

Demographic Change, Retirement Saving, and Financial Market Returns: Part 1

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Policy Abstract

This study analyzes trends and projections in retirement saving, focusing particularly on 401(k) plans. Understanding likely flows into and out of retirement plans is a first step in estimating how demographic changes will affect financial markets in the future. The analysis documents past trends and makes future projections about eligibility for 401(k) plans by cohort and year; participation rates by cohort and year; participation given eligibility; and contribution amounts. As illustration, the percentage of 40 year olds eligible for a 401(k) plan increased from 18 percent in 1984 to 34 percent in 1989 to 65 percent in 1999. Projecting forward, the average per person accumulation of 401(k) assets is projected to increase from about \$14,000 in 2000 to \$86,000 in 2020 and to \$273,000 in 2040. The dramatic increase is a result of increased eligibility, increased participation, the increasing portion of working lives during which contributions are being made to 401(k) plans, and the compounding of savings that takes place among those who will have started saving at younger ages. Aggregating together the individual cohort projections, total equity assets in 401(k) plans are projected to grow from about \$1.1 trillion in 2000 to about \$27 trillion in 2040. Initial consideration is also given to withdrawals from 401(k) plans, and how they are likely to differ from withdrawals from traditional pension funds. In continuing research, we will project the level of DB plan assets over the same time period, and then the level of assets in other retirement plans such as IRAs, Keoghs, and 403(b) plans. Those projections should enable us to evaluate the potential effects of demographic trends on rates of return in financial markets.