

Impact of Late-Career Health and Employment Shocks on Social Security and Pension Wealth

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Health and Employment Shocks May Derail Retirement Savings Plans

- Onset of health-related work limitations and job layoffs are common at ages 51 - 70
- These shocks affect growth in household financial and housing wealth
- Social Security may provide some protection
- Traditional DB pensions may be especially vulnerable to shocks immediately prior to retirement

We Examine the Impact of Health and Employment Shocks on Social Security, Pension, and Other Household Wealth

- Compute incidence of work disability and job layoffs up to age 62 for workers ages 51 to 55 at baseline
- Compare wealth at baseline and at last interview for those who do and do not experience shocks
- Estimate multivariate models to assess the impacts of shocks holding other factors constant

Health and Retirement Study (HRS)

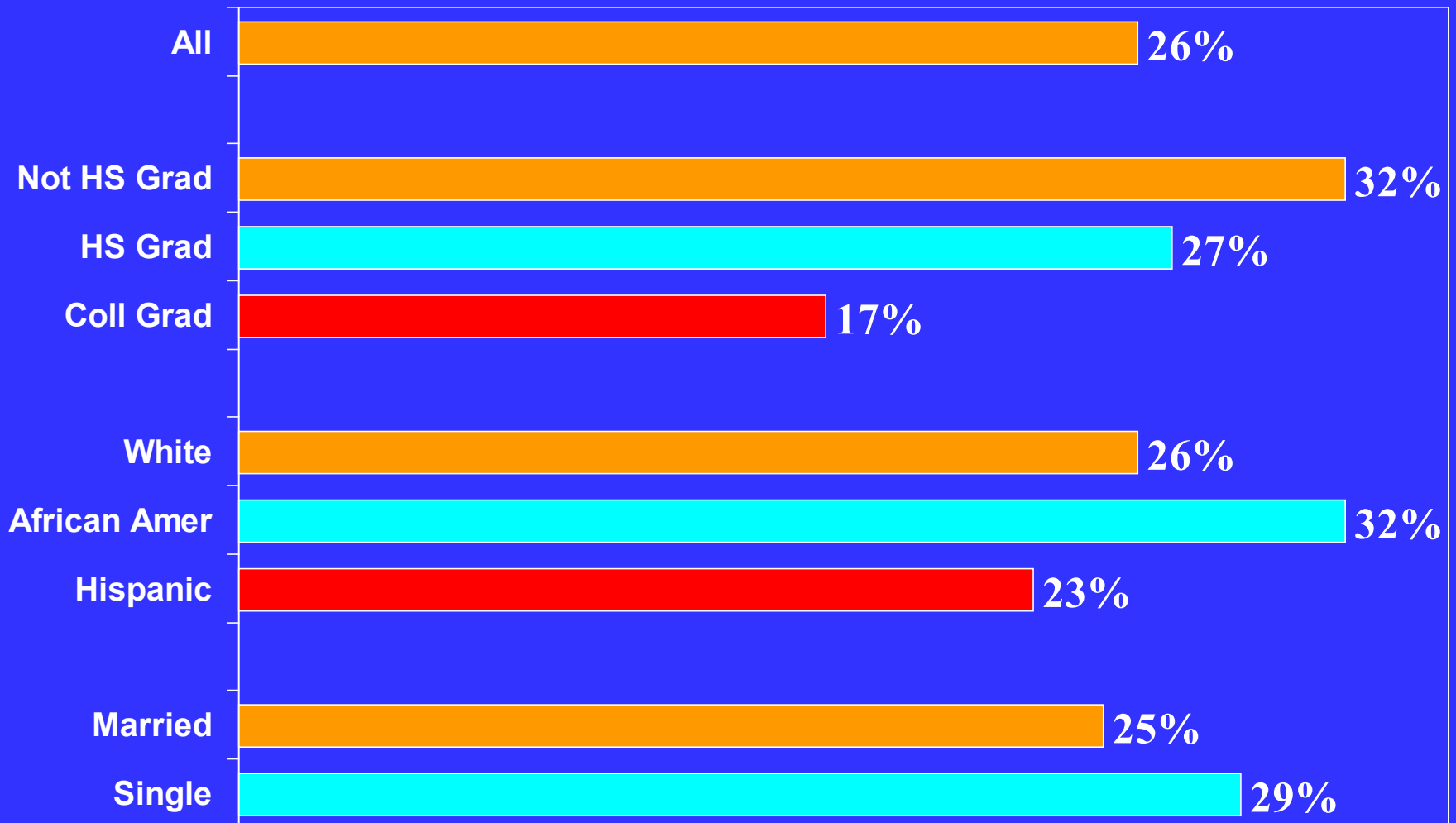
- Longitudinal study of Americans over age 50
- Collects detailed information on employment, health status, and assets
- Social Security administrative records and detailed pension plan characteristics are available for many respondents
- Full Sample: 3,004 workers ages 51-55 in 1992
 - re-interviewed every other year until 2004
- Social Security Sample: 2,384 workers
- Pension Sample: 847 workers

