

When the Nest Egg Cracks: Managing Risks in Retirement

Richard W. Johnson, Gordon B.T. Mermin, Cori E. Uccello
The Urban Institute

Presented at the 7th Annual Joint Conference of the
Retirement Research Consortium

August 11-12, 2005

Many Things Can Go Wrong at Older Ages

- Serious medical conditions are common
- Long-term care costs can be staggering
- Widowhood and divorce result in the loss of the spouse's income
- Job layoffs in the years prior to retirement can be especially costly

We Examine the Different Types of Negative Events that Strike at Older Ages

- Compute prevalence of medical conditions, disability, parental frailty
- Compute incidence of new medical conditions, disability, parental frailty, widowhood, divorce
 - over about 10 years
- Examine their impact on wealth and the chances of falling into “poverty”

Health and Retirement Study (HRS)

- Respondents age 51-61 in 1992, in community
 - re-interviewed every other year until 2002
 - 7,968 adults
- Respondents age 70+ in 1993, in community
 - re-interviewed in 1995, 1998, 2000, 2002
 - 5,880 adults
- Sample includes those who die before 2002
 - 10% of younger cohort & 42% of older cohort die
 - we exclude those who drop out for other reasons

Key Negative Events

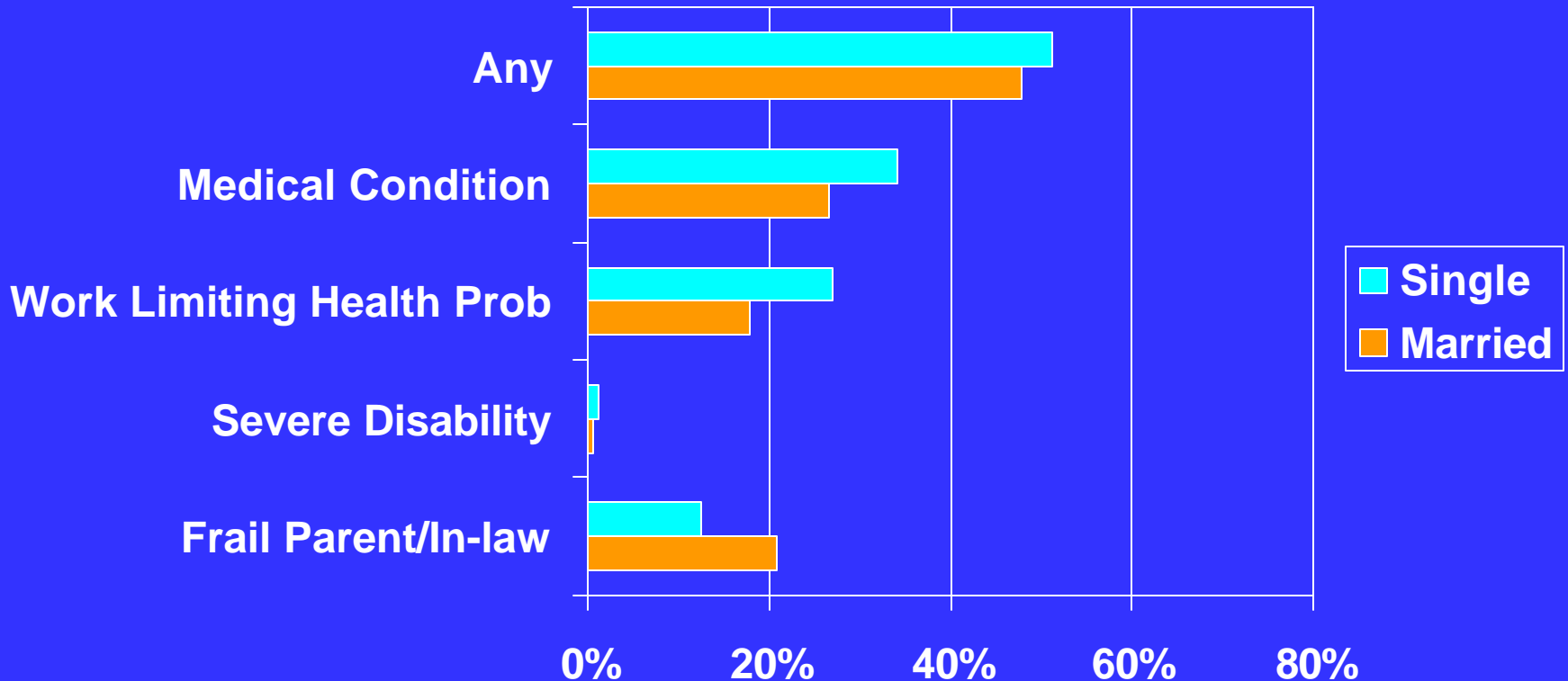
- Major Medical Condition (diagnosed by physician)
- Severe Disabilities
 - age 51-61: limitations with 2 or more ADLs (out of 3)
 - age 70+: limitations with 3 or more ADLs (out of 6)
- Presence of health condition that limits work
 - age 51-61 only
- Severe cognitive impairment
 - age 70+ only
- Spell of nursing home care

Key Negative Events (continued)

- Presence of frail parent
 - age 51-61 only
- Widowhood
- Divorce
- Job layoff
 - age 51-61 only

