Can I Retire? Benchmarks to Consider in Making the Retirement Decision

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O ne of the many responsibilities of financial planners is to help their clients with the decision to retire. This option represents a significant life-cycle event with many personal and familial ramifications to be considered. The purpose of this paper is to assist the financial planner in this process by providing benchmarks for a client to use in arriving at a decision.

There have been a variety of studies that project the requirements for individuals who are going to make the retirement decision, but very little in the way of concrete evidence concerning the experience of those individuals who actually decide to either retire or not to retire. We provide that evidence based on a longitudinal study of married couples and present both financial and nonfinancial variables in the format of benchmark scenarios.

During the last two decades, McCarthy (2002) suggests that retirement planning has shifted from a projection of income needs over the individual’s period of retirement and identification of potential shortfalls in income sources to a much broader analysis. This change has been based on the recognition of the complexity of this period of life and a variety of analytical tools and techniques that have developed. In particular, he notes that spending patterns change with age and that quality-of-life issues are playing a larger role in the decision-making process.

Anthes and Most (1999) believe that during the next 30 years, both men and women will live longer and that this increased longevity will dramatically affect the retirement experience. For example, it may be necessary to reconsider the meaning of terms such as work, early retirement, and financial adequacy. Quinn (2001) suggests that planning is multi-dimensional and should include the client’s lifestyle needs in terms of insurance, estate planning, and taxes. Furthermore, issues such as physical and mental health, personal relationships, intellectual curiosity, spiritual effects, and a sense of self-worth need to be incorporated into the planning process.

With the changing dimensions of the retirement decision, can the past be any guide to the future for the retirement planning process? We examine evidence from those who have entered or are near retirement, and the factors that appear to influence their decision to retire. Providing this insight to clients may help financial planners guide them through the retirement planning process.

Executive Summary

- The decision to retire is a significant life-cycle event for a financial planner’s client(s).
- To aid financial planners and their clients in this process, we analyze a longitudinal database of individuals who have retired or are near retirement. We summarize the findings and provide both financial and nonfinancial benchmarks that clients can use in arriving at their own retirement decision.
- Among the variables examined, we find that age, health, a spouse’s retirement status, and mortgage debt are the factors that most significantly influence the decision to retire.
- We also illustrate differences found between those who decide to retire and those who do not by providing eight benchmark scenarios. The first four scenarios compare retired and nonretired married couples based on their reported health status, while the second set of comparisons is based on the ownership of business assets.

Data and Methodology

Data sample. Our sample is derived from the first four waves of the Health and Retirement Study (HRS) database. It was first administered in 1992 to approximately 7,600 households in which at least one member was between the ages of 51 and 61. It has since been re-administered.
and the data disbursed for three additional "waves" of data from 1994, 1996, and 1998.

Based on the format of the database, we analyze the retirement decision of the designated "financial respondent" for each married household. This respondent self-reports his or her retirement status as being "completely retired," "partly retired," or "nonretired." In an effort to draw the cleanest comparisons between those who are retired and those who are not, we omit our study the semi-retired category.

The retired sample reflects those financial respondents who are newly categorized as retired within each respective wave. For example, the retired sample in 1994 are those financial respondents who did not consider themselves to be retired in 1992, but whose status has changed to retired in 1994. For 1992, the retired sample includes all households whose financial respondent is retired at the time of the initial survey.

Methodology. We use a probit regression to test which financial and nonfinancial factors significantly influence the decision to retire. To properly estimate this influence, we use the data from 1992 to estimate the respondent's retirement decision in 1994, and define the tests for 1996 and 1998 in a similar manner. Table 1 contains a description of each variable tested.