Measuring Health and Employment Shocks

- Onset of health problems that limit the amount or type of work people can do
- Laid off from job since previous interview
- Incidence up to age 62
 - Later shocks are likely to have smaller effects on Social Security and pensions

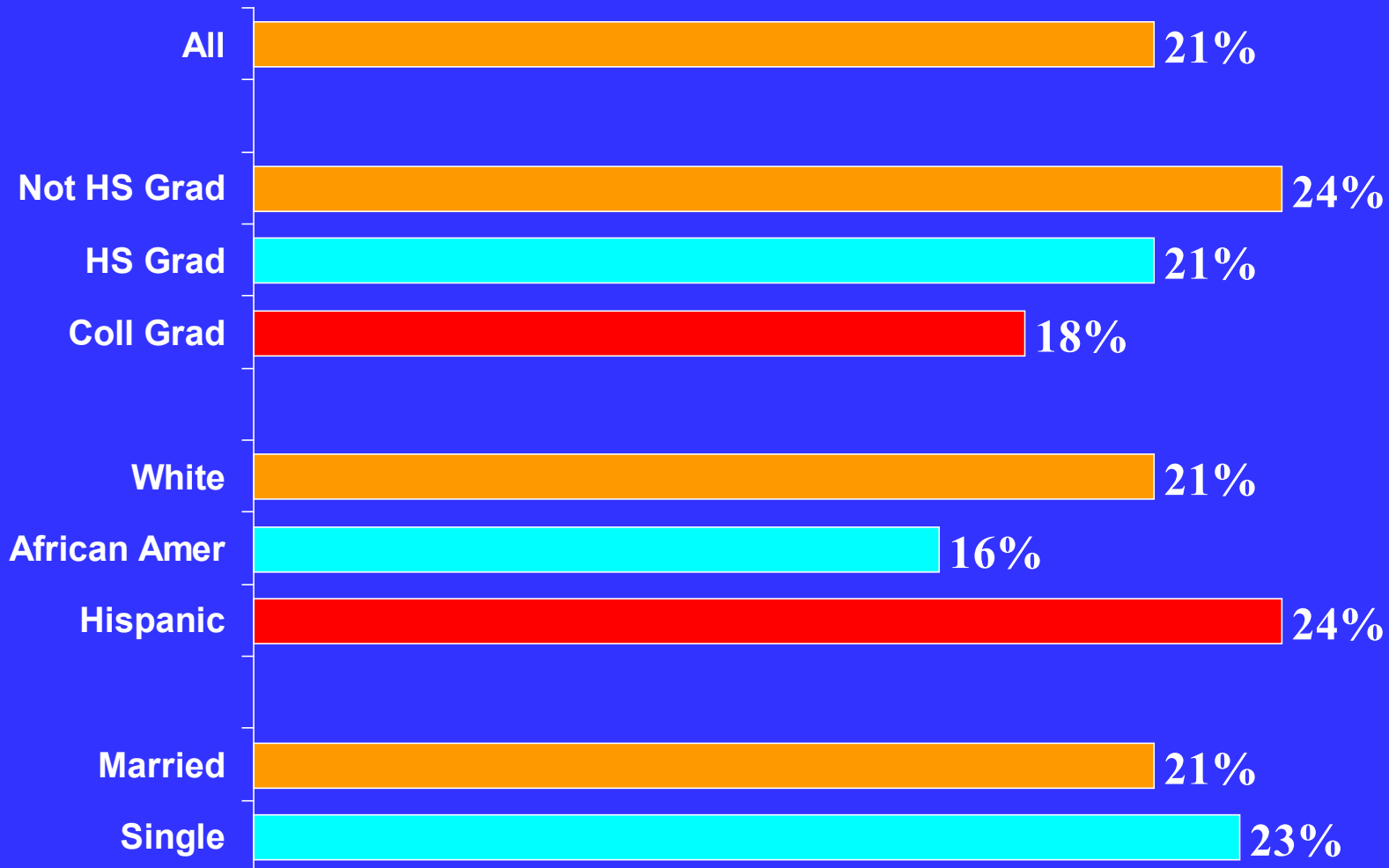
About One-Quarter of Workers Ages 51-55 Develop Work Disabilities Before Age 62