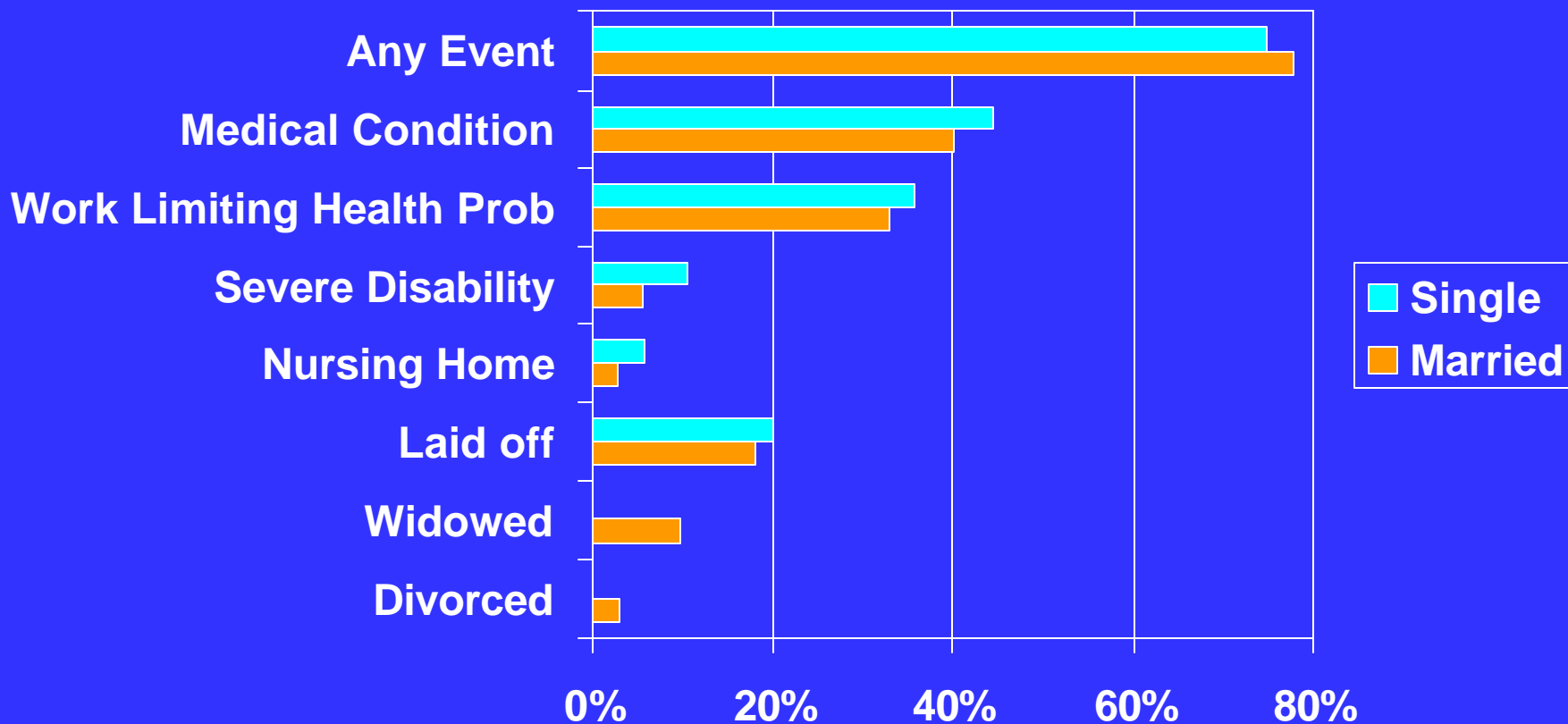
About One-Half of Adults Age 51-61 Have Health Problems or a Frail Parent or In-Law

Prevalence of Health Problems, Frail Parents,
Age 51-61, 1992



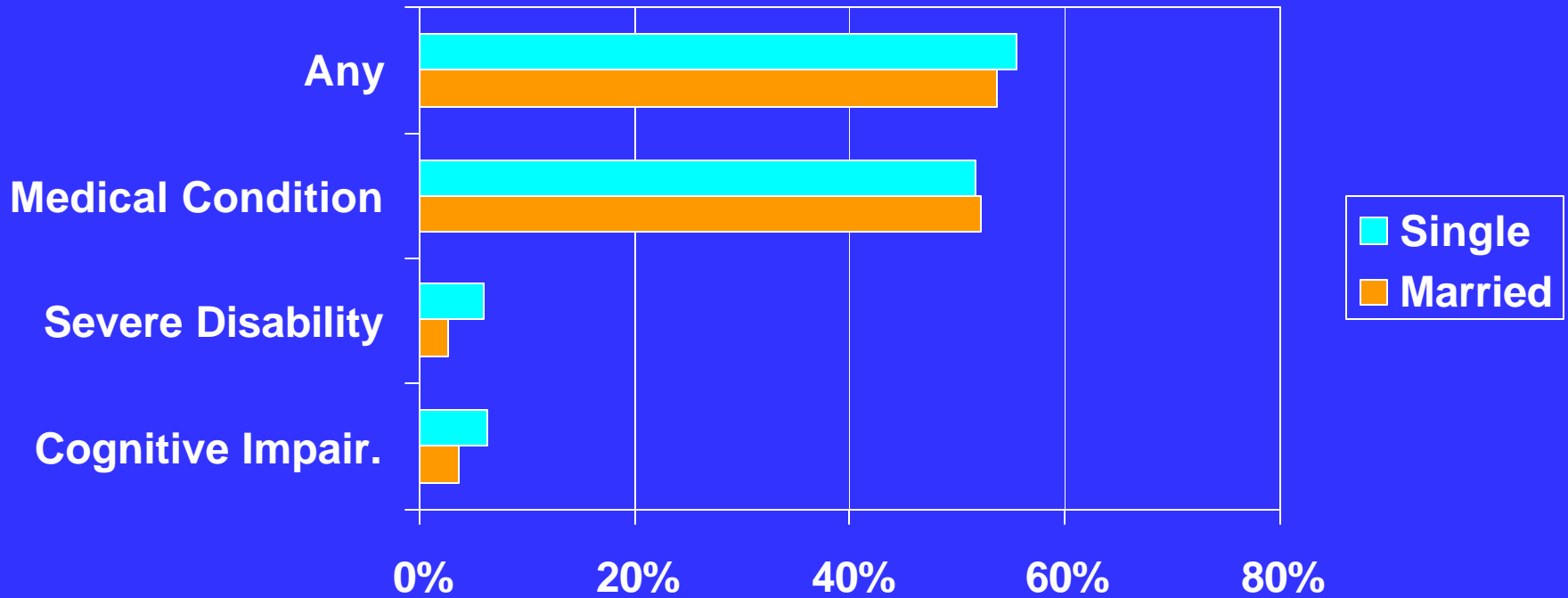
About Three-Quarters of People Age 51-61 Experience Negative Shocks Over 10 Years

