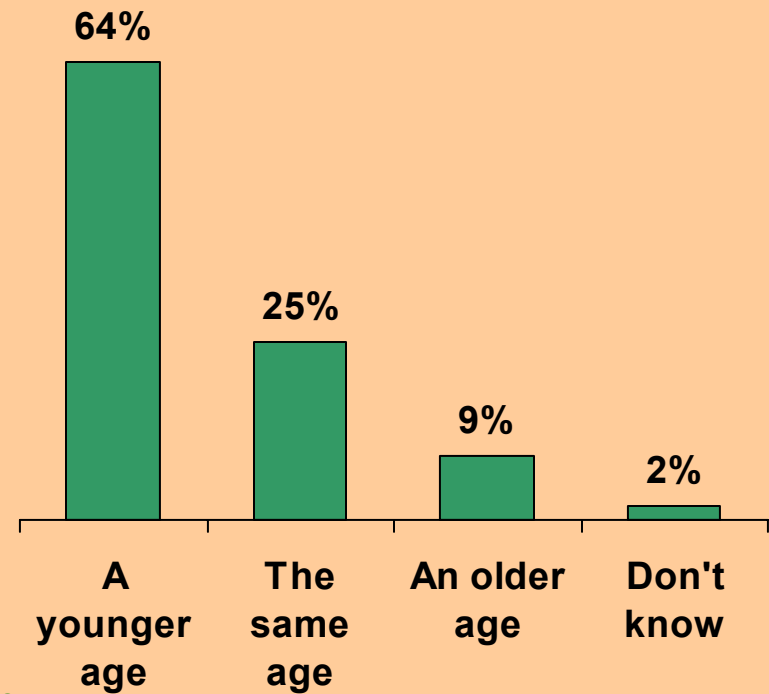
If this law were changed so that you could cut back on your working hours, but at the same time start collecting some of your pension, would this change your plans for retirement?

(Pre-retirees expecting pension from last employer, n=122)



Do you think you would start to retire at . . . ?

→
(n=55)



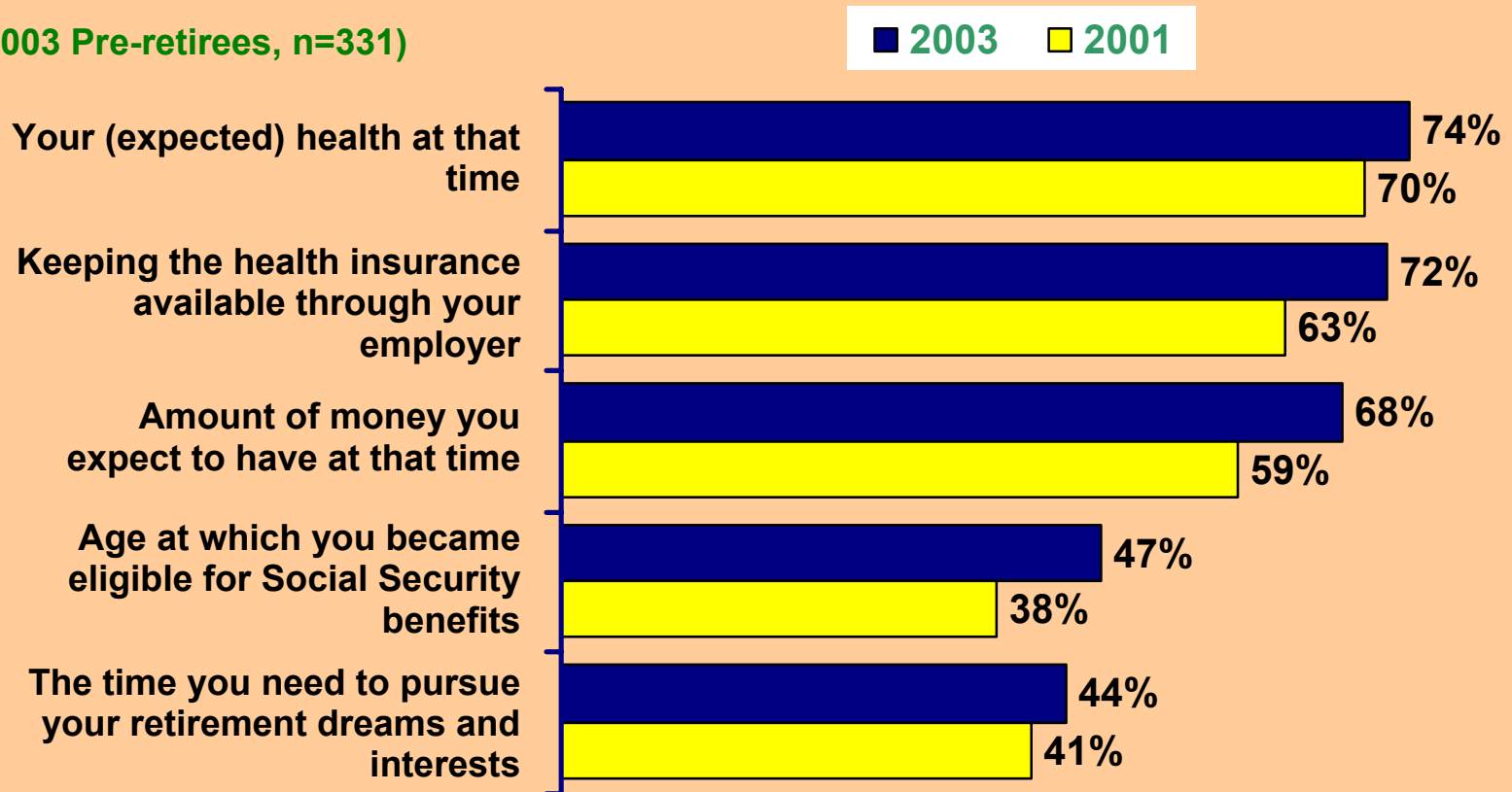
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Pre-retirees are now more likely to say finances matter in decision when to retire.