Incidence of Health-Related Work Limitations



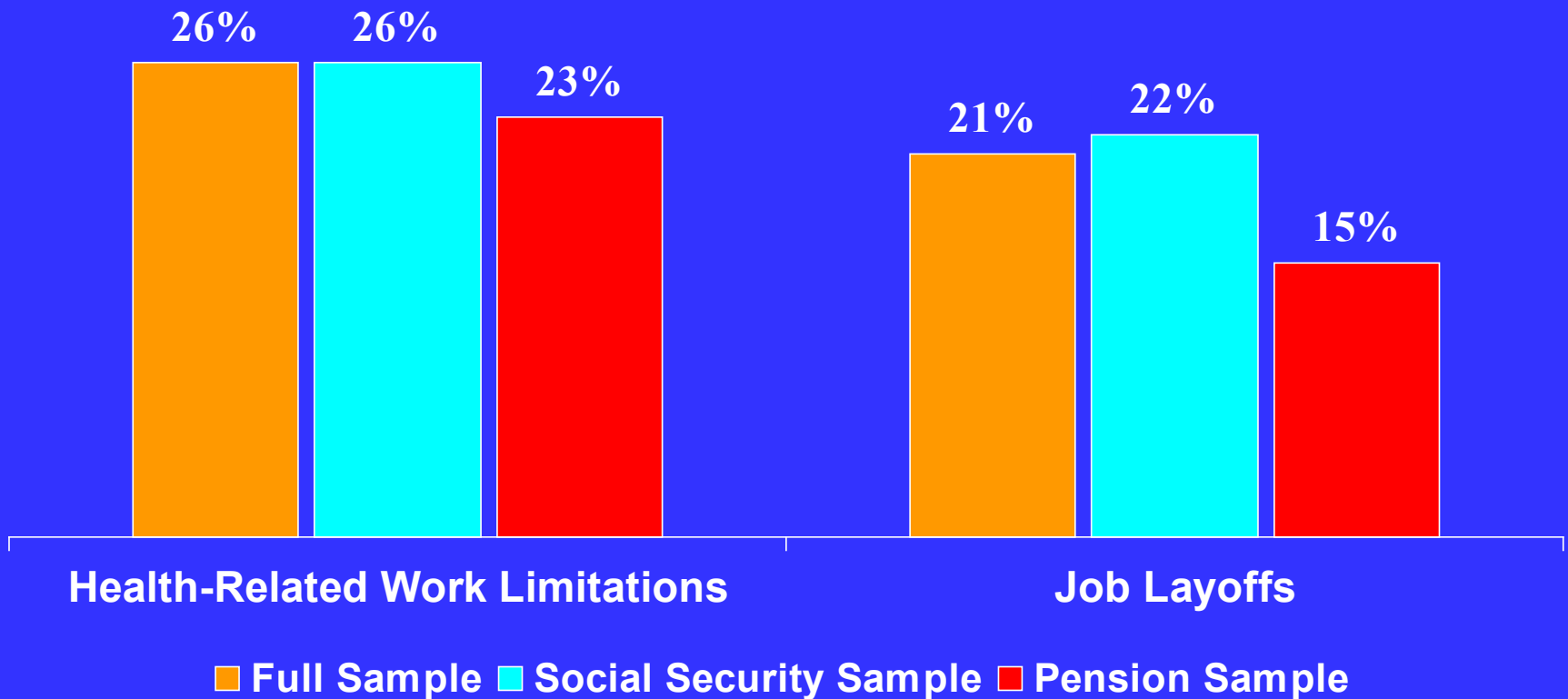
About One-Fifth of Workers Ages 51-55 Are Laid Off From Their Jobs By Age 62

Incidence of Job Layoffs



Shocks Are Less Common in Pension Sample

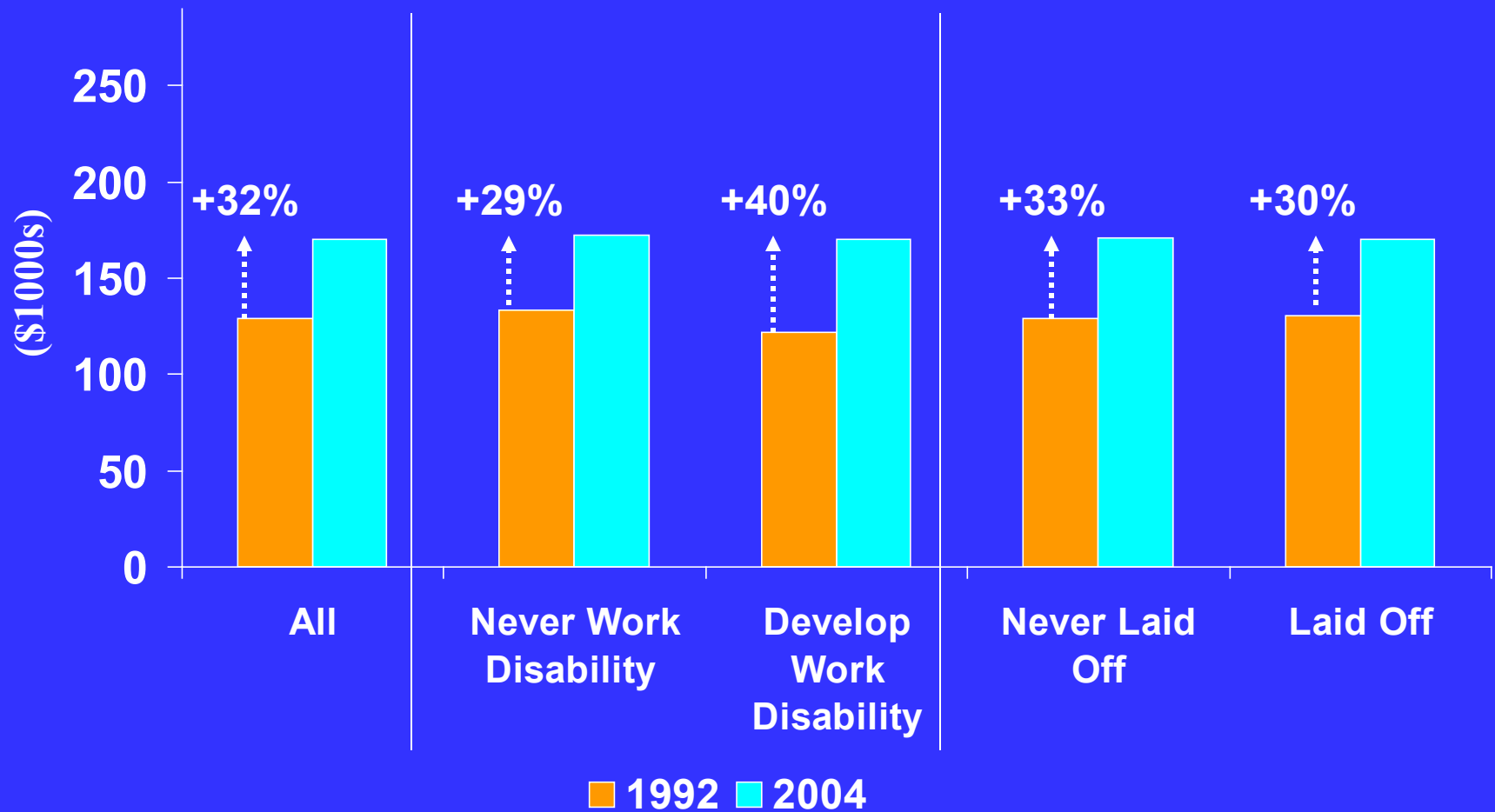
Incidence of Health and Employment Shocks, by Analytic Sample