Incidence of Negative Events, 1992-2002,
Age 51-61 at Baseline



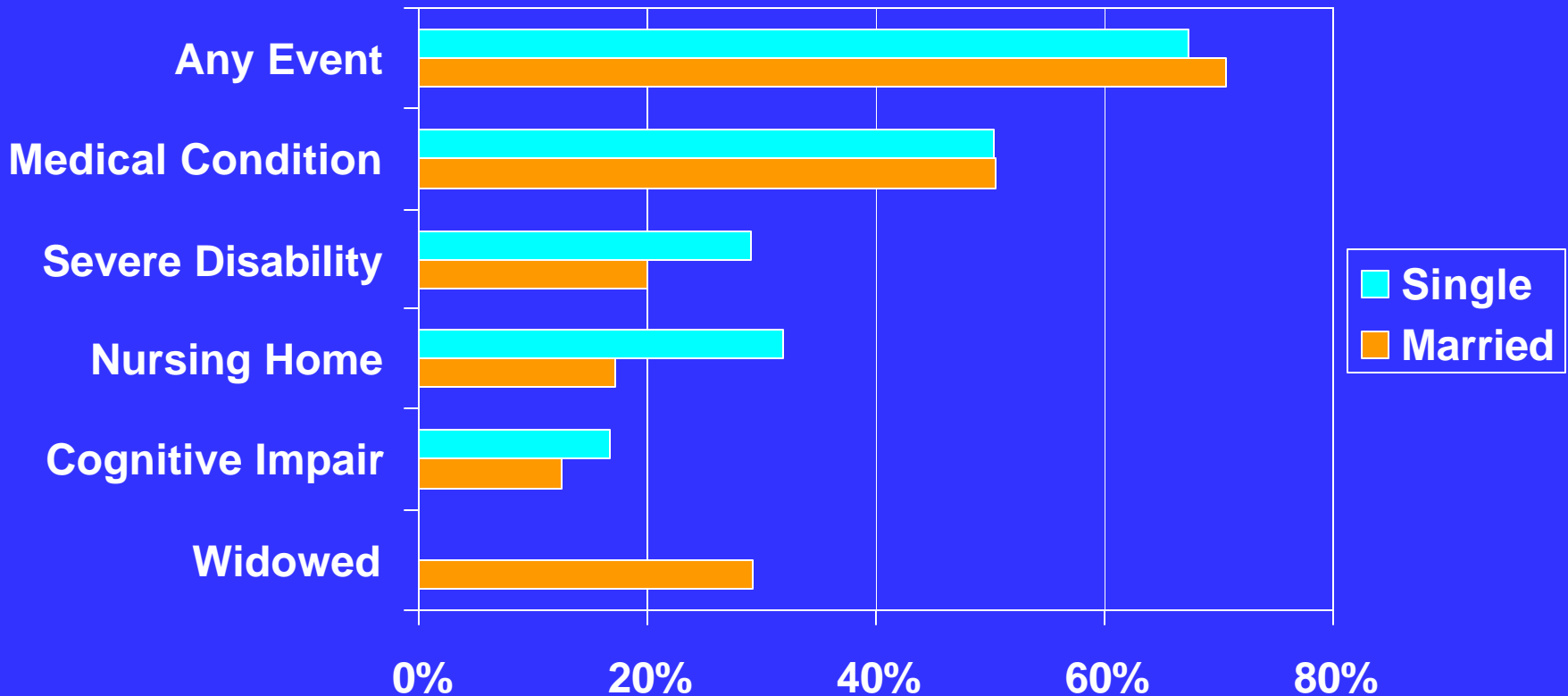
More Than Half of Adults Age 70+ Report Health Problems

Prevalence of Health Problems, Age 70+, 1993



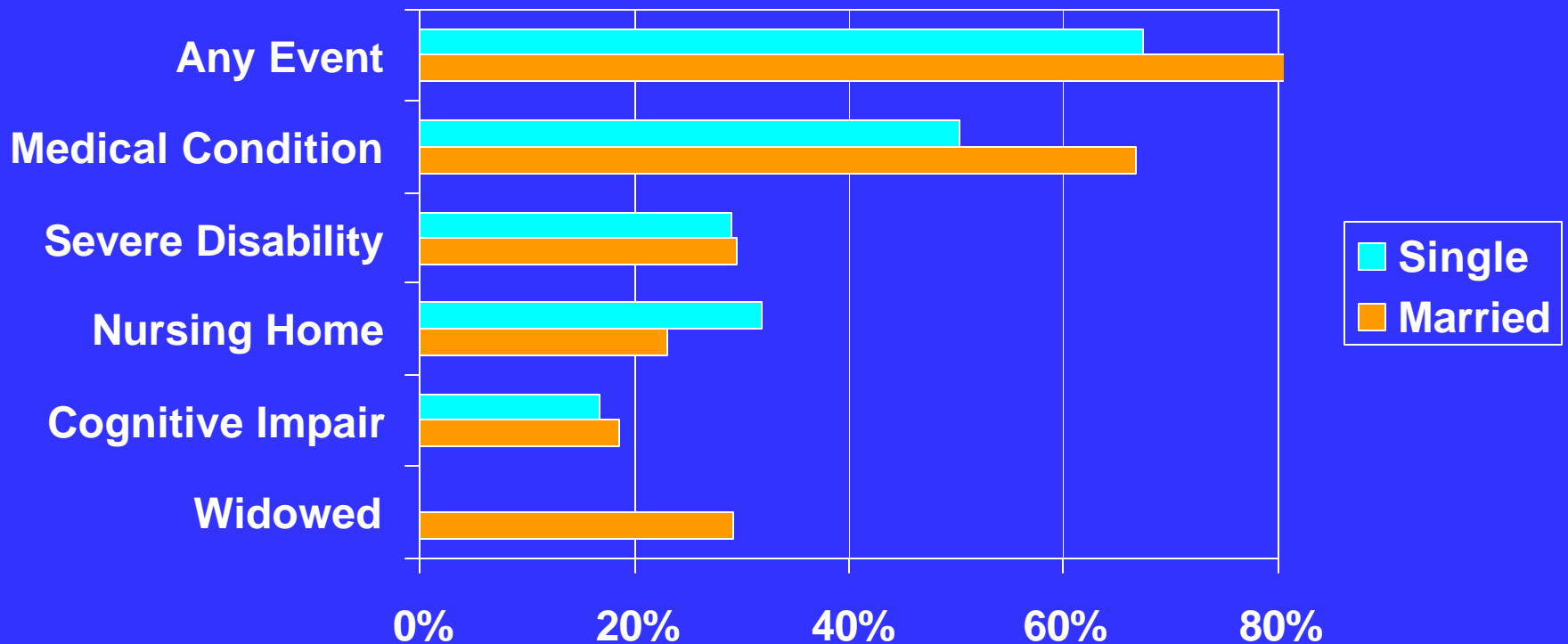
About Two-Thirds of People Age 70+ Develop Health Problems or Become Widowed Over 9 Years

