Middle Class Security Project

An Initiative of the AARP Public Policy Institute

Building Lifetime Middle-Class Security

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PREFACE

AARP hears daily from members across the nation who are struggling to maintain a toehold on the basics of middle-class security—a job, a modest pension, an affordable home, health insurance. In response to our members' concerns and to address the implications of economic stress for future retirement security, AARP's Public Policy Institute launched the *Middle Class Security Project*.

The prosperity of the middle class has been the basis for the American way of life for generations. Yet, for many, that prosperity is disappearing. This has prompted a focus on the "middle-class squeeze" in recent years and during the most recent presidential election campaign.

The *Middle Class Security Project*, an initiative of the AARP Public Policy Institute, analyzes the interplay of economic forces causing increasing distress among the middle class in America and recommends policy solutions. The project is based on a belief that all people should be able to realize a portion of the "American Dream" in their lifetimes and that each generation should be better off than those that came before. These core beliefs of our nation transcend politics and economics. A strong middle class is the moral bedrock of a functioning society. An ever-widening gap between the "haves" and the "have nots" leads to social instability, changes in the family structure, and difficulties for people trying to move up the socioeconomic ladder, achieve the American Dream, and live their best life. Failure to reverse the middle-class slide will have devastating effects both for today's older Americans and for the retirement security of future generations.

We must approach rebuilding the middle class holistically. Health care costs, jobs, savings and debts, income security, the cost of education, and the affordability of housing are all part of the total life experience of individuals and families. They are interrelated, and how we deal with one affects the others. Through careful research and analysis, the *Middle Class Security Project* provides that lens and offers an agenda for change.

A. Barry Rand
Chief Executive Officer, AARP

ACKNOWLEDGMENTS

At the request of CEO Barry Rand, the AARP Public Policy Institute (PPI) conducted a year-long, multi-disciplinary exploration of the well-being of America's middle class with a focus on prospects for financially secure retirement. The Middle Class Security Project offers insight, analysis, and an agenda for policymakers to consider. The project team included:

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AARP's Middle Class Security Project

www.aarp.org/security

The following reports were conducted or commissioned by AARP's Public Policy Institute as part of the Middle Class Security Project:

Building Lifetime Middle-Class Security

Donald L. Redfoot, *AARP Public Policy Institute*
Susan C. Reinhard, *SVP and Director, AARP Public Policy Institute*
Debra B. Whitman, *EVP for Policy, Strategy and International Affairs, AARP*

What Are the Retirement Prospects of Middle-Class Americans?

Barbara Butrica, *Urban Institute*
Mikki Waid, *AARP Public Policy Institute*

Assets and Debt across Generations: The Middle-Class Balance Sheet 1989–2010

Lori A. Trawinski, *AARP Public Policy Institute*

Tracking the Decline: Middle-Class Security in the 2000s

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Laura Sullivan, *IASP Research Associate, Brandeis University*
Donald L. Redfoot, *AARP Public Policy Institute*
Enid Kassner, *AARP Public Policy Institute*

The Elusive Middle in America—What Has Happened to Middle-Class Income?

Gary Koenig, *AARP Public Policy Institute*

In the Red: Older Americans and Credit Card Debt

Amy Traub, *Dēmos*

The Effects of Rising Health Care Costs on Middle-Class Economic Security

Harriet Komisar, *Georgetown University*

The Loss of Housing Affordability Threatens Financial Stability for Older Middle-Class Adults

Rodney Harrell, *AARP Public Policy Institute*
Shannon Guzman, *AARP Public Policy Institute*

How Older Americans Are Dealing with New Economic Realities

Tresa Undem, *Lake Research Partners*

***See also*:**

Video Portraits of Middle-Class Americans at www.aarp.org/security

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Table of Contents

MAJOR FINDINGS OF THE MIDDLE CLASS SECURITY PROJECT

The middle class today is smaller as well as older, more educated, more racially and ethnically diverse, and more likely to be single than middle-class households in the past. This project recognizes that most Americans identify themselves as middle class and that “middle class” is not synonymous with “middle income.” However, due to the broad availability of data on Americans’ income, project research utilized income as an indicator of membership in the middle class and analyzed economic trends affecting Americans in the middle income brackets.