How Do Shocks Affect Accumulation of Social Security Wealth (SSW)?

- Based on administrative earnings records and include retired worker, disability, spouse, and survivors benefits
- SSW in 1992 = the expected present value at age 62 of future benefits based on earnings through 1992
- SSW in 2004 = present value at age 62 of benefits received through 2004 + expected present value of future benefits

Mean Social Security Wealth in 1992 and 2004 by Onset of Health and Employment Shocks

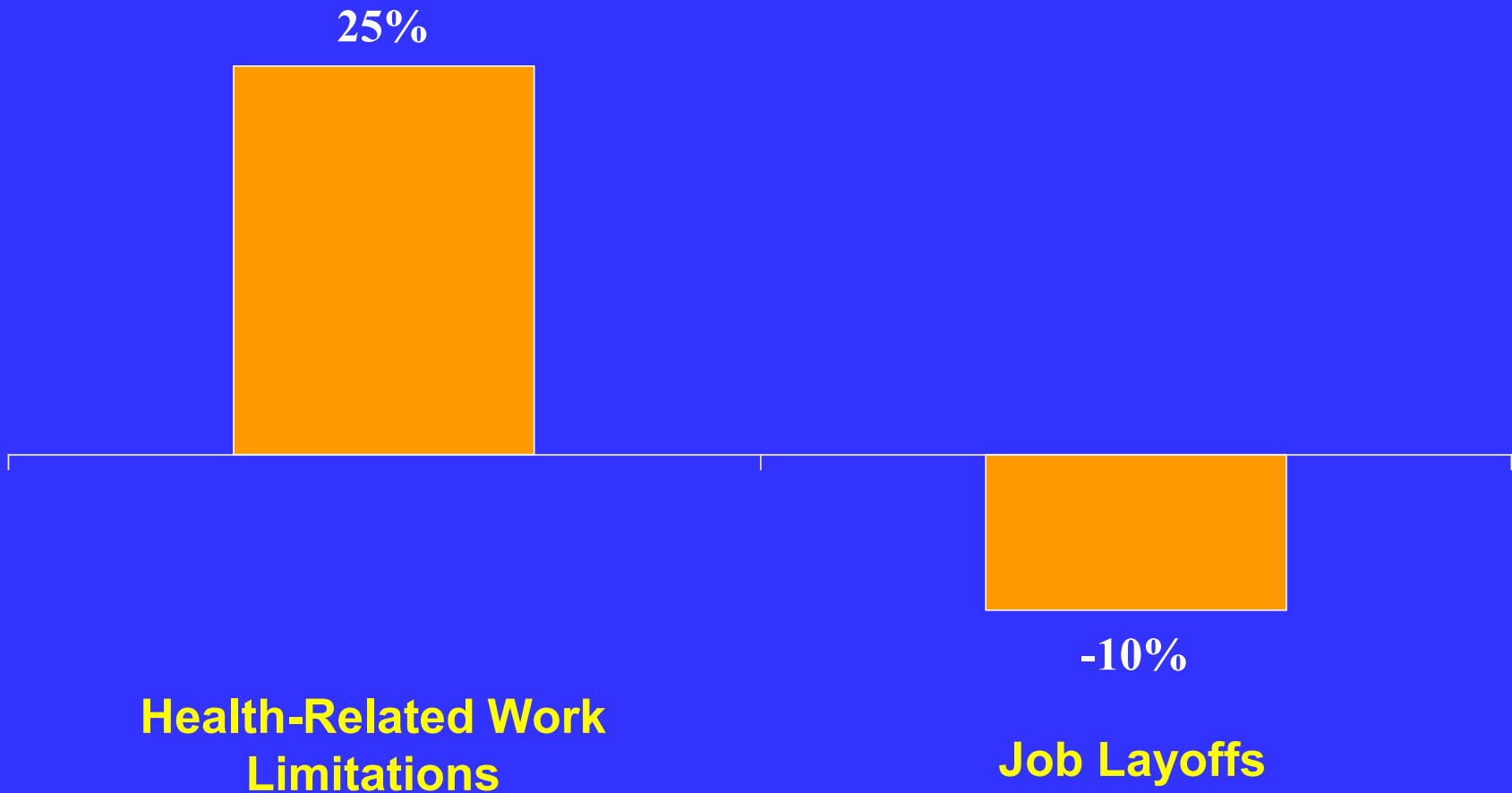


Multivariate Analysis of Change in Social Security Wealth

- OLS regression of change in SSW between 1992 and 2004
- Factors included:
 - Onset of health-related work limitation
 - Job layoff
 - Controls