How important are the following factors in your plan to retire at that age? (% saying very important)

(2003 Pre-retirees, n=331)



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In reality, some retirees have little control of their retirement date.

What event or situation occurred/will occur at that leads you to say you retired/will retire at that age? (among those providing age at retirement)

Top mentions (multiple responses accepted)	Retirees (n=242)	Pre-retirees (n=231)
Stopped working completely	22%	20%
Health problems/became disabled	19%	5%
Company closed/downsized	11%	--
Started receiving pension	10%	18%
Switched to another career	7%	4%
Family member had medical problem	5%	--
Got tired of working/ready to retire	5%	2%
Had enough money to stop working	5%	19%

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Comments

- Phased retirement should be an area of policy focus
- Today, most phasing into retirement is informal
- Significant policy barriers to formal programs
 - Academy letter to the IRS



Key Messages

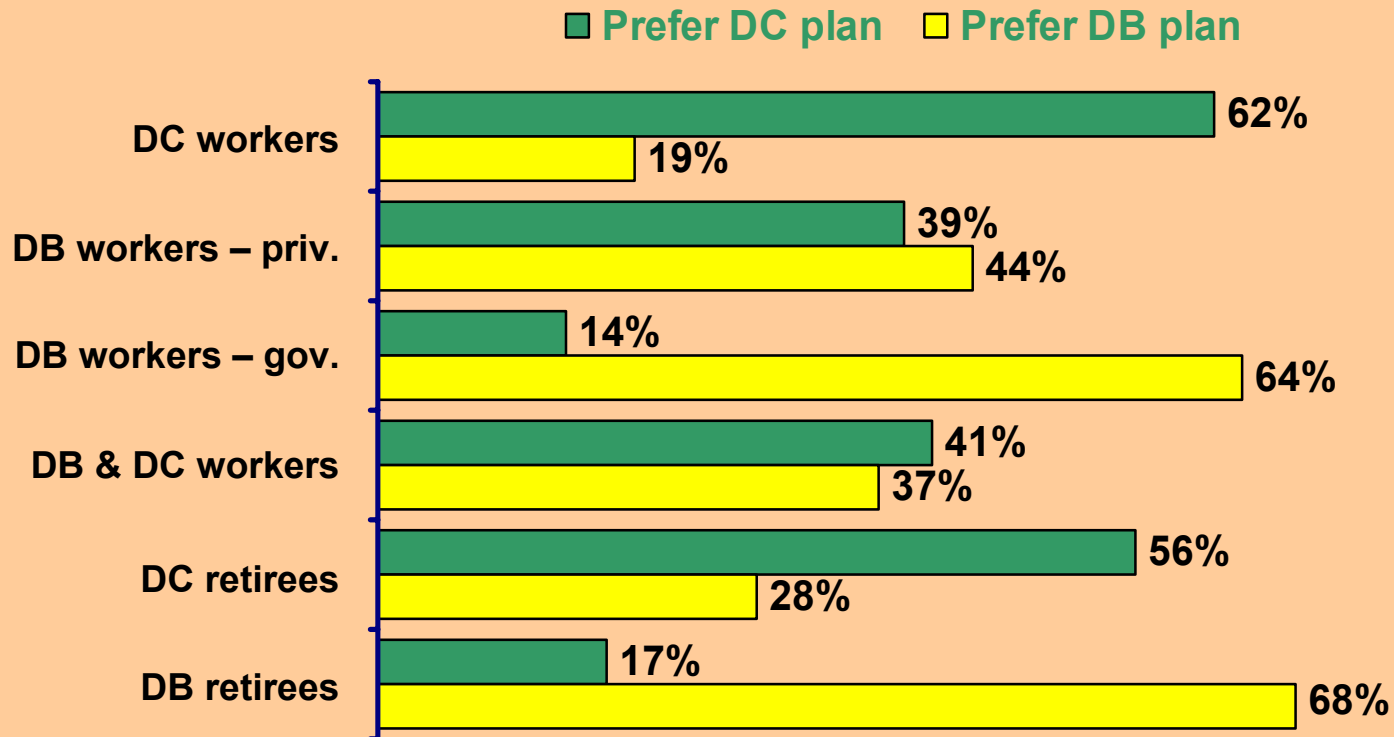
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- People tend to express a preference for the type of retirement plan they already have.



Generally, DC participants prefer DCs; DB participants prefer DBs.

Regardless of the type of plan(s) your employer provides/provided, which type of retirement plan would you prefer?

(Workers, n=790; Retirees, n=600)



SOA/Academy, Retirement Plan Preferences Survey



Comments

- DB is a valuable part of the portfolio
 - More effective in covering low-income employees than contributory DC plans
 - Don't depend on employee contributions