Incidence of Negative Events, 1993-2002,
Age 70+ at Baseline



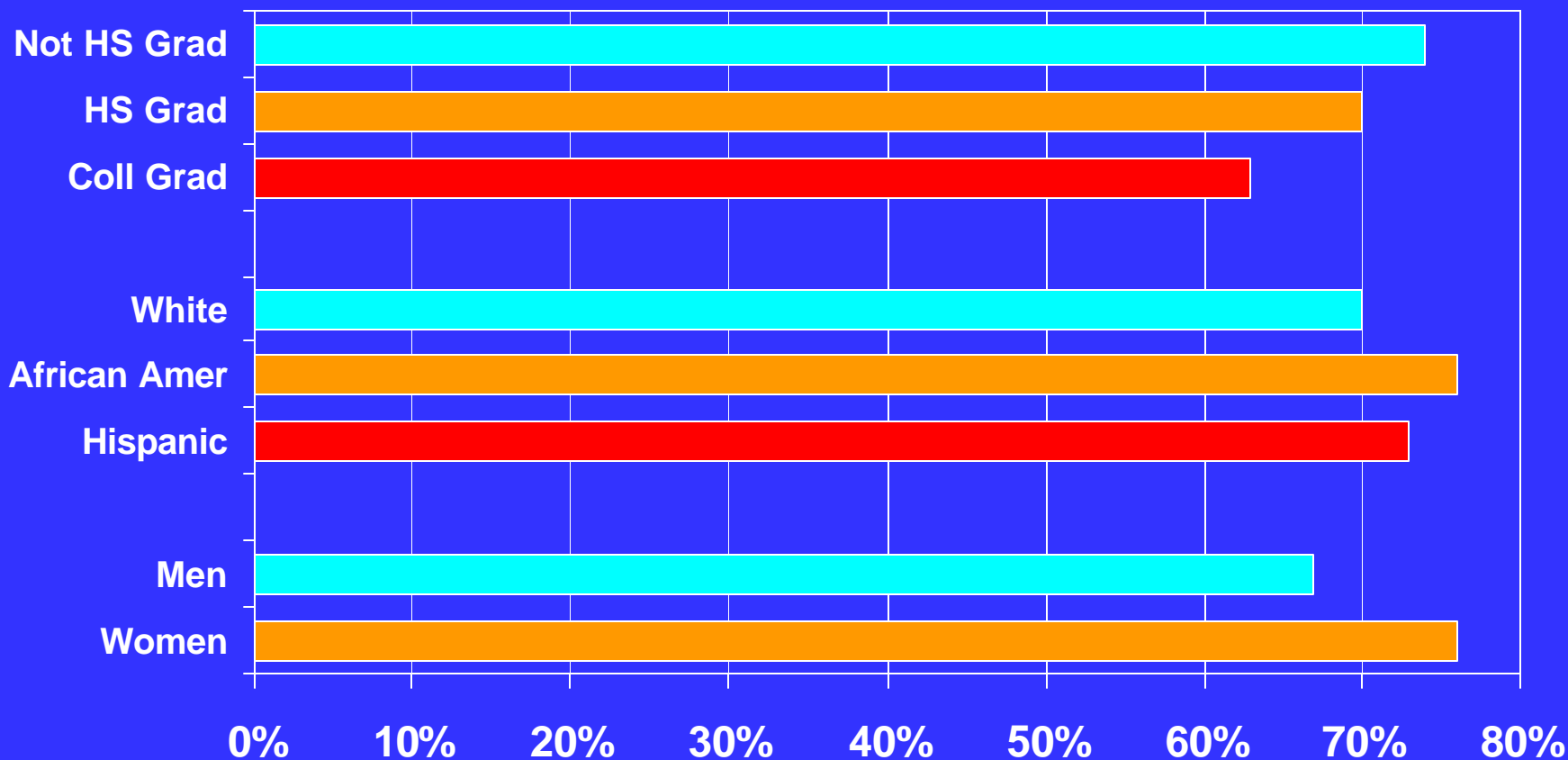
Accounting for Onset of Spousal Health Problems Increases Estimated Incidence of Negative Shocks at Age 70+

Incidence of Own and Spouse Negative Events, 1993-2002,
Age 70+ at Baseline



College Graduates Age 70+ Are Less Likely to Experience Negative Shocks than Adults with Limited Schooling