 - Demographics (marital status, education, race, age)
 - Earnings
 - Health status at baseline
 - Widowed after 1992
 - Divorced after 1992

Controlling for Other Factors, Layoffs Modestly Reduce Growth of Social Security Wealth, Whereas Health Shocks Increase Growth

Relative Impact of Shocks on Change in Social Security Wealth



How Does Social Security Protect Workers from Health Shocks?

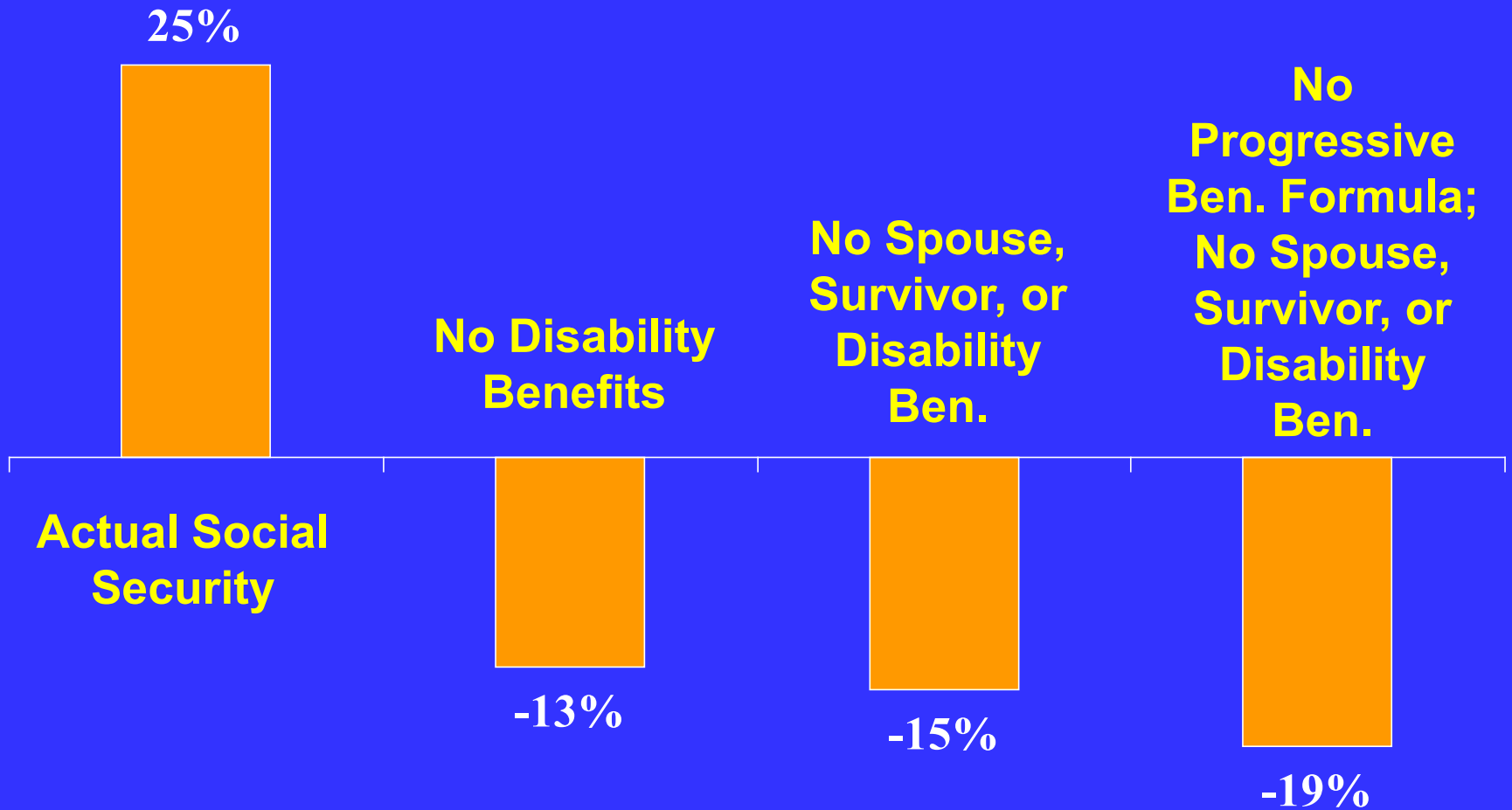
- Disability insurance provides benefits earlier and at higher levels in retirement for those who qualify
- Workers can receive benefits from current, divorced, or deceased spouse's work history
- Basing benefits on highest 35 years of earnings and progressive benefit formula favor those with limited employment histories and lifetime earnings

