What Will Happen to Poverty Rates Among Older Americans in the Future and Why?

Eric J. Toder

Poverty rates among the elderly have declined sharply over the past 50 years. Census data show that the fraction of Americans ages 65 and over with incomes below the poverty level declined from 35 percent in 1959 to just over 10 percent in 2002 (Bureau of the Census 2005). In contrast, the poverty rate for all Americans declined over the same period at a much slower rate, from 22 percent to 13 percent, making older Americans less likely than others to live in poverty. The expansion of the Social Security program has contributed significantly to lower poverty among older Americans; in 2002, Social Security benefits were 83 percent of income for Americans over age 65 in the bottom income quintile (Social Security Administration 2004). There is concern, however, that increasing earnings inequality among today's workers, higher divorce rates, the erosion of defined benefit pension plans, and a lower Social Security replacement rate could raise poverty rates among the elderly in the future.[1]

Projecting Changes in Poverty Rates between 1990 and 2020

Using a broader definition of income than the Census Bureau uses for measuring poverty (because it includes the potential spend-down from assets), we project that the poverty rate for the age 62 and older population group will decline from 7.8 percent in the early 1990s to 4.2 percent in 2020.[2] The main source of the decline in poverty is the growth in real earnings, as projected by the Social Security Administration's Office of the Chief Actuary. Because increases in initial Social Security benefits are linked to the growth in average wages,

annual Social Security benefits will increase over time in real terms, even though the increase in the normal retirement age will lower the percentage of earnings that benefits replace.

While poverty is projected to decline significantly, high poverty rates will persist among some groups. Groups that will remain at comparatively high risk of poverty include high school dropouts, blacks and Hispanics, never-married women and men, divorced women, and the oldest of the aged population.

Census thresholds for determining poverty are based on an absolute measure of a minimum standard of living at a point in time because they are indexed to the growth in the consumer price index. If poverty were defined in relation to prevailing living standards instead of an absolute level at a fixed point in time, then the thresholds for determining poverty-level income would be indexed to wages instead of prices. We define a wage-indexed poverty measure as a measure of *relative poverty*. The relative poverty rate measure shows how many people fall below an unchanging *percentage* of average real income, adjusted for family size, instead of an unchanging absolute real income level. The incidence of *relative* poverty, instead of decreasing, will increase from 7.8 percent of the 62 and older population in the early 1990s to 9.9 percent in 2020.

Why Relative Poverty Is Increasing

Changes in marital status and the normal retirement age (NRA) together contribute to about half the projected increase in relative poverty (table 1). If the distribution of marital status in 2020 were the same as in 1990, when fewer people were divorced, the relative poverty rate in 2020 would be about 0.5 percentage points lower than projected with the 2020 marital status distribution. The impact is greatest among divorced people (male and female) and younger retirees (ages 62 through 69). If the NRA of 65 had been retained, the relative poverty rate would be 0.6 percentage points lower in 2020 than with the current law NRA. The projected impact on poverty of raising the NRA is greatest among high school dropouts, members of minority groups, and never-married and divorced men.

The decline in lifetime earnings in relation to average economy-wide earnings for later baby boomer

TABLE 1. *Projected Absolute and Relative Poverty Rates in 2020, Population Age 62 and Older*

	Price-adjusted poverty rate (absolute)	Wage-adjusted poverty rate (relative)
Early 1990s (actual)	0.078	0.078
Projected 2020	0.042	0.099
Simulated 2020 poverty with		
1990 marital composition	0.037	0.094
Normal retirement age = 65	0.039	0.093
Constant average earnings across cohorts	0.042	0.099
Fixed earnings distribution across cohorts	0.043	0.099

Source: Author's calculations.

cohorts, however, is not associated with an increase in relative poverty because the decrease in male earnings was largely offset by an increase in female earnings. Similarly, restoring the more equal distribution of earnings for prewar cohorts compared with postwar cohorts, while holding average cohort earnings constant, does not increase projected poverty among postwar cohorts, in part because the progressive Social Security benefit formula makes postretirement income much more equally distributed than preretirement income.

Notes

This brief is from a longer paper by Barbara Butrica, Karen Smith, and Eric Toder (2002).

1. The Social Security normal retirement age (NRA) is scheduled to gradually increase from 65 to 67. Future retirees who take up Social Security benefits before the NRA will experience lower replacement rates than their predecessors.
2. The simulations used the Social Security Administration's Model of Income in the Near Term (MINT) to project poverty rates for the 62 and older population in 2020. The Urban Institute contributed to the development of MINT and is currently refining and updating it. The model version for this analysis (MINT3) projects the wealth and income of individuals born between 1926 and 1965 from the early 1990s through 2032 and couples through 2020 (Toder et al. 2002).

References

Bureau of the Census. 2005. "Historical Poverty Tables." http://www.census.gov/hhes/www/poverty/histpov/hstpov3.html.

Butrica, Barbara A., Karen Smith, and Eric Toder. 2002. "Projecting Poverty Rates in 2020 for the 62 and Older Population: What Changes Can We Expect and Why." Prepared for Boston College Center for Retirement Research. August.

Social Security Administration. 2004. *Income of the Aged Chartbook, 2002.* SSA Publication No. 13-11727. Washington, DC: Social Security Administration.

Toder, Eric J., Lawrence H. Thompson, Melissa Favreault, Richard W. Johnson, Kevin Perese, Caroline Ratcliffe, Karen E. Smith, Cori E. Uccello, Timothy Waidmann, Jillian Berk, Romina Woldemariam, Gary T. Burtless, Claudia Sahm, and Douglas A. Wolf. 2002. *Modeling Income in the Near Term: Revised Projections of Retirement Income Through 2020 for the 1931–1960 Birth Cohorts: Final Report.* Washington, DC: Urban Institute Research Report to the Social Security Administration.