Incidence of Negative Events, 1993-2002,
Age 70+ and Married at Baseline



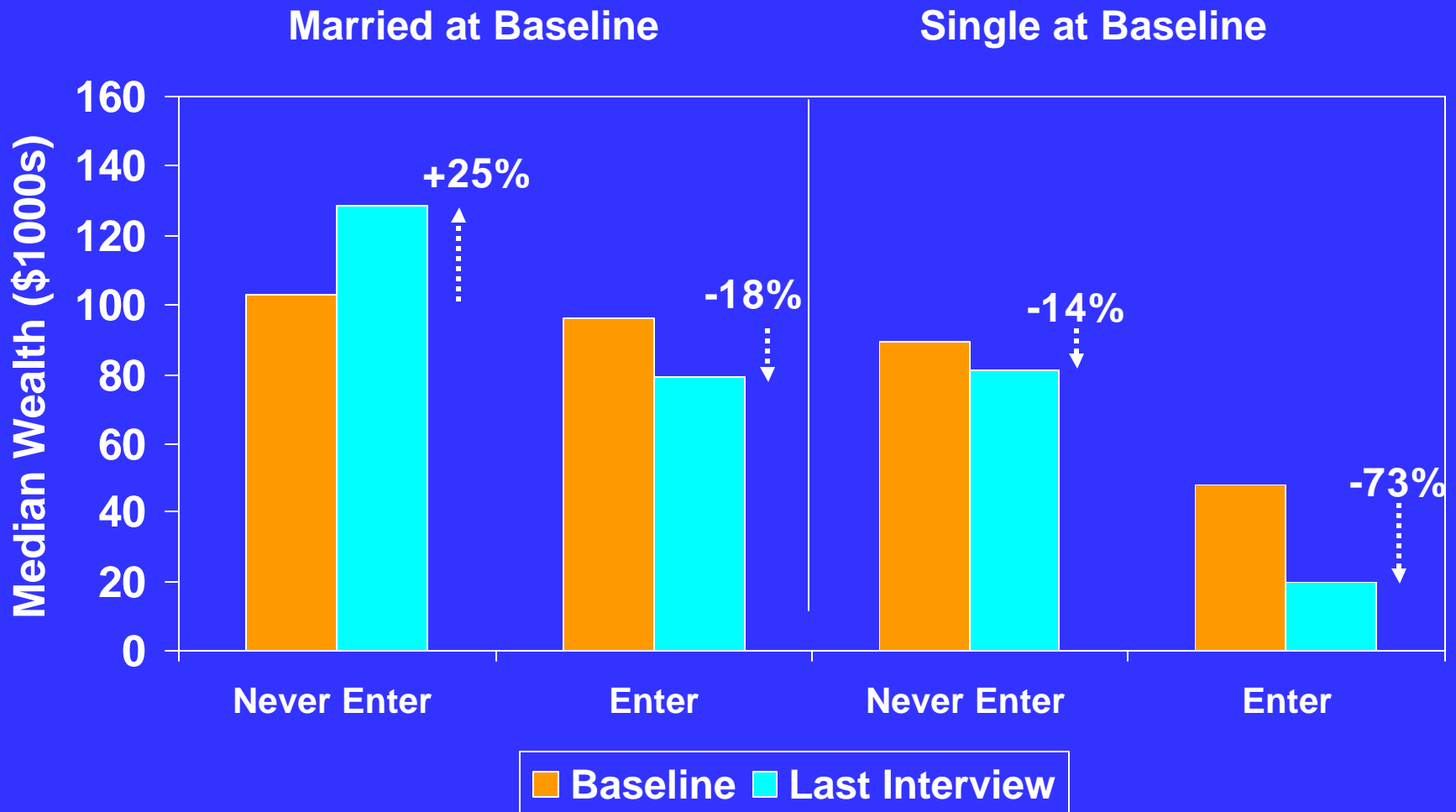
How Does Household Wealth Vary by Onset of Negative Events?

- Adults 70+ in 1993
- Compare wealth in 1993 and in 2002 (or death)
- Wealth includes housing, financial assets, other real estate, vehicles, and businesses, net of debt
 - Does not include DB pension and Social Security wealth
- Adjusted for inflation (2001 dollars)

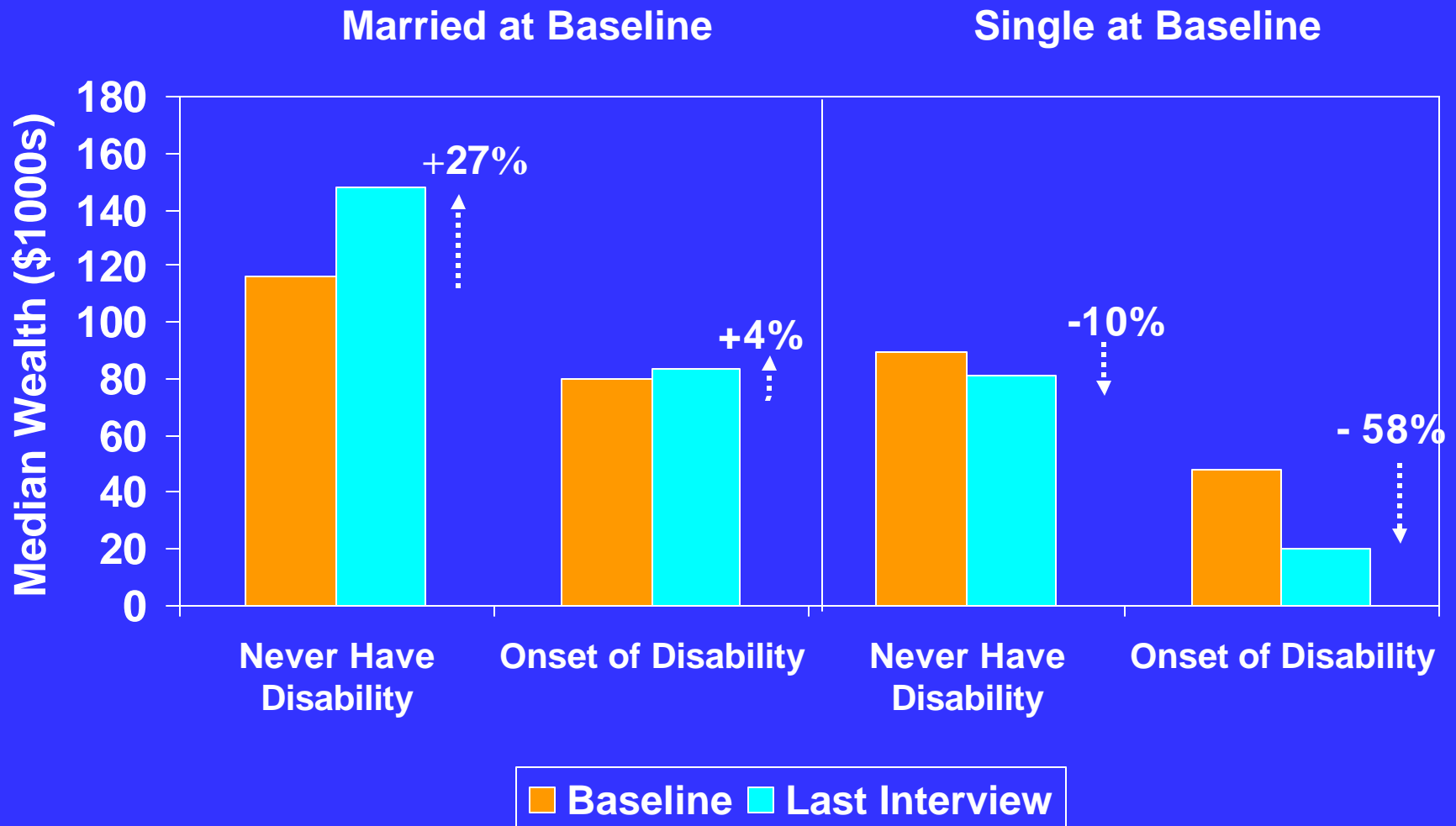
Need to Adjust Wealth for Household Size