To measure education's effect, we assume that the highest level of education in the household will likely be the most influential, and therefore define "household education" (HHEDU) as the maximum education level of the financial respondent or his or her spouse. The respondent's self-reported health status and that of his or her spouse (HEALTH/SP_HEALTH) are divided into five categories in the HRS survey, with a higher number indicating relatively poorer health. To measure the impact of the spouse's retirement decision, we also include a variable SP_RET. In connection with the health variable, the existence or lack of health insurance coverage may also significantly influence the decision to retire. To capture this effect, we include INSUR to indicate whether the household has employer-sponsored health insurance, as defined by the HRS survey.

We include CHILD in our model because raising children may place significant demands on household finances and potentially influence the retirement savings rate throughout the respondent's life. Simi-
Summary Statistics by Data Wave for Full Married Sample

For the 1992-1998 data, the newly retired category designates households whose financial respondent has retired since the immediately preceding survey.

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<td>57.34</td>
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<td>2.77</td>
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* and ** indicate the means of the newly retired and nonretired samples are statistically different at the 1% and 5% level of significance, respectively.

Empirical Results

Descriptive statistics and regression results. Table 2 shows the summary statistics for the newly retired and nonretired samples by year. With respect to the demographic variables, the average age of the financial respondent (AGE) and his or her spouse (SP_AGE) are significantly higher for the retired households than for the nonretired households. Note, however, that with the exception of the 1992 data wave, the spouse’s health status (SP_HEALTH) is not significantly different between the two groups.

The results for SP_RET show that, on average, the spouse of a retired respondent is more likely to be retired than is the spouse of a nonretired respondent. There is also a significant difference for the INSUR variable, with fewer retired households having employer-sponsored health insurance.

FIN is total household financial assets, and includes the balances of all fixed-income securities, equity holdings, individual retirement accounts (IRAs), and Keogh plans. BUSINESS includes the equity value of any family business, farm, and real estate holdings excluding the primary residence. INCOME is the sum of employment-based earnings and income streams from retirement pensions and Social Security for the household. As with SUPPORT, the dollar value of any mortgage on the respondent’s primary residence represents a potentially significant demand on current financial resources, so we include a MORTGAGE variable as well.

Among the financial variables, MORTGAGE is significantly lower for retired households. Historically, retirees have a paid-off mortgage that reduces the required income in retirement. In this sample, the average retired household still has a mortgage, but it is roughly half the amount of the average nonretired household (with the exception of 1996, where it is 64 percent). It could be that retirees are maintaining a mortgage for tax purposes (assuming deductions are itemized) while the significantly higher mortgage levels of the nonretired are an impediment to their retirement.
For the financial assets (FIN), the average retired household has accumulated from 130 percent more (in 1998) to 175 percent more (in 1994) than the average nonretired household. In contrast, the mean level of business assets (BUSINESS) is lower everywhere for the retired group. A possible explanation for the latter result is that BUSINESS reflects assets that are relatively illiquid and that may be difficult to convert to resources that are more conducive to retirement.

In summary, the results of Table 2 show that the retired and nonretired households differ significantly. The average married retiree is generally older, less educated, in poorer health, and is less likely to have employer-sponsored health insurance than his or her nonretired counterpart. The average retiree is also more likely to have a retired spouse and is less likely to be supporting dependents. The retired sample has mortgage debt, but at a significantly lower level than the average of the nonretired group. The average retired couple also has a greater accumulation of financial assets, but a lower amount of business assets and lower household income.

In addition to testing each variable separately to see if there is a statistically significant difference between retired and nonretired respondents, we use a probit regression analysis to simultaneously test for the influence of all of these factors on the retirement decision. When controlling for all the variables, we find the AGE, HEALTH, SP_RET, and MORTGAGE estimates are statistically significant. The results suggest that a respondent who is older, in poorer health, or who has a retired spouse is more likely to retire. The MORTGAGE estimate indicates that the higher the dollar value of the mortgage, the less likely the respondent is to retire.

Note that the asset and income variables do not significantly affect the retirement decision. This suggests that while the sample of married retirees has a substantially higher level of financial assets on average (see Table 2), the accumulation still exerts little to no influence over the decision to retire. While we suspect this may indicate adequate (as opposed to inadequate) financial preparation, we cannot say with certainty.