Simulating Social Security Wealth As If Progressive and Non-Earnings Related Features Did Not Exist

- No disability benefits
 - Use retired worker formula for everyone and do not allow take-up until age 62
- No spouse or survivors benefits
 - Base all benefits on own earnings records
- Eliminate progressive benefit formula
 - 40 computation years (not 35)
 - Flat formula that replaces 45% of average earnings for all workers

Disability Benefits Prevent Health Shocks From Reducing Growth of Social Security Wealth

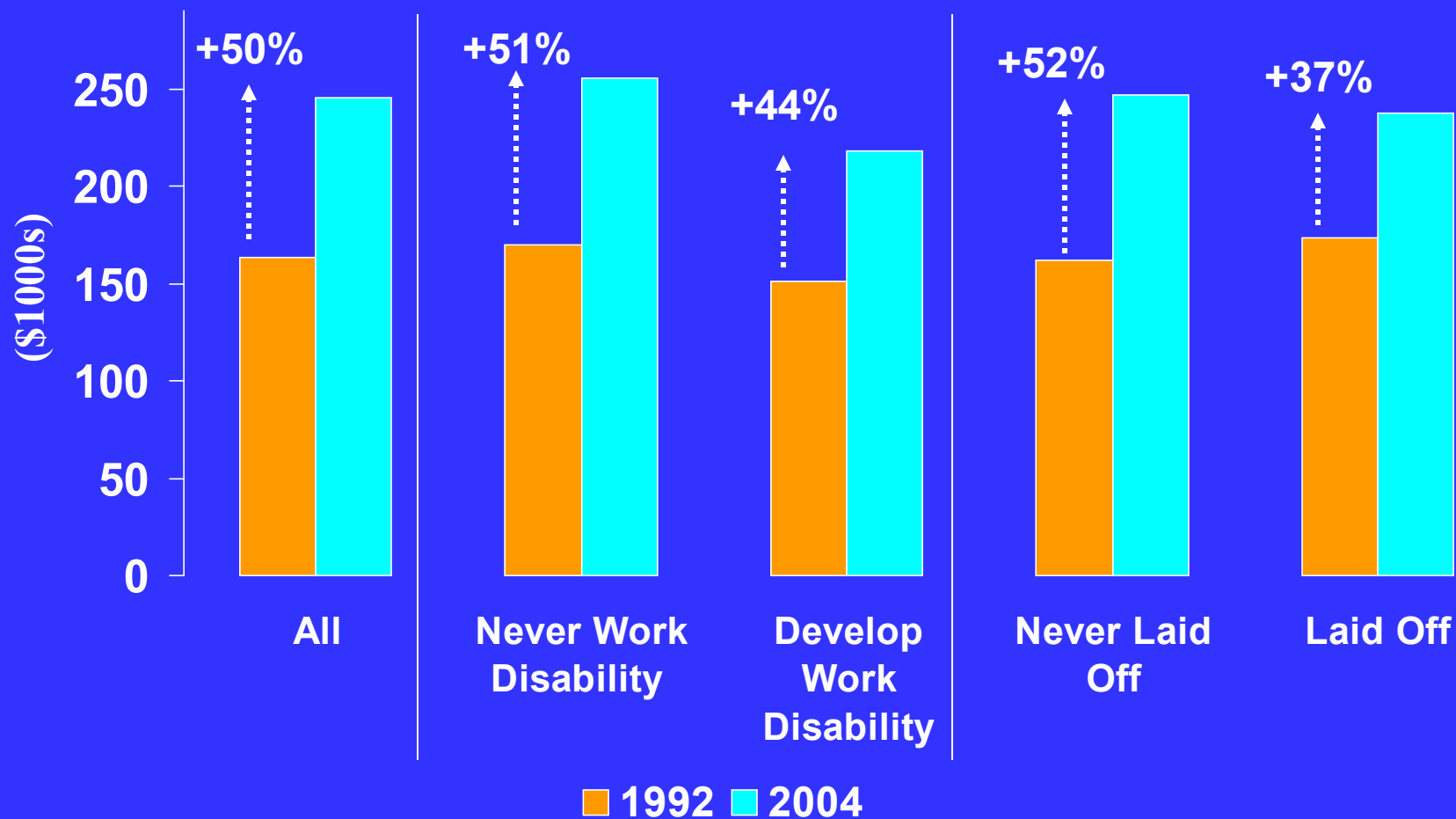
Impact of Health Shocks on Change in Social Security Wealth Under Alternative Benefit Scenarios