- Single people need fewer resources than married people
 - But couples save some by sharing expenses
- Analysis divides wealth of married couples by 1.62
 - Middle of the range of equivalence scales recommended by National Academy of Sciences (1995)

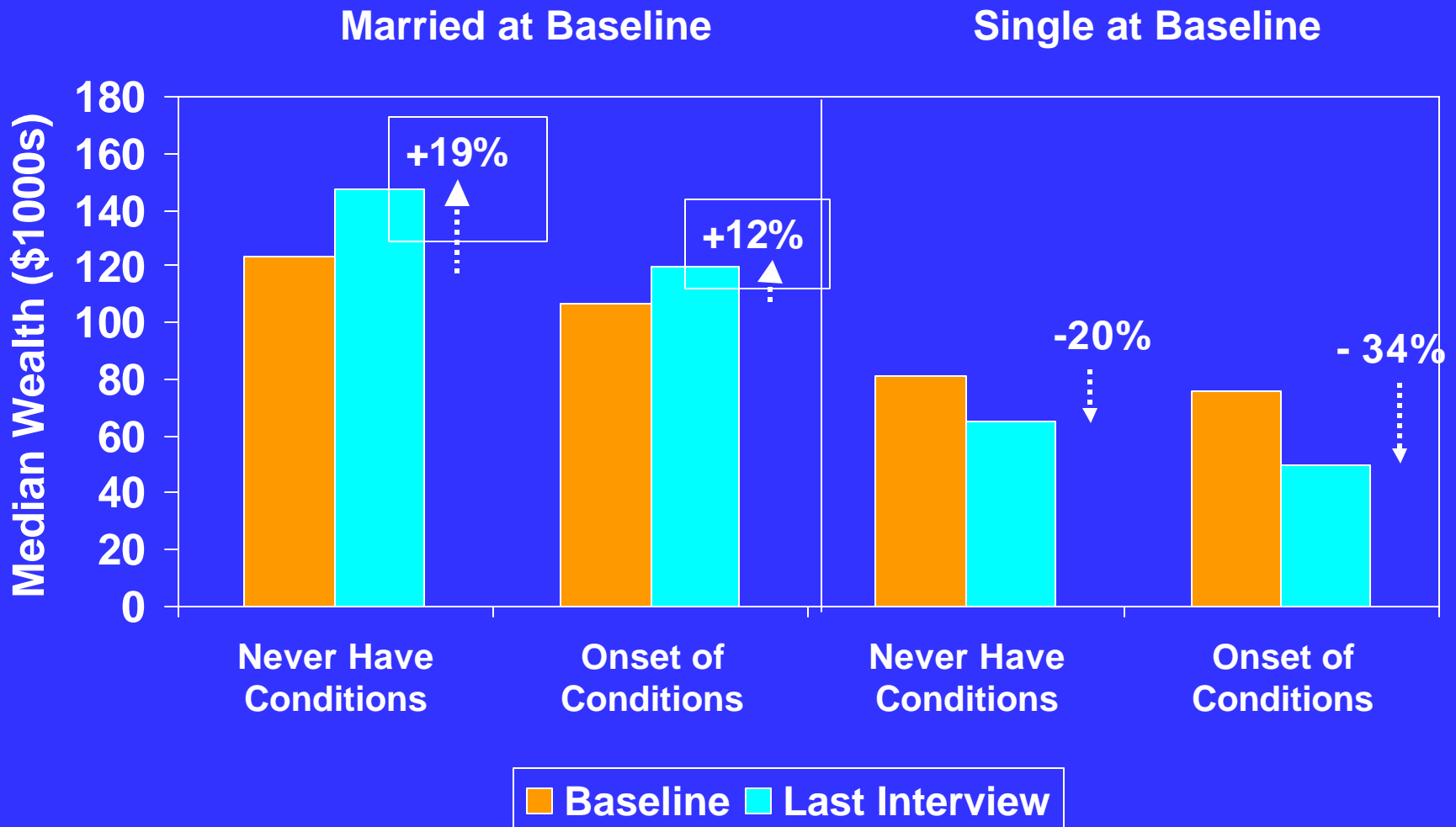
Change in Median Wealth Less Favorable for Adults 70+ Entering Nursing Homes



Median Wealth Grows Less or Declines More for Adults 70+ Who Experience Onset of Disability



Median Wealth Grows Less or Declines More for Adults 70+ Who Experience Onset of Major Medical Conditions



