Briefly Noted

Future Retirees at Greater Risk of Hardship

Most current retirees appear able to withstand some type of financial shock. Future retirees may have more difficulty doing so due to changes in the retirement system, says a research fellow at the Center for Retirement Research (CRR) at Boston College.

Financial shocks are primarily described as a spike in medical expenses or a sharp drop in income. The latter most often occurs when a retiree is widowed. Following the death of a spouse, Social Security benefits are reduced along with pension benefits (if the deceased had access to one).

While a drop in income can create problems, a 2009 study found that most retirees do not forgo needed food or medication. A separate study found that non-medical spending increases following a health shock. (Public and private insurance helped to cover the cost of the medical expenditures.) Combined, the studies found most widows to have sufficient reserves to maintain their standard of living.

Future retirees may have a tougher time absorbing such shocks. The transition from pensions to 401(k) plans is leading to a greater reliance on personal savings. A 2012 study found personal financial assets accounting for just 42% of retirement income for Gen-Xers in the middle-income range, assuming 80% of financial assets are annuitized at retirement. Projections cited by the CCR paper suggest retirement replacement rates could be 9% lower for middle-income Gen-Xers relative to recent retirees. The paper's author further cautions that these numbers could be conservative since many retirees may not annuitize or be able to do so at actuarially fair rates.

Future retirees also face the potential problem of a big financial shock occurring early in retirement. If forced to withdraw more than planned from their savings to cover expenses, they would increase the risk of incurring financial hardships later in life. There is also the possibility of a sharp downturn in the financial markets occurring soon after retirement, making difficult choices about managing savings even harder.

CCR suggests that households approaching retirement consider both increasing how much they save and reducing fixed expenses, especially by downsizing. Working longer, annuitizing wealth and using reverse mortgages are also suggested.

Source: "Will the Financial Fragility of Retirees Increase?," Steven A. Sass; Center for Retirement Research at Boston College; February 2018, Number 18-4.

Workplace Retirement Plans Affect Savings Behavior

A Pew Charitable Trusts survey looked at the difference in behavior between workers who participated in employer-sponsored retirement plans [e.g., 401(k) plans] and those who did not participate in such plans. More than one-third of private-sector workers lack access to workplace plans. Slightly more than three out of 10 (31%) who have access don't participate in such plans.

Among the survey's findings were:

- **Retirement Planning Is More Common Among Participants:** More than two out five participants (41%) in workplace savings plans said they have engaged in retirement planning within the past two years. In contrast, just 16% of those without access, and 14% of those with access, who have never participated say that they have planned for retirement. About half of all respondents who answered in the affirmative reported using online tools or calculators, though many admitted to simply guessing.
- **Participants Are More Likely to Save in Outside Accounts:** When asked about saving for retirement in external retirement accounts (e.g., an IRA), 53% of those participating in a workplace retirement plan said they do so. Conversely, just 15% of those who have both never participated and lack access to a workplace plan have such savings.
- **Not Being in Workplace Plans Adversely Affects Saving Habits:** Approximately 40% of participants who either lack access or have access to employer-sponsored plans but don't participate in them say they have not contributed anything to retirement savings within the past two years.
- **Majority of Survey Participants Would Not Contribute Windfall Savings to Retirement Accounts:** When asked what they would do with a $10,000 windfall, only 36% of respondents said they would set aside some of it for retirement. Those who both lack access and have never participated in a plan were the most willing to use the windfall to boost savings (43%), while just 36% of those currently participating in a plan say they would boost their savings. When given other options for spending the windfall, respondents from all categories allocated the largest dollar amounts to paying down debt.

Source: "Workplace Retirement Plans Tend to Sharpen Focus on Financial Futures;" The Pew Charitable Trusts; February 2018.

Survey: 8% of Older Adults Are Victims of Financial Fraud

A series of questions in the 2016 Health and Retirement Study (HRS) asked respondents over the age of 50 about financial victimization. (The median age was 68.) Eight percent reported to have fallen prey to at least one form of financial fraud within the past 12 months.