Significantly, research shows that the percentage of adults considered middle income (67 percent to 200 percent of median income) has dropped about 10 percentage points since 1970, from about 61 percent to 51 percent.[1] More recently, from 2000 to 2011, median income fell about 8 percent and was lower in 2011 than it was in 1997.[2] Major findings emerging from the project reports include the following:

- If current economic trends continue, living standards in retirement will decline. Our studies show:
  - The percentage of working income that an average retiree can expect to have (the replacement rate) is projected to fall from 80 percent for current retirees to 73 percent for future retirees. The replacement rate will fall to 55 percent if health care costs continue to rise at current rates.[3]
  - Among working-age middle-income households, the proportion that was secure overall decreased by 38 percent from 2004 to 2010 and the proportion that was vulnerable increased by 42 percent. These changes represent a major shift in middle-class security over a relatively short time.[4]
  - The average debt of the middle class has increased sharply since 1989, and the rate of increase rises with age. Average net worth of families age 25–49 decreased 32 percent from 1989 to 2010.[5]
  - Housing cost burdens increased significantly over the past decade, hitting African American and Latino households the hardest.[6] The percentage of middle-class families age 50–64 that own their own home decreased 7.1 percent over the past two decades to 77.9 percent.[7]
- Rising health care costs pose a significant threat to middle-class security for working-age and older Americans.
  - Over the past decade, the share of household budgets consumed by health care expenses increased by 51 percent—nearly double the growth in household average income (30 percent) and more than three times the rate of spending growth for all other products and services.[8]
  - One in five people are in families that have problems paying medical bills. Many of these families experienced serious financial stress, such as problems paying for other necessities (such as food, clothing, and housing) or medically related bankruptcy.[9]

- Social Security will be the main source of income for all but the wealthiest future retirees.
  - Social Security will account for 51 percent of per capita household income for future middle-income retirees—69 percent for low-income workers and 35 percent among high-income workers.[10]
  - Nearly one in three (30 percent) of current middle-income workers are projected to slide into low-income status by the time they reach retirement. Social Security will represent 82 percent of retirement income for this group.[11]

What Does the AARP Middle-Class Security Project Address?

What is happening to middle-class security in America? Millions of Americans are emerging from the recent Great Recession with diminished retirement savings, mortgages that are underwater, escalating health care costs, and adult children who are having trouble finding employment or paying for a college education. As the economy improves, will these problems largely disappear? Or is the middle class in a decline that threatens our way of life?

> "When I was growing up middle class…it certainly wasn't a cakewalk for my parents. But they didn't have anywhere near the worries that people have now."
> —Focus Group Participant, Tampa

Most Americans say they feel squeezed by stagnating income and escalating costs. These economic trends have been documented in numerous think-tank reports and a growing array of books by academics and pundits across the ideological spectrum.[12] While observers differ about the root causes of middle-class decline, they share the concern that these trends are not a temporary economic situation stemming from the recent Great Recession. Research increasingly shows a progressive loss of middle-class economic security over the past 40 years that has affected people of all ages and threatens the prosperity of generations of Americans.[13]

The Middle Class Security Project seeks to put together the pieces of the puzzle facing policymakers as they address the issue of middle-class security. The project examines the major components of middle-class status, including income, assets, debt, housing, health care, and education. It includes eight research projects commissioned or conducted by the AARP Public Policy Institute team, drawing on other research to augment our findings.

To ground this work in the experience of Americans living through these difficult times, the project includes the stories of real people gathered from focus groups and presented in a series of video interviews. This report synthesizes the work of the project and offers policy recommendations for rebuilding the middle class.

Who is Middle Class?

In the United States, nearly everyone believes they are middle class.[14] Middle class self-identification varies little by income, race/ethnicity, or age. Four out of ten people with annual incomes below $20,000 identify themselves as simply “middle class,” as do one in three individuals with annual incomes above $150,000.[15]

These findings illustrate why objective measures, such as the level of income, education, profession, or homeownership, do not fully capture the experience of being middle class. A U.S. Department of Commerce report concludes that defining “middle class” involves a combination of values, expectations, and aspirations, in addition to income levels.[16]

For practical reasons, the project’s research reports generally used some measure of middle income as a practical way to identify families in the middle class. Although measuring income is relatively straightforward, defining the “middle” still raises an array of issues. Research analyses, including reports for this project, often differ substantially in how they identify middle income—depending on data sources used, sources of income included, adjustments for household size and composition, and parameters for measuring the middle. Koenig notes that researchers typically define the middle class using one of three household-based measures:[17].

