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**What Individuals Should Plan For Retirement Risk Management**

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Marsh & McLennan Companies
Many people choose to retire and are happy in retirement

Decline in employer sponsored DB plans and retiree health
  - More individual responsibility, DC plans, lump sums
  - Long service employees often have good benefits: DB, DC and retiree health

Low savings rates

People want and need to work longer, return to work

Misunderstandings about retirement risk

Couples much better off than women alone

Little use of annuitization, but stated preference for regular income in studies

Big questions about future of retirement security
### Pre-retirees, Not Retirees, Are More Concerned About Risks Than in 2001

How concerned are you that...? (% very or somewhat concerned)

<table>
<thead>
<tr>
<th></th>
<th>Retirees (2003 n=273)</th>
<th>Pre-retirees (2003 n=331)</th>
</tr>
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<tbody>
<tr>
<td>You might not have enough money to pay for good health care</td>
<td>46% 2003, 43% 2001</td>
<td>79% 2003, 58% 2001</td>
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<tr>
<td>You might not be able to keep the value of your savings and investments up with inflation</td>
<td>57% 2003, 55% 2001</td>
<td>78% 2003, 63% 2001</td>
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<td>You might not be able to maintain a reasonable standard of living for the rest of your (and your spouse’s) life</td>
<td>46% 2003, 47% 2001</td>
<td>71% 2003, 54% 2001</td>
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<td>Your spouse may not be able to maintain the same standard of living after your death, if you should die first (Retirees, n=172; Pre-retirees, n=207)</td>
<td>34% 2003, 43% 2001</td>
<td>47% 2003, 40% 2001</td>
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SOA, 2003 Risks and Process of Retirement Survey

Mercer Human Resource Consulting
Knowledge and Understanding of Longevity Risk

- SOA/AAA Retirement Plan Preferences survey shows people prefer regular monthly income, but this is not supported by choices often made.
- Seems to be little focus on variability of life span.
- Retirement planning software generally asks for expected date at death.
- Outliving assets not a major concern and very incomplete understanding of longevity risk protection.
- We believe the public overvalues lump sums compared to regular lifetime income.
Retirees’ Top Concern is Inflation Risk

How concerned are you that…?
(Retirees, n=273; Pre-retirees, n=331)

- You might not be able to keep the value of your savings and investments growing faster than inflation
  - Retirees: Very concerned 25%, Somewhat concerned 32% (57%)
  - Pre-retirees: Very concerned 42%, Somewhat concerned 36% (78%)

- You might not be able to maintain a reasonable standard of living for the rest of your (and your spouse’s) life
  - Retirees: Very concerned 17%, Somewhat concerned 29% (46%)
  - Pre-retirees: Very concerned 34%, Somewhat concerned 37% (71%)

- You might deplete all of your savings and be left only with Social Security
  - Retirees: Very concerned 25%, Somewhat concerned 15% (40%)
  - Pre-retirees: Very concerned 36%, Somewhat concerned 29% (65%)

- Your spouse may not be able to maintain the same standard of living after your death (Retirees, n=172; Pre-retirees, n=207)
  - Retirees: Very concerned 15%, Somewhat concerned 19% (34%)
  - Pre-retirees: Very concerned 25%, Somewhat concerned 22% (47%)

SOA, 2003 Risks and Process of Retirement Survey
Pre-retirees are More Concerned About Health Care Risks Than Retirees

How concerned are you that you might not…?

(Retirees, n=273; Pre-retirees, n=331)

- Have enough money to pay for long-term care
  - Retirees: 20% (Very concerned) 27% (Somewhat concerned)
  - Pre-retirees: 33% (Very concerned) 32% (Somewhat concerned)

- Have enough money to pay for good health care
  - Retirees: 22% (Very concerned) 24% (Somewhat concerned)
  - Pre-retirees: 49% (Very concerned) 30% (Somewhat concerned)

- Be able to rely on children or other family members to provide assistance
  - Retirees: 15% (Very concerned) 16% (Somewhat concerned)
  - Pre-retirees: 13% (Very concerned) 20% (Somewhat concerned)

SOA, 2003 Risks and Process of Retirement Survey
Few Turn to Risk-reducing Products to Protect Themselves

How well does the statement about managing money in retirement describe you (and your spouse)?