 - Investment of DB funds is more efficient than DC and they make financial markets more efficient
 - Help participants manage risk
- Need a more level regulatory playing field



Summary

- Individual responsibility is growing in importance
 - In preference study: 88% of retirees had DB vs. 49% of workers
 - About half of the workers currently not in employer plans
 - Less have retiree health benefits
- From 2001 to 2003 pre-retirees increased risk focus



Summary (continued)

- Significant gaps in knowledge
- Major risk management strategy is “reduce spending”
- Very limited use of financial products for risk management
- Work growing in importance as part of retirement



Workers have other significant knowledge gaps.

- Cannot estimate eventual retirement benefit:
 - 50 % of DC workers, 34% of DB workers
- Do not know method used to determine benefit:
 - 22% of DC workers, 12% of DB workers
- Cannot estimate current termination benefit:
 - 33% of DC workers, 39% of DB workers
- Do not know when they would be able to access that termination benefit:
 - 25% of DC workers, 20% of DB workers

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Recommendations

- Make it easier for people to assess and manage risk
 - Education
 - Options
 - Default options that reduce risk
- Make it easier for people to phase into retirement
- Level the playing field to make DB plans more attractive to employers



Recommendations

- Make it easier for participants to get regular lifetime income from DC plans
- Build default options into DC plans that make automatic choices towards retirement security
 - Enrollment
 - Investment
 - Distribution



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