Student Loans & Retirement Savings

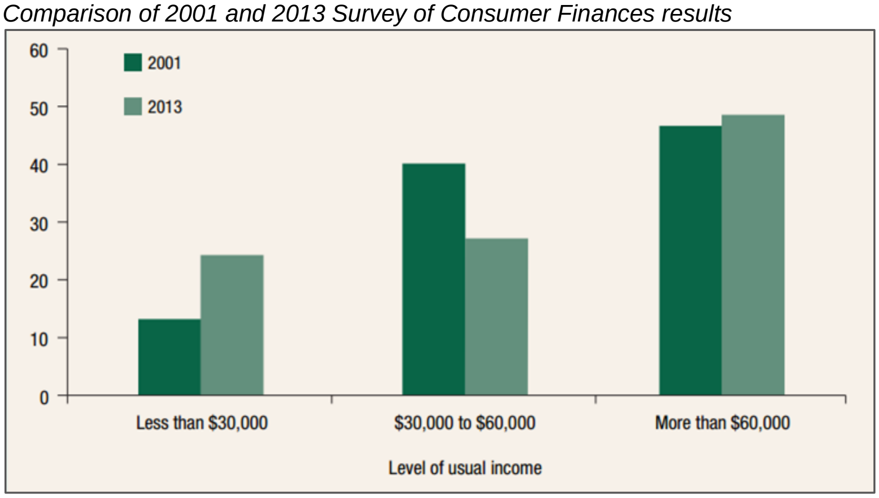
Can Education Debt Affect Overall Retirement Security?

Total student loan debt in the United States escalated to a grand total of $1.2 trillion in 2015, according to the Center for Retirement Research at Boston College. This amount has increased by *one trillion dollars* from $0.2 trillion in 2003. Does this statistic factor in to overall retirement savings?

Student loan debt accounts for more than 30% of total non-mortgage household debt in the United States, surpassing both vehicle loans and credit card debt.[1] For pre-retirees, this results in less money to save for retirement. According to the 2013 Survey of Consumer Finances[2], approximately 39% of young families[3] had education debt in 2013. Among these families, the average total student loan debt was $29,800. Comparatively, these figures were at 22.4% and $16,900, respectively, in 2001.

For young families with student loans, nearly 50% of this debt is held by households with typical annual income over $60,000. This figure increased only slightly from 2001, as shown in the chart below. However, young families with generally less than $30,000 in annual income hold approximately 25% of education debt, a dramatic increase from the less than 15% in 2001.[4]

Share of young families' education loan debt, by income group
Comparison of 2001 and 2013 Survey of Consumer Finances results



Source: Federal Reserve Bulletin. September 2014. Volume 100, Number 4.

[1] Munnell, Hou, & Webb. Will the Explosion of Student Debt Widen the Retirement Security Gap?. Center for Retirement Research at Boston College. February 2016, Number 16-2.
[2] The Survey of Consumer Finances is a triennial report produced by the U.S. Board of Governors of the Federal Reserve System
[3] "Young families" is defined by the Survey as "those with a head of household younger than age 40 at the time of the survey."
[4] Changes in U.S. Family Finances from 2010 to 2013: Evidence from the Survey of Consumer Finances. Board of Governors of the Federal Reserve System. Federal Reserve Bulletin. September 2014. Volume 100, Number 4.

Those Most Affected

The sector of young families with less than $30,000 in aggregate, annual income is likely comprised of Millennials who started their professional career during the Great Recession.

Many Millennials graduated but could not get jobs in their desired field, often leaving them to take a lower paying, part-time job. For those lucky enough to have a job offering an employer sponsored retirement plan, the burden of education debt, coupled with other pressing financial obligations, likely masks the need to save for retirement. Companies that sponsor a defined contribution plan, such as a 401(k), report high participation by Millennials, according to LIMRA[5]. However, the LIMRA Secure Retirement Institute found that, on average, Millennials with student loan debt defer a lower percentage to their retirement account, often lower than what is needed to maximize their employer match.[6]

Long Term Effect

Researchers at the LIMRA Secure Retirement Institute found that ***an average student loan of $30,000 - repaid over ten years - can result in $325,000 less in retirement savings***.[7] In a previous article, [Igniting the Spark: Motivating Millennials to Save for Retirement](), we discussed the long term opportunity cost of waiting just six years to begin saving for retirement. ***With forty years to grow, starting contributions just six years earlier can result in more than $150,000 in savings***.[8]

The effect of student loan debt on pre-retirees, especially the Millennial generation, is astounding, however, student loan debt is proving to be a burden for retirees and workers nearing retirement as well. For retirees, education loans accounted for 15% of non-mortgage debt in 2013, compared to less than 1% in 1989.[9] This is likely the result of an increasing trend where parents and grandparents take on student loans to assist children and grandchildren in paying increasingly higher education costs.

Taking on additional debt near retirement age can make it harder for retirees to replace their pre-retirement income. For those taking out loans during retirement for a child or grandchild's education, this additional debt can cause the retiree to alter their lifestyle or reenter the workforce to avoid running out of retirement income.

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[5] LIMRA is a research, learning, and development organization which provides financial institutions with insight and analysis on retirement, insurance, and distribution. LIMRA was previously known as the Life Insurance Marketing and Research Association; however the legal name for the organization was changed to LIMRA.

[6] LIMRA Secure Retirement Institute: $30,000 in student loan debt could mean $325,000 in lost retirement savings. 23 November 2015.

[7] Based on the assumption of a 22-year old beginning his/her career with $30,000 in student loan debt compared to a 22-year old beginning his/her career with no student loan debt.

[8] Assuming $2,000 contributions at the beginning of each year with 7% annual earnings

[9] LIMRA Secure Retirement Institute Study Finds Student Loan Debt a Growing Concern for Retirement Saving. 28 May 2015.

The Bottom Line

Pursuing a higher education is an investment that can lead to increased income and upward growth for those who achieve it. However, new graduates during the Great Recession entered the workforce to find historical unemployment rates while saddled with the burden of student loan debt. For those lucky enough to be employed and have an employer sponsored retirement plan, saving for retirement may seem like an unnecessary task while more student loans and other pressing financial responsibilities abound. Nevertheless, the cost of waiting to begin saving can be detrimental in the long run. The best advice for young professionals feeling the strain of student loans is to save what they can. Even small amounts saved early can grow into much larger amounts when given a long time period to compound. Deferral amounts should be increased with raises and when other debts are paid. Small sacrifices today can lead to a more financially secure retirement in years to come.