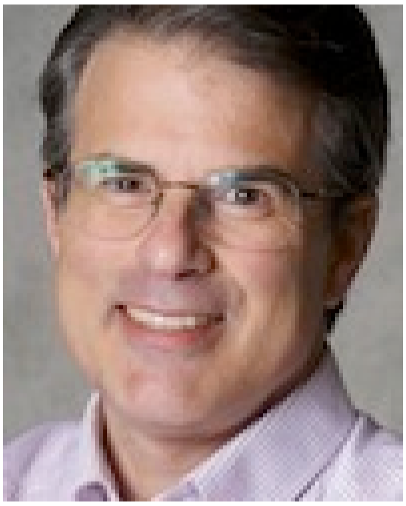
So Far, Most 401(k)s Don’t Amount to Much

By Kerry Pechter *Thu, Nov 7, 2019*

The 401(k) system still hasn’t produced the generation of wealthy retirees that, under ideal conditions, it could have. Scholars from the American Enterprise Institute and the Center for Retirement Research at Boston College explain why.



The 401(k) defined contribution retirement saving system has been in existence in the U.S. since 1981, introducing millions of “Main Street” Americans to the pleasures and pain of Wall Street. Leading-edge boomers were 35 years old.

Since then—perhaps not coincidentally—the Dow Jones Industrial Average has grown, with only two great interruptions, from 1,016 on April 28, 1981 to 27,492 on November 5, 2019. That’s nominal growth: Its compound annual growth rate with dividends, adjusted for inflation, has been 7.8%.

Over that period, bonds haven’t done too badly either. Between April 1981 and October 2019, the 10-year Treasury showed an average annual return of 6.6% (or 3.67% when adjusted for inflation).

But, to the mystification of some economists and the frustration of many savers, those four decades of dizzying index growth—no doubt driven in part by a worldwide Boomer savings boom as well as the IT revolution—the 401(k) system hasn’t produced the generation of wealthy retirees that, under at least on paper, it might have.

Some plan participants have certainly large accumulations—those continuously employed in high-paid jobs in profitable companies with generous matching contributions and the capacity to save a high percentage of salary on a tax-deferred basis—but the average journeyman worker has lower-than-expected accumulations in 401(k)s or IRAs.

A new **study** from the Center for Retirement Research at Boston College (the Center) shows that in 2014 “the typical older worker [had] less than $100,000 in 401(k)/IRA assets, instead of the $364,000 he would have had under a system in which workers participated throughout their careers, paid zero fees on account balances, and did not withdraw money prematurely from their accounts.”

To someone who has experienced the U.S. workplace over those years, that finding isn't surprising. Since the creation of the 401(k), I worked for only about nine consecutive years in a company with an excellent 401(k) plan (i.e., one with ultra-low fees, a 50% employer match and a 10% discretionary employer contribution).

Saving for retirement wasn't even my primary concern for most of that time. There was a three-bedroom ranch to finance and children to educate. And I cheated a bit, briefly borrowing $1,100 from my plan to buy a used 16-foot sailboat, of all things. Had my wife not participated in a generous TIAA plan for 20 years, I'm not sure where we'd be.

My case turns out to be fairly typical. After looking closely into the subject, the authors of the study, Andrew Biggs of the American Enterprise Institute along with the Center's Alicia Munnell (its director) and Anqi Chen, found four reasons why 401(k)/IRA accumulations for individuals ages 55 to 64 are so inadequate.

According to their analysis of federal census data and the *Survey of Income and Program Participation* (SIPP) , the ideal $364,000 accumulation was reduced to $247,800 by the "immaturity" of the 401(k) system, to $136,200 by the fact that so many small and mid-sized employers had no plan to offer, to $122,800 by fees, and to $92,000 by pre-retirement withdrawals ("leakage").

On the bright side, that $92,000 balance is for individuals, not households. Many households have two earners, each potentially covered by a plan for at least part of his or her career. On the dark side, when the researchers removed people under 30 and people with defined benefit plans from the study, the ideal accumulation was only $270,000 and the total average individual accumulation at retirement in 401(k)s and IRAs was only $90,000. That's after the longest bull market that the known universe may ever see, when millions of Boomers are departing the labor force, the global economy is wheezing, and governments everywhere are crying poorhouse.

If the 401(k) system hasn't benefited Americans evenly, it's not alone in that shortcoming. You could similarly indict the public schools and the health care system, and for the same reason. The competition for jobs in profitable companies, which often come bundled with generous retirement plans, generous medical coverage and access to good school districts, is intense. By definition, many are left out.

Some people are eager to improve the retirement savings situation. In eight or 10 states, workers without employer-sponsored retirement plans are being offered state-sponsored

Roth IRAs. The 401(k) industry has been lobbying for legislation (the SECURE Act) that would allow small companies to join big, provider-sponsored 401(k) plans.

Personally, I believe that if every company put at least 10% of salary into a leak-proof, career-long, portable retirement plan, on top of a match, then all Americans would reach retirement in much better shape. But don’t hold your breath waiting for that.