(Retirees, n=273; Pre-retirees, n=331)

- I think it is a good idea to buy insurance to protect financially against things like the possibility of needing extended nursing care.
  - Retirees: 27% (Very well), 24% (Somewhat well), 52%
  - Pre-retirees: 22% (Very well), 36% (Somewhat well), 58%

- I think it is a good idea to buy annuities, because they protect people by paying a guaranteed income for life, no matter how long you live.
  - Retirees: 13% (Very well), 25% (Somewhat well), 38%
  - Pre-retirees: 13% (Very well), 31% (Somewhat well), 43%

SOA, 2003 Risks and Process of Retirement Survey

Mercer Human Resource Consulting
Instead, People Try to Reduce Spending

How well does the statement about managing money in retirement describe you (and your spouse)?

(Retirees, n=273; Pre-retirees, n=331)

I try to reduce unnecessary spending so that I can set aside as much money as possible to keep the value of my savings growing.

Retirees
- Very well: 35%
- Somewhat well: 41%

Pre-retirees
- Very well: 24%
- Somewhat well: 49%

I try to invest a considerable portion of money in stocks and stock mutual funds, hoping that in the long run their value will rise.

Retirees
- Very well: 22%
- Somewhat well: 24%

Pre-retirees
- Very well: 25%
- Somewhat well: 30%

SOA, 2003 Risks and Process of Retirement Survey
Key Messages and Conclusions

- Retirement plan participants are very concerned about regular income security
- Pre-retirees are much more concerned about retirement security than in 2001
- People do not assess and manage risk well
- The emerging pattern of phasing into retirement is likely to increase
- People tend to express a preference for the type of employer-provided retirement plan they already have
Conclusions from Research

- Individual responsibility is growing in importance
  - In preferences study: 88% of retirees had DB vs. 49% of workers
  - About half of workers currently not in employer plans
  - Less retiree health
- From 2001 to 2003
  - Pre-retirees increased risk focus
- Significant gaps in knowledge
- Major risk management strategy is “reduce spending”
- Very limited use of financial products for risk management
- Work growing in importance as part of retirement
Implications: Very Important Directions for Retirement System

- Policy action needed
  - Strengthen and revitalize DB system
  - Level the playing field
  - Support employer plans

- Without such action, many more people will be in trouble
Implications
Educational priorities

- Education will not do whole job, but can help
- Education on post-retirement risks should be high priority
  - Understanding of risks/danger of focusing on the mean
  - Strategies for coping
- Tailor to individual circumstances
- Content
  - Savings
  - Investment strategies
  - Risk reducing vehicles
  - Public programs of last resort
  - Appropriate spending levels during retirement
Summary
Where we are today

- Large improvement in economic status of elderly
- Critical need for policy action if gains are not to be lost
- Disconnects are common
- Inadequate risk protection and savings
- Population will age dramatically as baby boomers age
- Still too much poverty, particularly among women alone
- More people working after retirement
“The corporate DB system can be healthy and efficient if plans make affordable choices and if both sponsors and regulators manage them appropriately. Neither group should overreact to the recent past; greater transparency and a balanced approach to reform are critical to both.”

