

Book reviews

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Working Longer: The Solution to the Retirement Income Challenge. Alicia Munnell and Steven Sass. Brookings Institution Press, 2008, ISBN 978-0-8157-5898-3, 224 pages. doi:10.1017/S1474747210000302

This is a concise and very readable book that argues persuasively that while American life expectancies are increasing, the various components of our public and private retirement system are contracting, and that replacement rates (the ratio of post- to pre-retirement income) of retirees will decline significantly in the future unless major changes in behavior occur. Munnell and Sass believe that the easiest way for most to offset these impending declines is delayed retirement, and they estimate that 2 to 4 years of additional full-time work (an average retirement age of about 66 rather than the current 63) will suffice for most workers.

Analysts have long referred to the three-legged stool of retirement income – Social Security benefits, employer pension benefits, and income from savings. In 2007 these provided, respectively, 36 %, 17 % and 16 % of the aggregate income of American households aged 65 and older. Where is the other 31 %? It nearly all comes from earnings. The percentage of income from earnings is even higher for those aged 62 to 64 (65 %) and then declines with age, from nearly half (45 %) of the income of aged units aged 65 to 69 to 9 % for those aged 80 and above. So the stool is really four-legged (and has been: earnings provided 28 % of the income of Americans 65 and older in 1962), or five-legged, if one considers post-retirement health insurance sponsored by some employers.

Munnell and Sass argue in Chapter 1 that four of these five legs are wobbly. Net Social Security replacement rates will decline, because of the increase in the normal retirement age from 65 to 67 (already underway, and equivalent to an across-the-board benefit cut), increased Medicare B premium deductions, and increased federal income taxation of Social Security benefits, since exemption thresholds are not indexed for inflation. Only about half of American workers are covered by employer pensions (mostly middle- to upper-income employees), and nearly two-thirds of those are now covered by defined contribution plans (basically, saving accounts), whose eventual payout depends on financial market returns. Personal savings (beyond institutionalized pension savings) has always been modest and sometimes negative. The percentage of firms offering retiree health insurance has dropped precipitously (e.g., from 66 % in 1989 to 35 % in 2006 for large firms), and plans still existing have become less generous. What is the remedy for this dire financial forecast? Additional earnings!

In the next 4 chapters, the authors ask: Will older men want to work longer? Will older women? Will employers hire them? And what can be done – by employees, employers and the government? The authors are cautiously optimistic about labor supply, but worried about the demand for older workers, since productivity eventually declines with age, while compensation (especially for health care costs) tends to rise with age. To make this remedy work, employees must pay more attention to their future finances (e.g., read this book!), keep skills up to date, and stay healthy. Employers must address the challenges and opportunities of an aging workforce, and make workplace accommodations where necessary; for example, some older workers prefer hours flexibility or less strenuous jobs as they age. A key player must be the government, which has already encouraged additional work late in life by lowering Social Security benefits and by eliminating what were once significant financial work disincentives at age 65. But what is really needed, according to Munnell and Sass, is an increase in the earliest age of benefit eligibility, from 62 to 64. This, they acknowledge, is a controversial recommendation, and one that would harm those who cannot work additional years (which they estimate to be 15 to 20% of the workforce), and who tend to be vulnerable on a number of counts (health, education, wage rates and retirement benefits).

There are many strengths of this slim volume. It is very well written and designed for the citizen, not for professionals in the field. It makes excellent use of graphs, charts and footnotes, where considerable technical detail and bibliographic information reside. The simple math behind the authors' major point (please consider working several more years!) is straightforward and compelling. When estimating available assets per year of retirement, additional years of work both increase the numerator (additional earnings and employer pension contributions, additional savings, and higher Social Security benefits) *and* decrease the denominator (years of retirement). They point out in a short summary Chapter 7 that four additional years of work can change the ratio of working years to retirement years from about 2:1 (40:20) to almost 3:1 (44:16).

I am more optimistic than the authors that American men and women will want to and be able to work longer than they used to. In fact, they already are. Between 1950 and 1985, the labor force participation rates of men aged 62, 65, 68 and 70 *declined* by 37% (81.2 to 50.9), 57% (71.7 to 30.5), 64% (57.7 to 20.5) and 68% (49.8 to 15.9), one of the most dramatic demographic changes in recent history. But since then, the retirement environment has changed equally dramatically; it's a whole new world. Social Security has eliminated strong retirement incentives, as have employers, to an extent, by largely moving from defined-benefit to defined-contribution plans, which have no age-specific retirement incentives. Mandatory retirement is gone and not coming back. People are living longer and healthier lives, jobs are less strenuous, and workplace technology has improved. How have workers responded? Between 1985 and 2008, participation rates of men 62, 65, 68 and 70 have *increased* by 11% (to 56.6), 43% (to 43.7), 45% (to 29.8) and 52% (to 24.1)! And female rates have increased even more for these same ages (since 1985, by 52%, 101%, 84% and 90%). In addition, the majority (over 60%) of older Americans now retire gradually, in stages, utilizing bridge jobs on the way out, between full-time career employment and complete labor force withdrawal. The era of earlier and earlier retirement is over, and has been for 25 years. A new era has begun.

I hope that this book has two impacts: encouraging middle-aged workers to think about working a few years longer and encouraging Congress to discuss an increase in Social Security's early retirement age, along with the attendant changes (perhaps to disability policy) required to protect those unable to work longer. If it does, this book, in addition to being a pleasure to read, will make a very valuable contribution to the national retirement policy debate.

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Pension Strategies in Europe and the United States. Robert Fenge, Georges de Ménil, and Pierre Pestieau, eds. MIT Press, 2008, ISBN 978-0-262-06272-5, 304 pages. doi:10.1017/S1474747210000314

This book is part of the CESifo Seminar Series and presents a collection of theoretical and empirical research papers shedding light on implications of pension system reforms