COVID-19’s Financial Impact on Older Americans

By George A. (Sandy) Mackenzie *Wed, Apr 8, 2020*

'Pandemics and financial crises have occurred throughout history,' writes our guest columnist, a former IMF official. 'Think of the biblical account of Ancient Egypt, and the cycle of lean and fat years. That story has never really gone out of date.'

The COVID-19 pandemic is affecting the finances of older Americans in a variety of ways. The effect depends partly on whether they are retired, working, or recently unemployed. It also depends on the sector of the economy they work in, the level of unemployment insurance (UI) benefits they receive, and the speed with which the benefits are disbursed by their state.

On the plus side, older workers will be less hard hit than the young. Older Americans are more likely to hold public service jobs, and this sector will probably be less badly affected. Workers in the leisure and hospitality industries (restaurants, bars, etc.) have been especially hard hit. The median age in this sector is only 32 years compared with the economy-wide average of 42 years. Gig workers in general tend to be young, and they are suffering more than most.

Whatever their age, low-paid workers will see a higher share of their income replaced by UI benefits, which the Coronavirus Aid, Relief, and Economic Security (CARES) Act—the 2.3 trillion-dollar stimulus law signed last week by the President—has increased by $600 per week for 13 weeks.

Nonetheless, American households headed by those near retirement (aged 55-64 year old) still depend for almost all of their income on the labor market. Their labor force participation rate is high and their unemployment rate low in normal times, but even in normal times the loss of a job for this age group usually leads to a long period of unemployment. A subsequent job is often paid less, and comes without health benefits.

A question that arises is whether a long period of extraordinarily low economic activity in the wake of the pandemic will lead to a permanent exit of older workers from the labor market. If so, the hardship they experience would be considerable. The debt burden of this age group is already substantially higher than it was in the early 1990s, although declines in interest rates may have at least partially offset the burden of servicing that debt.

Responses to a drop in cash flow

Social Security. Americans who have reached age 62 can claim Social Security retirement benefits, but this means that they will forego the substantial increase in the benefit that results from delaying a claim to their normal retirement age or even later. Those who can keep working and delay claiming Social Security probably should.

Dividend stocks. Most American households, even older households, do not hold a substantial share of their assets in stocks or bonds. According to the Federal Reserve’s Survey of Consumer Finances, even the top 10% of households by income with a head aged 55 to 64 held on average just nine percent of their total assets—which include a household’s principal residence and other real property—in directly and indirectly held stocks in 2016. For the 65-74 age group, the share in stocks was twelve percent.

However, the clients of financial advisors who subscribe to the *RIJ* are undoubtedly well up in the top 10% of income, and the share of stocks in their total assets would be much higher. Many have already suffered a substantial decline in the value of their assets, and they face some difficult decisions.

For older Americans still enjoying a steady income, the undoubtedly strong temptation to liquidate the share of their portfolio in stocks or stock mutual funds should probably be resisted, although the decision to do so obviously depends on the individual circumstances of the households affected. The key question investors need to ask is whether they could survive financially if the stock market did not recover strongly.

To judge from the experience of the Great Recession, the stock market will eventually recover. That said, we are living in extraordinarily uncertain times, and the often seismic day-to-day swings in the market are unnerving. Shifting stock holdings from growth stocks to stocks emphasizing income might be worth considering to avoid the need to sell stocks to finance current expenditure.

Retirement plan savings. For older Americans who have lost their jobs, emergency withdrawals from their 401(k), IRAs and other retirement accounts will probably be necessary, but these need to be kept to a minimum. For those households that have managed to accumulate at least a moderate balance in their retirement plans and are nearing retirement age, withdrawals can be seen as a bridging strategy until the Social Security benefit kicks in.

Some employer-provided 401(k) plans offer plan participants either phased withdrawals or annuities in addition to lump-sum withdrawals. Choosing between a lump-sum withdrawal and an annuity is never an easy decision. Human beings, being human, tend to underestimate the value of a future income stream relative to a lump sum paid today, and this tendency is probably exacerbated in uncertain times. The decision to take a lump sum over a future stream of income is probably best made with the help of a financial advisor.

Reverse mortgages. Taking out a conventional mortgage is another strategy for homeowners with sufficient equity in their properties. A reverse mortgage (RM), or a reverse-mortgage line of credit, are other possibilities, since they do not have to be paid back until the death of the mortgagor or the sale of the property. RMs have not proved popular, but these strategies may be relevant for some of the clients of *RIJ* subscribers.

The future

Even if labor market participation rates recover, a long period of unemployment could seriously jeopardize this group’s retirement prospects, quite apart from the impact of the pandemic on the value of their assets. The years from 55 to 64 should normally be the ones where retirement assets are being built up. Mortgages are being paid down, and other financial obligations, like financing the education of dependents, should be declining. (That said, older households have recently been incurring substantial direct debt to finance their children’s education.)

Looking to what we must hope will be a brighter future, Americans households of all ages need at least to begin to save more. The strategy of living for paycheck to paycheck has now been revealed as fatally unwise and short-sighted. No one could have self-insured against the pandemic, but many households could have been better prepared to weather its effects.

We must pray that we are never again assailed by a time as trying to the soul as this one, but pandemics and financial crises have occurred and reoccurred throughout history. Think of the biblical account of Ancient Egypt, and the cycle of lean and fat years. That story has never really gone out of date.

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