Descriptive benchmarks. Table 3 divides the HRS sample into two categories based on the respondent’s self-reported health condition and ownership of a business. We do so to determine if drilling down into the data based on a specific characteristic will produce more information than simply examining the retired and nonretired samples at an aggregate level. For clarity, we focus on the single set of survey results from 1998.

Panel A of Table 3 provides descriptive statistics for the sample when the focus of the analysis is on their reported health condition. It is constructed on four out of the five possible self-reported health conditions, with “good health” being a combination of those who report themselves in excellent or good health and “bad health” being a combination of those who report themselves in poor or very poor health. The sample size is 1,116 households for this slice of the data, with 933 (84 percent) reportedly being in good health.

For the nonfinancial benchmarks, Panel A shows that those in poor health are less educated, and are more likely than their healthy counterparts to have a spouse who is also in poor health. Those in poor health are also more likely to lack employer-sponsored health insurance.

When we test for differences in financial variables, those who report good health have a mortgage that is more than twice as large as those in poor health. This suggests that those who are in poor health either have lower-priced homes or have managed to pay off more of the debt on their property, or both. In addition to a much larger mortgage, those in good health have two-and-a-half times more financial assets than those in poor health. Lastly, those in good health have almost twice the income of those in poor health. These financial differences suggest that those in poor health may have been in this condition for some period of time.
Table 3, Panel B, divides the sample into those who own a business and those who do not, with 58 percent of the sample (581 households) having business assets. The average business owner is more likely to be male and the nonbusiness-owner female. While there is a significant difference in education level, the difference is not as large as when health is examined. Also, there are significant differences in HEALTH and SP_HEALTH, but the overall health of both the respondent and the spouse appear to be more alike. The business owner is less likely to have employer-sponsored health insurance, and is more likely to be supporting dependents.

There is a significant difference between the two groups on all of the financial variables. The business owner's mortgage is 135 percent larger, the financial assets are over 200 percent greater, and the income is 132 percent greater than those who do not own a business.

Our examination of the sample when divided into groups based on health and business asset ownership suggests that there are enough statistical differences to view each of these groups by their decision to retire or remain in the workforce. Table 4 provides a total of eight scenarios of average married couples to serve as benchmarks for the financial planning client's edification.

Health and the decision to retire. The first scenario can be illustrated by Mike and Karen (MK in Table 4). Mike is in good health and recently retired. He has at least some college education. Karen reports herself in good health and likely to be working. The couple has employer-sponsored health insurance, which is probably coming from Karen's employer. Mike and Karen have children, but are not financially supporting them or any other dependents. They are carrying a mortgage on their home of $24,144 and have financial assets in taxable and tax sheltered accounts of $157,895. Their business assets are valued at $92,888 and their household income is $58,472. They are both too young to collect Social Security benefits, but Mike is very close to being able to apply for a reduced benefit.

Contrasting with this first scenario is our second couple, Jim and Susan (JS). Jim considers himself to be in poor health and has just recently retired. Jim has a high school diploma, which represents significantly less education than Mike. Jim's wife Susan is still working and reports her health as good, but statistically it is not as good as Karen's. Although the couple has employer-sponsored health insurance, they are statistically less likely to have it than are Mike and Karen. They have children, but financially support no dependents. Their mortgage is $17,929, which is 74 percent of the mortgage that Mike and Karen have on their home. Their financial assets are $72,094, significantly less than (46 percent of) the first couple's assets. Their business assets are similar at $85,377, but their
Contributions

Lahey

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Lahey

income is statistically less than Mike and Karen at $31,037.

The primary differences between the two couples are the likelihood of having employer-sponsored health insurance, their health condition, education level, and their financial assets and income. Mike appears to be in good health and has a higher mortgage, twice the financial assets, and a much higher income level. One might conclude that Jim’s retirement decision was based more on his health condition than his financial condition.

