BY JOHN MULLIN

Wiser Policy for Seniors

The American population is aging rapidly. The share of people who are 65 or older grew from 12 percent in 2000 to 17 percent in 2020. It's forecast to grow to 22 percent by 2040, according to the U.S. Census Bureau.

In view of this trend, economists are attempting to improve their understanding of the economic decisions facing older people — decisions that are likely to become increasingly important for the U.S. economy as the population distribution skews older.

Richmond Fed economist John Bailey Jones has conducted extensive research on the economics of older households. He was introduced to the subject around the time he was finishing graduate school at the University of Wisconsin-Madison. "It really wasn't planned," Jones recalls. "I was invited to work on a project with a classmate, and I liked the technical challenges of the problem. It was an interesting puzzle."

Over time, his appreciation of the topic grew. "The behavior of older people is really important," he says. "I don't think it's been adequately studied, and there's a lot of new data that's becoming available that allows us to answer questions we may not have been able to ask or answer in the past."

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Jones' research in recent years has spanned three closely related areas: saving after retirement, medical costs in old age, and Social Security reform.

So-called "life-cycle" models of lifetime consumption typically predict that people will accumulate savings in their working years and spend much of those savings during retirement. Yet studies have shown that many couples continue to accumulate wealth after retirement. Three primary motives for this have been suggested: that retired couples save as a precaution against unanticipated medical expenses, that they save out of a desire to leave bequests to their heirs, or that they save out of a desire to remain in their own homes.

In a 2021 working paper, "Why Do Couples and Singles Save During Retirement," Jones and his co-authors assessed the relative importance of the various motivations. The answer, it turns out, depends on a household's wealth. "We find that, for couples and wealthier singles, the bequest motive dominates at the margin," Jones says. "But if you look at less affluent singles, it appears that medical expenses are more of a driver."

Even though enrollment in the Medicare program is nearly universal, the program has many coverage gaps. Consequently, medical expenses remain a major concern among older households — one that can shape their spending and saving decisions.

In a 2018 journal article, "The Lifetime Medical Spending of Retirees," Jones and his co-authors estimated the amount of medical spending remaining in the lives of households whose oldest member turned 70 years old in 1992. The researchers found that the figure was high and uncertain: On average, these households would incur $122,000 in medical expenses in their remaining lives. But the numbers were much higher for some families — the 5 percent of households with the largest medical bills would incur expenses above $300,000.

To Jones, one of the more striking findings of this research was that forward-looking lifetime medical expenses did not diminish quickly with age. "Let's say that, when I am 70 years old, my future medical expenses are expected to total $100,000," Jones says. "If I live until age 80, my future medical expenses are not expected to be much lower than that. A lot of this is because a nontrivial chunk of medical spending comes in the last few years of life."

Much of Jones' research has been devoted to understanding the effects of the U.S. Social Security system. In a 2020 working paper, "Social Security Reform with Heterogeneous Mortality," Jones and co-author Yue Li of the University at Albany examined, among other things, the implications of increasing the system's normal retirement age — the age of eligibility for full benefits, currently 67 for retirees born in 1960 or after. While this reform would lower costs by countering the trend toward a longer-lived population, the researchers showed that it exacerbates inequality by disproportionately cutting the benefits of lower-income people, who tend to have shorter lifespans. Using a life-cycle model, they found that societal welfare is maximized when Social Security benefits are independent of lifetime earnings and when early-retirement penalties are reduced.

Jones expects that variants of the life-cycle model will remain essential to answering the many policy design questions surrounding population aging. In a recent literature review, "Savings After Retirement," Jones and his co-authors argued that the life-cycle model has been one of the great successes in economics. He advocates for economists to continue improving the framework — for a better understanding of the behavior of older households and the policies that affect them. **EF**