Multivariate Analysis of Wealth Levels and Change in Wealth

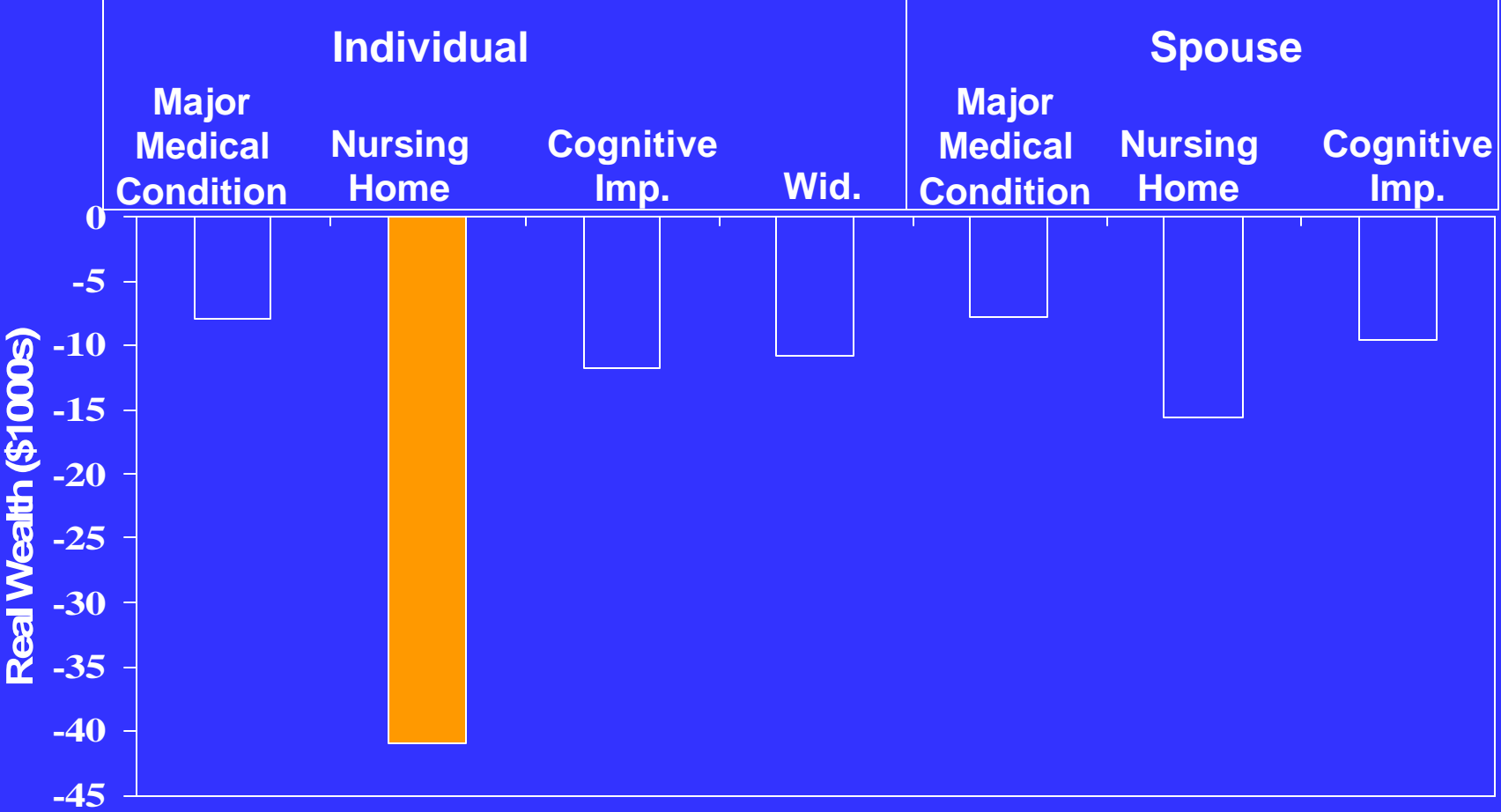
- Adults age 70+ in 1993
- Estimate wealth at last interview and change in wealth over the 9-year period (or until death)
- Median regressions
 - Distribution of wealth and change in wealth are skewed
- Separate regressions by gender and by marital status at baseline

Factors Included in Multivariate Analysis

- Shocks
 - Individual experiences
 - Major medical condition
 - Cognitive impairment
 - Nursing home spell
 - Widowed
 - Spouse experiences
 - major medical condition
 - cognitive impairment
 - nursing home spell
- Other controls
 - Demographics (education, race, age)
 - Individual and spouse health conditions at baseline

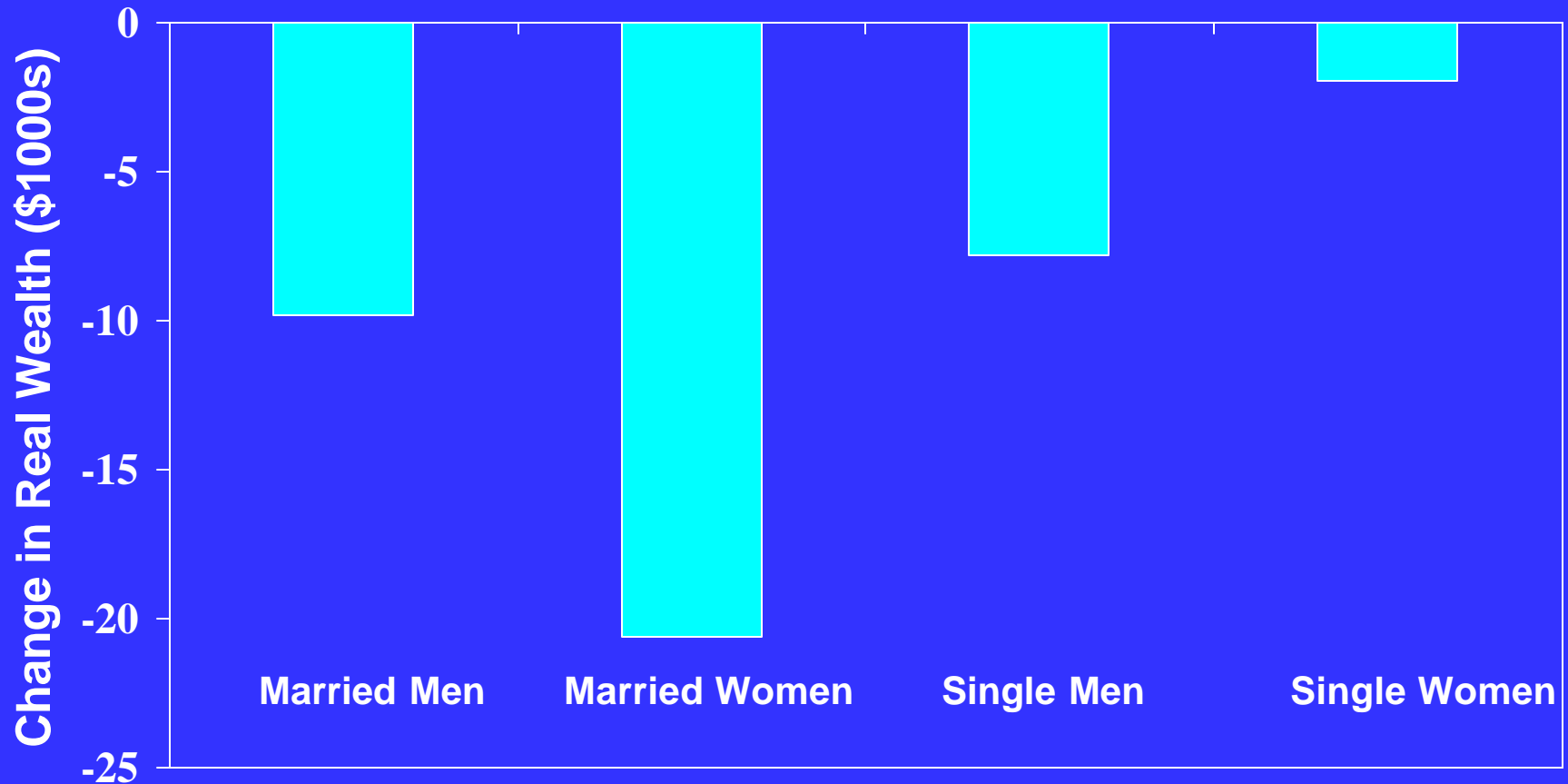
Controlling for Demographics and Baseline Conditions, Nursing Home is the Only Shock Consistently Affecting Wealth