Our third scenario involves Matt and Ann (MA), with Matt being in good health and deciding to continue to work rather than retire. They are younger than the first two couples, and at least one of them has some college education. Ann reports that she is in good health and is still working. They have employer-sponsored health insurance which may be coming from one or both of their employers. They have two children whom they assist financially.

Matt and Ann’s mortgage is $45,169, or double that of Mike and Karen, while their financial assets ($101,640) are 64 percent of the first couple’s. Additionally, their household income is $73,942, or 126 percent of Mike and Karen’s income. It may be that Matt’s decision to continue working is driven by the need for additional income to support the higher mortgage and compensate for fewer financial assets.

For the fourth couple, John and Leslie (JL), John is also not retired but reports that he is in poor health. When compared with Matt and Ann, their education level is significantly lower, with John and Leslie having little more than high school diplomas. Like John, Leslie reports she is in poor health but has decided to keep working. The couple has employer-provided health insurance, which may be one of the reasons that John and Leslie are both still working.

They have an adopted child and are financially supporting John’s mother. Their mortgage balance is 45 percent of Matt and Ann’s ($20,233), but their financial assets are only 25 percent of Matt and Ann’s ($23,861). They have far and away the fewest financial assets. They also have the lowest-valued business assets at $57,754. They have a household income of $41,190, which is 56 percent of Matt and Ann’s.

When the four couples are compared, those who are in good health appear to be in better financial condition than those in poor health, regardless of whether they are retired. They have larger mortgages, more financial assets, business assets, and income. The results highlight the important effects of a client’s health condition in particular, and the need to consider potential health risks and the availability of insurance coverage if they decide to retire. Finally, those who continue to work may be doing so because of a need to build financial assets and reduce their mortgage balance.

Business ownership and the decision to retire. For the scenarios involving business ownership, our first representative couple is Paul and Christina (PC). Paul has recently retired and owns business assets. They each have some college education and both report they are in good health.
Our last illustrative couple is Kevin and Jane (KJ). They own no business assets and Kevin is still working. At least one of them has some college education and each reports good health, but their education level is significantly lower and their health conditions significantly poorer than Andy and Dawn's. But they are more likely to have employer-provided insurance than are Andy and Dawn. Kevin and Jane have children whom they are financially supporting. Their mortgage is $33,851, significantly less than Andy and Dawn's mortgage. Kevin and Jane's financial assets are $59,989, which is significantly less than (50 percent of) Andy and Dawn's assets, particularly when you consider that Kevin and Jane do not have any business assets. Their household income is $59,738, and is also significantly lower than that of Andy and Dawn.

The four couples described in the business ownership category provide clear benchmarks of the effect of having a business. In addition to having greater financial assets, both Paul and Christine and Andy and Dawn have business assets that exceed $200,000. But Andy and Dawn have chosen to continue to work and have a much larger mortgage balance, lower financial assets, and are younger than Paul and Christine. Interestingly, the two couples who do not own a business are in poorer health, have less education, less financial assets, and a smaller household income than their business-owning counterparts.

Summary and Conclusion

The findings of this study suggest that the retirement decision is based on criteria that include both nonfinancial and financial factors.

- Our descriptive statistics show that the average married retiree and nonretiree differ on numerous factors.
- When actually making the decision to retire, we find that age, health, the spouse's retirement status, and mortgage debt are the factors that most significantly influence the decision.
- To make the data more relevant to financial planning clients, we illustrate differences between those who decide to retire and those who do not by providing a description of eight different
The first four couples are compared based on their reported health status and the second four are compared on the basis of owning a business or not. By examining the nonfinancial and financial aspects of these eight couples who have reached the age to consider a retirement decision, we provide the financial planner benchmark examples for his or her clients to consider.

### Endnotes

1. Note that because of limited data availability, pension and 401(k) data are not included in our study. Financial planners should be aware of this when interpreting the results.

2. Full regression results are available from the authors on request.

### References


