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CENTER FOR RETIREMENT RESEARCH AT BOSTON COLLEGE

# HOW MUCH IS THE WORKING-AGE POPULATION SAVING?

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It is crucial that today's workers save for retirement. This is because Social Security replacement rates will decline due to increases in the Normal Retirement Age, rising premiums for Medicare, higher personal income taxes, and potential adjustments to restore financial balance to the system. And accumulations in 401(k) plans may well be much lower than people anticipate. As such, personal saving will become increasingly necessary for retirement security.

So how much are individuals saving for retirement? The standard measure, the personal saving rate reported in the official U.S. National Income and Product Accounts (NIPA), has fallen dramatically and in 2004 stood at a dismal 1.8 percent of disposable personal income. But is this indicator an accurate measure of saving behavior?

The NIPA personal saving rate is a much beleaguered statistic. Economists complain that 1) consumer durables that generate services over an extended period of time (such as automobiles and dishwashers) are treated as consumption rather than investment; and 2) interest income and outlays are not adjusted for inflation. Analysts interested in retirement security bemoan the exclusion of capital gains, because these gains may help finance post-retirement consumption. This study focuses on a new issue — namely, NIPA combines the saving of the working-age population with the dissaving of retirees. This aggregation would not distort trends in saving if retirees were a constant proportion of the population, but with the retirement of the baby boom generation, their ranks will swell. As a result, even if the saving of each age group remains unchanged, the aggregate saving rate will decline.

This study thus attempts to separate the saving out of current income done by the working-age population (those under age 65) from that undertaken by retirees (those 65 and over). The first section describes the NIPA accounts. The second section estimates the share of NIPA personal saving that belongs to those under age 65. The third section broadens the calculation of household saving to include business saving.

Three conclusions emerge from this analysis. First, adjusting the NIPA personal saving rate shows that personal saving by the working-age population is significantly higher than the reported national rate. Moreover, allocating a portion of business saving to working-age households further raises their saving rate. The pattern of saving over time is also easy to understand. It remains more or less steady until the last half of the 1990s, at which point it declines in response to the run-up in the stock market. When the bubble burst, the NIPA saving rate rebounded as people no longer had capital gains to spend.

Second, commentators should be careful not to double count saving through employer-sponsored plans by referring to pension saving and personal saving as if they are different components. In fact, for most of the time between 1980 and 2003, pension saving accounted for all of personal saving, and, today at least, saving outside of pensions is negative for the working-age population.

Finally, the analysis (inadvertently) helps explain the puzzle surrounding the collapse of the *total* NIPA personal saving rate beginning in the early 1980s. While capital gains were part of the story in the 1990s, most of the downward trend can be explained by changes in the saving rate of those 65 and over. Three factors conspire to make their saving increasingly negative. Pension income – not counted in the NIPA – has become an increasingly important source of the income of those 65 and over. The decline in nominal interest income as inflationary pressures waned in the 1980s reduced saving rates for the whole population, but had a particularly large effect on those 65 and over who receive a disproportionate share of the interest. And the rising cost of health care boosted expenditures — again particularly for those 65 and over who bear a disproportionate share of the burden.

In short, the total NIPA personal saving rate increasingly understates the saving of the working-age population, and the discrepancy will only increase as the share of the population 65 and over rises. However, a significant NIPA saving rate by the working-age population does not necessarily mean that they are adequately preparing for retirement since virtually all of personal saving, and most of private saving, consists of saving through pension plans.



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