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TOPIC #13: **Age of Retirement Influences Consumption**

PROMPT: **Discuss Age of Retirement influences on consumer consumption during retirement.**

An important variable influencing consumer consumption decisions during retirement is the Age of Retirement. Three applications of this variable are broadly discussed—age of small business owners versus retirement preparedness, correlation of subjective retirement age expectation versus actual consumption decreases at retirement, and transitions in consumption patterns in early retirement years versus later retirement years.

Small business owners are important to financial planners, as their businesses employ 50% of the country's workforce and often practitioners are responsible for coordinating the client's personal and business planning together. Studies are limited on isolating business owners and psychological factors leading them towards retirement preparedness. One researcher McCullough (2012) did a series of surveys on small business owners and the level of preparedness for retirement planning looking at behavioral factors of engagement, satisfaction and future time perspective. Business owners consistently reported the highest level of job satisfaction, was derived from of aspects of personal freedom, sense of independence and flexible lifestyle.

McCullough referenced a previous study by Stawksi et al. (2007) that hypothesized and tested a model suggesting retirement goal clarity "mediates the relationship between age and retirement planning activities". Of McCullough's six main hypotheses raised, levels of job satisfaction and engagement at work in business owners was thought to negatively affect retirement goal clarity, and therefore lead to less retirement planning knowledge and less retirement planning activities. McCullough concluded that business owners' satisfaction *increased* likelihood of acquiring retirement goal clarity. Further, this was most significant in owners who were older than 49 or in the business more than 14 years and already had retirement plans in place.

Haider and Stephens (2007) tackled the traditional thinking that consumption decreases at retirement. The study recognized how age plays an important role in retirement planning, and how older households often reduce consumption as they age. Based on life cycle/permanent income hypothesis, Haider and Stephens offered that, the consumption fall may not be as dramatic as expected. They studied whether the relationship between age and actual retirement is the same as the relationship between age and expected retirement. They juxtaposed "retirement expectation" alongside studies where retirement income expectations are good predictors of realized income, where subjective job loss probabilities are related to subsequent job displacements.

Drawing on two longitudinal studies that sampled 11,000 individuals aged 58-63 and 7,700 aged 51-61, the researchers isolated questions regarding each individual's expected age of retirement. Their findings showed over 66% of respondents retired within 1 year of their expectations and concluded it was a strong predictor. Pre-retirees update their expectations as they nearer their previous target date, and with each two-year interval or "wave" of assessment, the retirement age expectation increases its correlation with actual retirement decisions. These researchers concluded that age profile of actual retirement versus expected retirements are not the same, "which means that age is not a valid instrument for expected retirement" (Haider & Stephens, 2007) but rather, *subjective retirement expectations* is a better instrument for expected retirement. Once retired, consumption falls by 7-11% for workers who retire as expected, which is about 33% less in magnitude when age is benchmarked instead of subjective expectation.

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Frank et al. (2012) addresses the longevity risk of early age withdrawals in retirement and subsequent withdrawal complications as retirees live into old age. Therefore, Frank et al. (2012) questioned *when* retirees might recognize they may live into very old age and consider transitioning into different consumption patterns. Also, they illustrate how unadjusted withdrawal rates become exponentially larger as a retiree nears 85 years old, which emphasizes the importance of practical withdrawal patterns in the early years. The researchers outlined two types of retiree outlooks. First is "Consumption Oriented", the desire to consume more during the early "go-go" years and cut back during "slow-go" and "no-go" years. Second is "Inheritance Oriented", those who prefer to "push" consumption into later years by preserving some of their current portfolio balances, often worried about longevity risk due to family history. Frank et al. (2012) concluded retirees in their 60's are more consumption oriented, and retirees in their 70's are more inheritance oriented. Therefore, how early one retires to this transition range (mid 70's) will likely have greater pressure on duration of resources.

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