Morgan Stanley report for CIEBA
Appendix
## Overview of Post-Retirement Risks

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<th>Risk</th>
<th>Potential Range for Risk</th>
<th>Risk Transfer Options</th>
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<td>Outliving assets</td>
<td>Life spans at age 65 range from 0 years to over 40 years.</td>
<td>Annuities, including joint and survivor annuities</td>
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<td>Loss of a spouse</td>
<td>Periods of widowhood of 15 years or more are not uncommon.</td>
<td>Joint and survivor annuities; life insurance; pension benefits with payment to survivor</td>
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<td>Decline in functional status</td>
<td>Cost of care on account of frailty can range from $0 to over $2,000,000 for a couple over their lifetimes. Nursing home care costs may run $70,000 or more per person per year today.</td>
<td>Long-term care insurance and continuing care retirement communities.</td>
</tr>
<tr>
<td>Out-of-pocket medical expenses</td>
<td>Medical costs not covered by Medicare for retirees over age 65 can range from $0 to over $1,000,000 for a couple over their lives.</td>
<td>Medical insurance</td>
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<td>Inflation</td>
<td>Inflation can range from 0% in any year to 10% or more; inflation has been much higher in other countries.</td>
<td>Products with cost-of-living adjustments; Better education on investing lump sums</td>
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## Four Studies of Risk

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<th>Study</th>
<th>Methodology</th>
<th>Sponsors and Partners</th>
<th>Sample</th>
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<td>Retirement Plan Preference Survey (2003)</td>
<td>Two stage mail panel</td>
<td>SOA, AAA</td>
<td>Second stage surveys: sent to 1,088 workers and 1,889 retirees. Response rate for workers 75% and 33% for retirees</td>
</tr>
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<td>Retirement Confidence Survey (2003)</td>
<td>Telephone Interviews Series starting in 1993</td>
<td>EBRI, ASEC, Matthew Greenwald &amp; Associates</td>
<td>1000 individuals were interviewed, 782 workers, 218 retirees</td>
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</table>
| Insight into Participant Investment Knowledge & Behavior | Eight in a series starting in 1991 | John Hancock, Mathew Greenwald & Associates | 801 respondents
Respondents were people who contributed to 401(k) plan and had a choice of funds to invest. |
Marital Status
By Age and Sex, United States 2000

Source: Table 51, Statistical Abstract of the United States 2001, U.S. Census Bureau
# Educational Messages Might Be Targeted to Four Age Groups

<table>
<thead>
<tr>
<th>Content</th>
<th>Long Before Retirement</th>
<th>Age 50 - Retirement</th>
<th>At Retirement</th>
<th>Post-Retirement</th>
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<td>Savings</td>
<td>Get people to save enough</td>
<td>Continue to save</td>
<td>Save to keep up with inflation</td>
<td>Maintain assets or start conservative spend-down</td>
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<td>Invest well for the long term</td>
<td>Invest for different time horizon</td>
<td>Shift investments</td>
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<td>Risk Management</td>
<td>Start to consider retirement dollars</td>
<td>Finalize risk putting management in place</td>
<td>Maintain risk management program and be sure it is fully implemented</td>
<td>Management program</td>
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Savings:
- Get people to save enough
- Continue to save
- Save to keep up with inflation
- Maintain assets or start conservative spend-down

Investment:
- Invest well for the long term
- Invest for different time horizon
- Shift investments
- Maintain investment program
- Consider “regular income” for some money
- Shift more money into “regular income”

Risk Management:
- Start to consider retirement dollars
- Finalize risk putting management in place
- Maintain risk management program and be sure it is fully implemented
- Management program
Misperceptions of Average Investment Returns

What do you expect stocks, bonds, money market and stable value investments to earn annually, on average during the next five and twenty years?

Source: Responses to the John Hancock Survey of Defined Contribution Plan Participants 2002
Workers Have Other Significant Knowledge Gaps

- Cannot estimate eventual retirement benefit:
  - 50% of DC workers, 34% of DB workers
- Do not know method used to determine benefit:
  - 22% of DC workers, 12% of DB workers
- Cannot estimate current termination benefit:
  - 33% of DC workers, 39% of DB workers
- Do not know when they would be able to access that termination benefit:
  - 25% of DC workers, 20% of DB workers