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DOES HOUSEHOLD DEBT INFLUENCE THE LABOR SUPPLY AND BENEFIT CLAIMING DECISIONS OF OLDER AMERICANS?

BY BARBARA A. BUTRICA AND NADIA S. KARAMCHEVA

According to data tracked by the Federal Reserve System's Board of Governors, Americans' indebtedness increased dramatically from the late 1980s until just before the Great Recession. In 2007, the typical family with debt owed \$70,600, up from \$25,300 in 1989 (Federal Reserve Board 2010). By 2010, the median value of debt for families with debt was \$70,700, with debt payments accounting for about 18 percent of their disposable income (Bricker et al. 2012).

Indebtedness could affect older adults in two different ways. On one hand, debt might compel older individuals to continue working and delay Social Security benefit claiming into their mid-sixties and beyond so they can pay off their financial obligations. On the other hand, indebted adults who are cash-strapped and unable to service their debt because they are not working or because they do not earn much might claim their benefits as soon as they are eligible to obtain the necessary cash to make their loan payments. Determining which of these opposing effects dominates and how debt influences labor supply and claiming decisions is an empirical question whose answer has important implications for individuals' economic well-being in retirement and for the Social Security program itself.

To our knowledge, this is the first paper to explore the link between older adults' indebtedness and their labor supply and receipt of Social Security benefits. We use data from the *Health and Retirement Study* and find that older Americans are more and more likely to have debt, they carry increasingly larger amounts of debt, and they are more leveraged than ever. Between 1998 and 2010, the share of adults ages 62 to 69 with any type of debt increased from 48 to 62 percent. The median value of outstanding debt for those with debt grew from \$19,000 to \$32,100 per person in 2010. And the average debt-to-asset leverage ratio increased from 10 to 18 percent. As for the impact these trends have on the labor supply and benefit claiming decisions of older Americans, we find:

- Nearly half of adults ages 62 to 69 with debt are working, compared with only a third of those without debt. On the flip side, only 71 percent of older adults with debt receive Social Security benefits, compared with 78 percent of those without debt. The differences between those with and without debt are especially noticeable through age 65.

- Even controlling for other factors, we find that having debt is positively and significantly correlated with older adults' propensity to work and negatively and significantly correlated with their likelihood of receiving Social Security benefits. In particular, those with debt are 8 percentage points more likely to work and 2 percentage points less likely to receive benefits than those without debt.
- In addition, the amount of debt also has a statistically significant impact on older adults' behavior; an increase of \$10,000 in debt per person increases the likelihood of working by 0.7 percentage points and reduces the likelihood of receiving benefits by 0.3 percentage points.
- Among the sources of debt, mortgage debt consistently has a stronger impact on labor supply and Social Security receipt than do other forms of debt. Having a mortgage increases the likelihood of working by about 7 percentage points and reduces the probability of receiving Social Security benefits by 3 percentage points. The effects of mortgage debt on work and retirement are even larger among homeowners.
- We also find that older adults with outstanding debt, particularly mortgage debt, are more likely to delay fully retiring from the labor force and to postpone claiming Social Security benefits. For example, close to 65 percent of homeowners with mortgages are still working at age 64, compared with only 54 percent of those without mortgages. Furthermore, almost 50 percent of homeowners with mortgages still have not claimed their benefits by age 65, compared with only 35 percent of those without mortgages.
- Again, these findings hold even after controlling for other factors. For example, having debt reduces the relative probability of fully retiring by approximately 22 percent, and the relative probability of claiming Social Security benefits by 14 percent.

Older adults are supposed to be at the peak of their wealth accumulation and debt-free going into retirement, yet over time they have become increasingly more indebted and more leveraged. Our study suggests that older adults may be dealing with their indebtedness by delaying their retirement and Social Security benefit receipt. Consistently, we find that labor force participation is higher and benefit receipt is lower among those with debt compared with those without debt. We also consistently find that debt is associated with delaying both retirement and Social Security claiming.

Delaying retirement and benefit claiming as long as possible increases financial security in retirement for everyone, but it is especially important for those with debt. So it is encouraging to find that older adults with debt are delaying both retirement and Social Security benefits. At some point, however, age and health prevent most people from working. When that time comes, how will those with debt manage their monthly mortgage and credit card payments? Possibilities include selling their homes, buying reverse mortgages, or declaring bankruptcy.

More than ever, retirement security will depend on retirees having enough income and assets to pay for basic living expenses and to service their debt. Ideally, older adults would pay off their debts well before retirement age. So it is going to be important to identify those who are financially fragile, to better understand their circumstances and to look for ways to help repay their debt before retirement. Financial education, stricter regulations for financial and lending institutions, and controlling health care spending, a major source of debt, are all ways that policymakers might help to achieve this goal.

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CENTER FOR RETIREMENT RESEARCH AT BOSTON COLLEGE

Hovey House, 140 Commonwealth Avenue, Chestnut Hill, MA 02467-3808
 phone 617.552.1762 fax 617.552.0191 crr@bc.edu crr.bc.edu