1. The middle segment of the income distribution (e.g., 50 or 60 percent of households in the middle of the income distribution);
2. Income levels relative to median household income (e.g., 67 to 200 percent of median income); or
3. Income levels relative to the official poverty level (e.g., 200 to 500 percent of poverty level).

Reports in the Middle Class Security Project used variants of these measures to define “middle class,” in part due to characteristics of the data sources upon which they relied. The reports also differ with respect to how inclusive their measures of income are and whether or not they adjust for household size. Nevertheless, taken together, they reveal clear trends in the experience of being middle class in America today.

SIGNS OF RISING MIDDLE-CLASS STRESS

A growing number of people in national surveys express anxiety about maintaining middle-class status:

- Nearly two out of three individuals feel that maintaining a middle-class life in America is more difficult than it was five or six years ago.[18]
- Eighty-five percent say it is harder to maintain a middle-class lifestyle today than it was 10 years ago.[19]

> "I feel like I'm just one big crisis away from utter devastation."
> —Focus Group Participant, Milwaukee

- Four out of ten say they are "struggling to remain" in the middle class, with six out of ten concerned about maintaining their standard of living or worried about finances. These percentages were substantially higher among those with lower incomes, but signs of economic stress were substantial even among those reporting incomes over $100,000 per year.[20]

All of the research reports in AARP's Middle Class Security Project document this increased stress on middle-class families. A multidimensional Middle-Class Tracking Index, created for this project,[21] found that security had declined by 38 percent among middle-income households and vulnerability had increased by 42 percent between 2004 and 2010. The number of "income vulnerable" households (those below 250 percent of the poverty threshold) increased by 20 percent and the number of households below the poverty line increased by 28 percent. Declines were particularly severe among younger households, those with less than a college education, households of color, and households with children.[22]

Research for this project found that the net worth of younger workers (ages 25–49) decreased by a third (32 percent) between 1989 and 2010. For preretirees (ages 50–64), net worth increased only slightly during this period. But in both cases, increases in average debt offset increases in accumulated assets, an indicator of the stresses that middle income families are experiencing. Perhaps more troubling are the huge percentage increases in debts among retirees. Among recent retirees (ages 65–74) and older retirees (age 75 and older) debt levels increased at a faster rate than they did among households in their working years.[23]

Similar signs of stress were reflected in our project's finding that the average credit card debt of cardholders age 50 and older (who carried balances for three months or more) had average balances of $8,278, and now carry higher levels of credit card debt than younger people. Distressingly, a third (34 percent) of these credit card holders were using their credit cards to pay for basic living expenses such as rent or mortgage payments, groceries, utilities, or insurance because they did not have enough money in their checking or savings accounts.[24]

Most poignantly, stories of the struggle to maintain middle-class lifestyles were a constant theme that emerged from participants in focus group research conducted for AARP in Philadelphia, Tampa, and Milwaukee. After a lifetime of enjoying the rewards of a secure middle-class lifestyle, generally including such things as steady jobs, homeownership, and health insurance coverage, people shared stories of their lives disrupted by jobs lost, changes in health status, and erosion of pay and benefits. Many recounted efforts to cut back not only on extras such as entertainment or eating out, but also on basic necessities such as food and medical care. Some were underwater on their mortgages and at risk of losing the homes they had worked so hard to purchase. The devastation of losing middle-class security was dramatically illustrated by one woman who noted that her husband had suggested that they divorce. "He was going through a lot of emotional turmoil…and the reason why he wanted the divorce was because he felt he couldn't provide [for me]."[25]

These examples provide a brief window into the lives of those who have worked hard only to find their savings diminished, their home values sharply reduced, or their health care unaffordable—all because of market conditions or adverse life events over which they often had little control. These experiences have shaken the confidence of many families. Long after stock prices or home values recover or a family member regains employment, a sense of the fragility of middle-class security will linger. And for those whose situation does not recover, the effects can be devastating.

The Middle Class Security Project was designed to examine how multiple forces are combining to negatively impact middle-class families in ways that affect current and future generations. We have identified three major themes:

- The security of middle-class families is under attack from all sides—besieged by stagnating income; escalating debt; and rising costs for housing, education and health care.
- Middle-class security in retirement takes a lifetime to build.
- A threat to one generation undermines security for all.