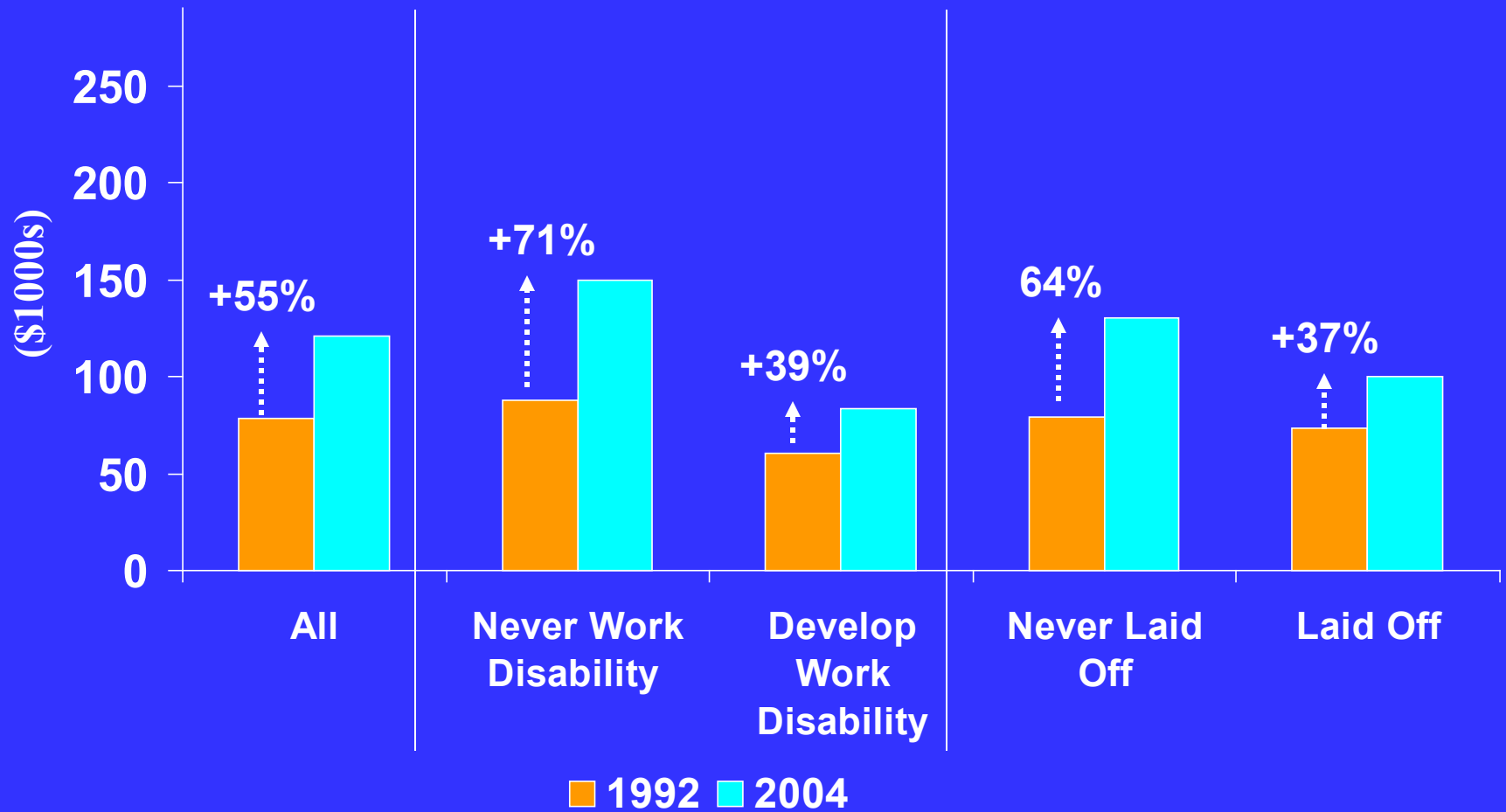
How Do Shocks Affect Accumulation of Pension and Other Household Wealth?