The HRS module not only asked respondents if they had been victimized, but also asked about several types of investment fraud situations including, but not limited to, a meeting offering a free meal for some sort of investment (e.g., timeshares or annuities), an email or telephone pitch for an investment by a stranger, a pitch for high-return investments (e.g., oil and gas) and a fraudulent investment recommended by a friend, relative or adviser. Survey participants were also asked about financial scams such as paying money to receive a prize or experiencing or being aware of attempted unauthorized use of their financial accounts.

On a percentage basis, the number of respondents who admitted to being victims of a specific type of investment fraud was small. For example, only 3% said they had invested after being given a free meal. Four percent said they paid to win an award (though the study's authors noted that the question did not instruct respondents to exclude lottery tickets which, while being very risky, are not fraudulent).

Responses to the financial scam section were higher. Thirty percent of respondents revealed "that others had used or attempted to use one of [their] accounts without permission." The question was not specific enough to differentiate between those who were victims of such events and those who were targeted, but not victimized. The study's authors describe the high level of such occurrences as indicative of actual and attempted "financial exploitation by family and friends or identity theft by strangers."

Not found by the survey were consistent characteristics about which seniors might be more prone to victimization. No systematic association was found among education, wealth, health, age, gender or marital status. Levels of financial literacy also didn't seem to be a factor, though those with greater financial knowledge were "significantly more likely" to indicate that an account of theirs had been used or was attempted to be accessed without permission.

Source: "Exploring the Risks and Consequences of Elder Fraud Victimization: Evidence from the Health and Retirement Study," Marguerite DeLiema, Martha Deevy, Annamaria Lusardi and Olivia S. Mitchell; Michigan Retirement Research Center Working Paper; WP 2017-364.

Overconfident CEOs Buy Back More Stock

Companies with chief executive officers who exhibit signs of overconfidence are more likely to repurchase their own shares and tend to allocate more dollars to doing so. While these actions are followed by aggregate positive post-repurchase returns, the returns are not as positive as they are for repurchases by companies with CEOs who are comparatively less confident.

Overconfidence was defined by two methods. First, the study's authors looked at whether a CEO was holding onto vested, in-the-money options. These are contracts that the CEO can currently exercise and realize an immediate profit when doing so. Overconfident CEOs are more likely to hold onto such options (likely on the expectation of the options increasing further in value). Second, articles in the financial media were analyzed to determine how confident or cautious the CEO was described as being.

Both measures of overconfidence were found to be "associated with a significantly greater likelihood of a repurchase and significantly larger dollar amount of repurchases in the following year." The relationship is weaker among companies with strong growth prospects or that are experiencing higher stock returns. The latter may signal less concern among overconfident CEOs about the valuation of their stocks.

The study also identified several other commonalities:

- Overconfident CEOs are more likely to engage in stock buybacks at lower levels of cash holdings than other CEOs. Overconfident CEOs are also more likely to engage in buybacks when their companies have lower credit ratings.
- Overconfident CEOs who "have more power, and are more insulated from internal or external discipline, will be more likely to act on their behavioral bias to do more repurchases." Such CEOs also serve as the chairman of the board for their respective companies.
- Institutional investors seem to approve of such repurchase activity. The study's authors suggest that buybacks may be viewed as preventing overconfident CEOs from investing in underperforming investments. Alternatively, buybacks may provide an avenue for institutional investors to sell their shares.
- Overconfident CEOs are more likely to reduce special dividends and buyback shares than non-overconfident CEOs. Nonetheless, special dividends still tend to remain higher when an overconfident CEO is running the company.

Source: "Does CEO Bias Escalate Repurchase Activity?," Suman Banerjee, Mark Humphery-Jenner and Vikram Nanda; Journal of Banking and Finance (2018).