Impact of Shocks on Wealth at Last Interview for Women Who Were Married at Baseline



Controlling for Demographics and Baseline Conditions, Nursing Home Shock Reduces Growth in Wealth

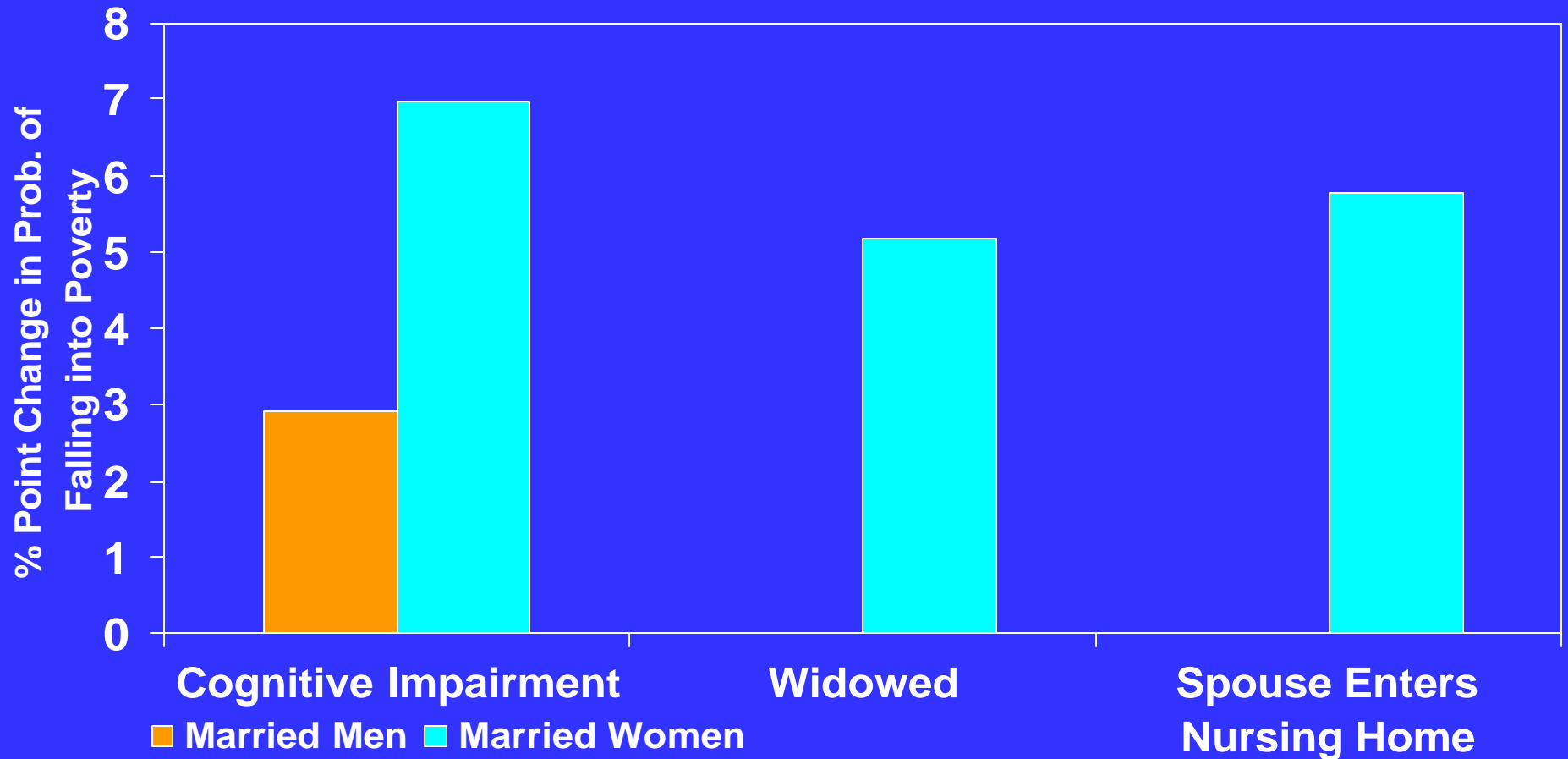
Impact of Nursing Home Shock on Change in Wealth
over the 9-year Period



Multivariate Analysis of Falling into “Poverty”

- Probit estimates of probability of falling into “poverty” between 1993 and 2002 (or death)
- Define an alternative poverty line
 - Same as official poverty line for singles
 - Use singles’ threshold*1.62 for married couples
 - Official poverty line for married couples = singles’ threshold*1.26
- Restricted to adults with household incomes above our “poverty” threshold in 1993

Impact of Shocks on Probability of Falling into “Poverty” Varies by Gender for Adults Who Were Married at Baseline



Conclusions

- Most older people experience some type of negative event over a 10-year period
- People with these shocks end up with less wealth than others
- Except for nursing home entry, these negative events do not reduce wealth after controlling for other factors
- Cognitive impairment and, for women, widowhood and spousal nursing home entry increase chance of falling into “poverty”