- PW based on pension plan characteristics, Social Security administrative records, and self-reported hire and quit dates
- PW in 1992 = the expected PV at age 62 of future benefits based on earnings through 1992
- PW in 2004 = PV at age 62 of benefits received through 2004 + expected PV of future benefits
- Other household wealth includes housing, financial assets, other real estate, vehicles, and businesses, net of debt
 - Examine medians

Mean Pension Wealth in 1992 and 2004 by Onset of Health and Employment Shocks

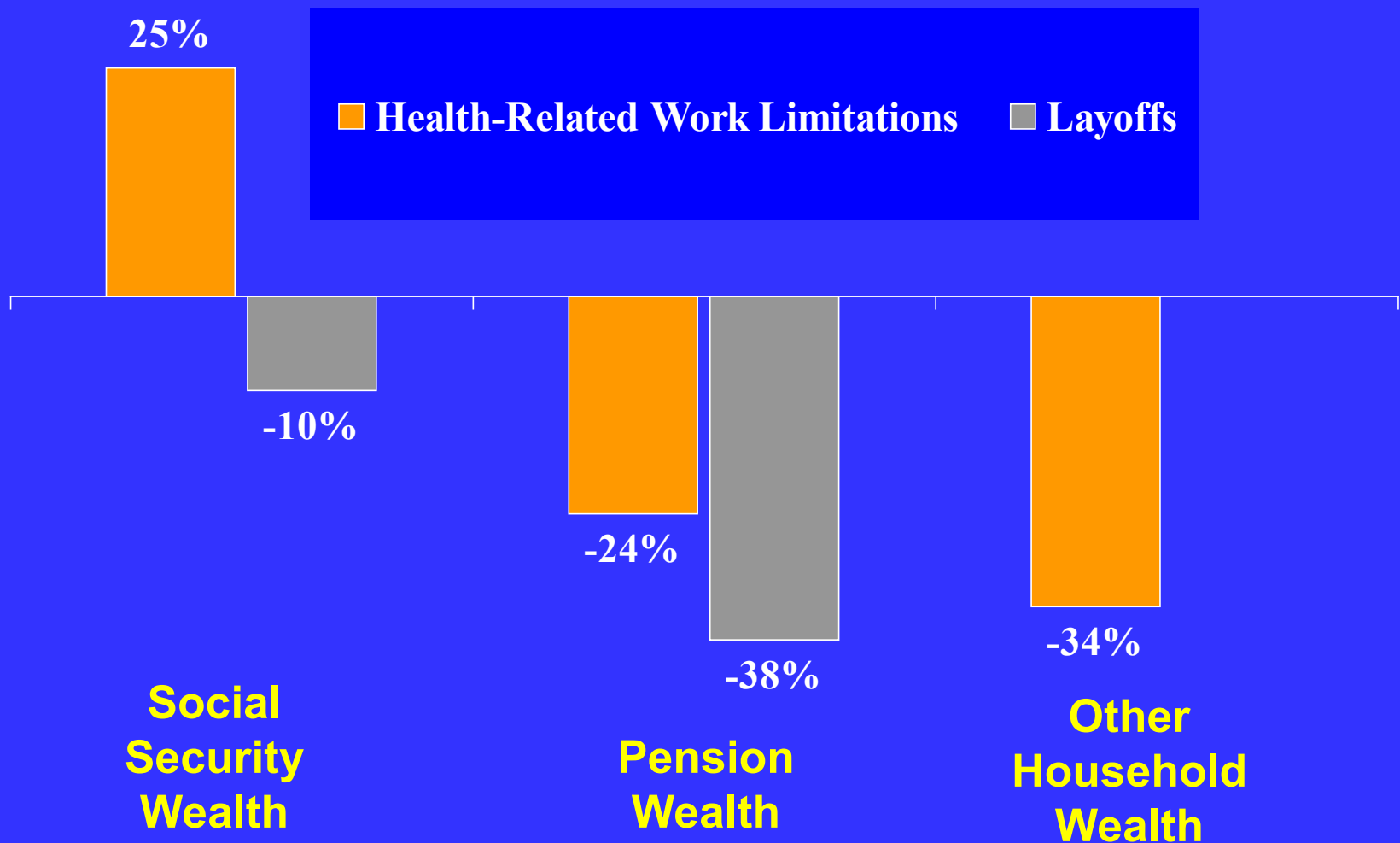


Median Other Household Wealth in 1992 and 2004 by Onset of Health and Employment Shocks



After We Control for Other Factors, Health Shocks Have Negative Impact on Pension and Other Household Wealth

Relative Impact of Health and Employment Shocks on Change in Social Security, Pension, and Other Household Wealth



Discussion

- Social Security provides some protection, but those who develop work disabilities may experience hardship in subsequent years
 - We haven't yet examined impact of health shocks on SSW based just on benefits received after age 62
 - Worker who become disabled experience sharp income declines before age 62
 - Only 25 percent of those experiencing health shocks qualified for disability benefits

Discussion Cont'd

- Layoffs substantially reduce the accumulation of traditional pension wealth because workers miss out on the wealth run-up that occurs shortly before retirement
 - But traditional pensions are becoming less common
- Layoffs have smaller impact than health shocks on earnings-related SSW and other household wealth
 - Despite well-known employment challenges faced by displaced older workers, results suggest long-term impact may be less severe
- Effect of late-career shocks is modest when compared to total retirement wealth