

Retirement crisis: From bad to worse

You've been hearing about a looming Social Security problem for years, but it's not the only big trouble facing boomers and the generations behind them.

By Jim Jubak (MSN/Money)

Baby boomers and the post-boomer generations are facing a retirement crisis. And it now goes way beyond the worries about a collapse of Social Security that so preoccupied us before housing prices headed south.

The crisis I'm talking about is a result of economic and monetary policies that have turned a pattern of boom-bust-boom-bust into business as usual in the U.S. economy. The 2007-and-counting collapse of the housing, mortgage and debt markets isn't an isolated disaster but part of a decade-long shift away from saving and investing toward speculation and gambling with our future.

We don't have a whole lot of time to fix this crisis. The boomers born in 1946 will turn 65 in 2011. For many of us in the baby-boom generation, financing a relatively comfortable retirement, which never looked easy, looks increasingly impossible.

For those of you in the post-boomer generations, I'm sure it seems even more likely that we boomers will try to pick your pockets to finance our retirements. And I'm not sure that you're wrong to believe that. This crisis wouldn't be so bad -- and might not even exist -- if we hadn't dug ourselves such a deep hole to begin with and then kept on shoveling.

Pig in a python

That initial hole was largely demographic. The number of Americans 65 and older is projected to increase to 69.4 million in 2030 from 35.5 million in 2000, the Census Bureau says. That's not entirely bad news -- much of the increase comes from Americans living longer -- but it is a problem if you're trying to figure out how to pay for all those people to retire.

Because the baby-boom generation is so much bigger than succeeding generations, the ratio of people in the retirement years, 65 and older, to those in the working years, 20 to 64, will rise from 20.6% in 2005 to 35.5% in 2030, according to the Census Bureau. That will put a strain on any retirement system that depends on contributions from current workers, as Social Security does, to pay the benefits of current retirees.

Fortunately, Social Security is only one part of the stream of cash that we use to pay for retirement in the United States. Most of the other sources aren't based on funding current benefits from current contributions. They rely on current savings, invested over time, to produce a future sum sufficient to pay for retirement or part of it.

There are three big pieces to this saving and investing part of the retirement cash flow:

- **Traditional pensions.** With these, most of the saving and investing is done by employers, which also bear the risk that retirement assets will fall short of promised benefits. As of 2005, only 37% of workers were covered by a traditional pension, according to the [Employee Benefit Research Institute](#). And a growing number of company pensions are winding up in the hands of the Pension Benefit Guaranty Corp., a government agency and payer of last resort that is underfunded to the tune of \$14 billion, as I described in "[The year's scariest investing news](#)" on Feb. 26.
- **Accounts funded by contributions from workers.** These include 401(k)s and individual retirement accounts. The Employee Benefit Research Institute estimated workers had about \$7.5 trillion in these retirement accounts as of October 2007.
- **Home equity.** For most people, the house they live in is their biggest retirement asset. In retirement, people cash in on the value of their homes by selling and then buying less expensive houses, renting or moving in with the kids. More people are also using [reverse mortgages](#) to extract equity from their homes in retirement. As of October, working from numbers published by the Federal Reserve and changes in home prices measured by the S&P/Case-Shiller index, I calculated a total value of about \$20.7 trillion for the value of all U.S. residential real estate.

As anyone planning to retire in 10 years or so knows, your biggest nightmare -- the one where you wake up screaming -- is a collapse in the financial markets and the economy in the years just before you retire.

If you've had such a nightmare, take a shower and then buckle down to some serious financial discipline. Bring lunches from home and brew your own coffee instead of rushing out to Starbucks. You know the drill. And invest the extra you save to make up for lost dollars and time.

Or you can decide to make up the difference by making riskier bets in the hope that the gamble will enable you to catch up.

Looking for a shortcut

There's no evidence that we're cranking up the financial discipline, however, and plenty of evidence that we're rolling the dice.

How we'll react to the housing bust of 2007 isn't yet known. But the evidence from how we reacted to the 2000-02 bear market doesn't fill me with confidence. According to the Federal Reserve's 2004 survey of consumer finances, the percentage of families that save anything at all went down to 56.1% in 2004 from 59.2% in 2001. (The Fed does these every three years, and the 2007 survey isn't out yet.)

The Employee Benefit Research Institute reports that the number of people participating in defined-contribution plans, including IRAs and 401(k)s, declined to 52.2 million in 2004 from 52.9 million in 2002.

The housing boom certainly didn't have any of the trappings of a disciplined attempt to reach retirement goals. As home values rose, homeowners withdrew money from these vital retirement assets to use on current consumption. In the early stages of the boom, 2001 through 2004, the average homeowner's equity fell from 58% of home value to 55%. That's during a period when home values climbed 67%, according to the S&P/Case-Shiller index, when equity would have been rising if consumers hadn't been so busy cashing out. According to the Web site [RGE Monitor](#), homeowners pulled \$800 billion out of their homes in 2005 alone.

Grim news on several fronts

Sure, that was great for the U.S. and global economies. All that extra consumer spending kept the economies ticking along when Europe and Japan were barely growing. But don't expect the global economy to return the favor now by buying enough from the U.S. to push economic growth back over 3%.

U.S. exports might climb enough to help us avoid a recession, but will they get economic growth back over 3%? Forget it, at least anytime soon. In February, the Federal Reserve cut its forecast for 2008's economic growth to 1.3% and for 2009's to 2.1% to 2.7%. The central bank also noted that growth could remain below "normal" as far out as 2012.