I. Introduction

Today's older workers will live longer and spend more time in retirement than workers in any previous generation. This trend presents a challenge to workers and to public policy that has to date been met with analyses that, by looking primarily at household wealth and savings, address the issue only around the edges. The key question, however, tends to be ignored: will households have enough *income* to afford a decent standard of living in retirement?

Between 1989 and 1998, a period of strong economic growth and a 248% rise in stock prices, the annual income that a household headed by a person approaching retirement (i.e., age 47-64) could expect in retirement rose at the average by 7%, to $50,000 a year. But gains for the average have not meant gains for all households. Over this same period, the share of these near-retirement households unable to expect adequate income in retirement increased:

- By 1998 (the latest year of available data), 18.5% of households headed by a person approaching retirement could expect incomes below the poverty line. This share actually increased during the 1990s, up from 17.2% in 1989.

- The share of these households unable to replace half of their pre-retirement income rose sharply, from 29.9% in 1989 to 42.5% in 1998. The share was even higher in 1998 among African American and Hispanic households, at 52.7%.

The increasing reliance on individual investment of retirement funds – exemplified most clearly by the growth in 401(k)s, individual retirement accounts, and other defined contribution pension plans – and the decline in traditional pensions, might lead one to expect that the period of fast stock market growth that began in 1983 would have produced more retirement wealth and improved retirement income adequacy. After all, by 1998 59.7% of households approaching retirement had investments in defined contribution accounts, up from 11.9% in 1983.

Yet for the typical (median) household headed by a person age 47-64, retirement wealth actually declined from 1983 to 1998, by 11%, while rising 4% on average. Retirement wealth declined for the household at the middle of the wealth distribution while it rose overall because the pattern of retirement wealth growth was very unequal:

- Among households headed by a person approaching retirement, only households with wealth holdings above $1 million saw consistent increases in their wealth, after inflation. All other wealth classes, even those with between $500,000 and $1 million in net worth, saw their retirement wealth fall from 1983 to 1998.

- Growth in retirement wealth tended to be the province of white households, who saw a 6.1% increase in average retirement wealth. Black and Hispanic households experienced a 19.9% drop.

- Growth in retirement wealth also tended to be the province of college-educated households, who experienced a 6.4% increase in their average wealth. Among the 72% of the workforce without a college degree, mean retirement wealth dropped by 39.1% where the household head had less than 12 years of schooling, 9.9% for high school graduates, and 10.5% for workers with some college.

One reason for the deterioration of retirement wealth for the typical household is that pension coverage for households (either traditional pension or defined contribution plan) barely changed from 1983 to 1998. Among households headed by a person age 47-64, 73.7% were covered by a pension plan in 1998, an improvement of only 3.5 percentage points in pension coverage compared to 1983. At this rate it will take 113 years to achieve pension coverage for all households.

Thus, an extraordinary 15-year run-up in stock prices at a time when public policy was encouraging expanded individual investment for retirement did not enhance retirement income adequacy for the typical household, even as the market was near its height. Moreover, it is important to remember that all gains made after 1998 in terms of household wealth had disappeared by the third quarter of 2001, when household financial net worth fell back to its third-quarter 1998 level. New policies are needed to ensure that the broad majority of households have access to pensions and adequate incomes in retirement.

As a first step for public policy, pension coverage needs to be improved. Until then, as long as a substantial share of future retirees lack adequate resources, it seems prudent for policy makers to keep Social Security intact, rather than subject it to the risks of privatization. This is particularly true now that Social Security offers almost universal coverage: thanks to mandatory coverage for most workers, Social Security's reach rose from 82.4% in 1983 to 98.4% in 1998.

Next, retirement wealth accumulation needs to be improved for the vast majority of households. The growing system of voluntary accounts in the United States has produced greater inequality between rich and median households and declining retirement wealth for the typical household. In contrast, Social Security, which pools contributions in order to ensure a retirement income floor for all participants, is the one segment of the retirement system that distributes its wealth universally. Thus, one possibility for improving the adequacy of retirement income for the typical household would be to improve Social Security benefits.