The Security of Middle-Class Families Is under Attack from All Sides

Middle-class families are besieged by stagnating incomes, escalating debts, and rising costs for housing, education, and health care. The people we talked to as part of our focus group research described complex experiences of middle-class security (or insecurity) that often have more than one cause and result in many interacting effects. While researchers tend to focus on one or another aspect of middle-class security and public programs address specific needs, the various factors that contribute to middle-class security are not experienced as discrete silos in the lives of individuals and their families. Research and public policy should address the holistic needs of struggling middle-class families at critical junctures in their lives in order to contribute useful solutions that will sustain them through life's hurdles to a secure retirement.

> "Food prices have gone up, gas prices, expenses are going up every year but…I've gotten a letter from the U.S. government that 'you're not getting a cost-of-living increase in your benefits.'"
>
> —Focus Group Participant, Milwaukee

The U.S. Department of Commerce noted this multidimensional aspect of middle-class security in a report for the Vice President's Task Force on the Middle Class in 2010. As the authors observed, "Middle class families are defined by their aspirations more than their income. We assume that middle class families aspire to home ownership, a car, college education for their children, health and retirement security and occasional family vacations." The report also observed, "Most importantly, prices of three big expenditure items—housing, health care, and college—have gone up faster than incomes. These factors make attaining a middle class lifestyle harder today than it was two decades ago."[26] In the subsections below, we will look at four of these foundational dimensions of middle-class security—housing, health care, education, and retirement savings—and how the erosion of security in each interacts in the lives of individuals and families.

Housing

Homeownership is often referred to as the "American Dream," almost synonymous with achieving middle-class status. More than half of middle-class families owned their homes, and the primary residence was by far the largest asset at every age. Thus, the collapse of housing prices, the financial crisis, and the resulting Great Recession have had huge negative effects on the net worth of middle-class households.

> "I can hardly keep up with my [property] taxes right now."
> —Focus Group Participant, Philadelphia

Analysis for this project found that, among households age 25–49, average net home equity declined by 55 percent between 2007 and 2010, compared with declines of 32 percent for households 50–64, 22 percent among households 65–74, and 15 percent among households age 75 and older. Strikingly, homeownership rates declined by 7 percent among middle-class households age 50–64 between 1989 and 2010.[27]

The Middle Class Security Project revealed that housing cost burdens have increased for both middle-class homeowners and renters. Among middle-income households age 50 and older, the percentage who pay more than 30 percent of their incomes on housing costs, a level considered to be housing cost burdened, rose from 20 percent to 29 percent between 2000 and 2009.

The percentage of families age 50–64 with a mortgage increased by 13 percent between 1989 and 2010, and the median amount of mortgage debt for these families increased 159 percent.[28] Among middle-income households age 50 and older, homeowners with mortgages were the most cost-burdened household type. Nearly half (47 percent) of such households were cost burdened in 2009, compared with 5 percent of homeowners without mortgages and 35 percent of renters.[29] Similarly, the Middle-Class Tracking Index found a 22 percent decline in housing security (defined as spending less than 20 percent of income on housing) among middle-income working-age households, and an increase of 21 percent in housing vulnerability (spending more than 30 percent of income on housing) between 2004 and 2010. Housing security declined substantially among all age groups, education levels, racial and ethnic groups, and family types.[30]

Increased housing costs diminish resources available for other purposes and have led to increased residential segregation by class in recent years, which creates obstacles to accessing services essential to achieving middle-class status.[31] For example, being able to purchase a home with access to good schools is a critical way that young families enable their children to attain the education increasingly needed to ensure middle-class status. A recent study found that housing costs in districts with high performing schools were 2.4 times as expensive as in districts with low-performing schools, pricing many middle-class families out of access to this pathway to middle-class security.[32]

Health Care

The Middle-Class Security Project documented the various ways that costs related to health care are jeopardizing middle-class security—from mounting cost burdens of health care services, to the diminishing role of employers in providing health insurance, to the impact on wage and hiring decisions by employers.

Health care costs averaged $8,402 per person in 2010, nearly triple the level of two decades earlier. Health care costs rose at roughly twice the rates of inflation and of per-person gross domestic product growth between 2000 and 2010. During that decade, the share of family budgets that went to health care expenditures increased by 51 percent, far outpacing income growth and more than three times the rate of spending growth for other goods and services. Not only are one in five families struggling to pay medical bills, but the growing share of family budgets spent on health care also makes it difficult to pay for other basic necessities and to save for longer term needs like college education for children or for retirement.[33] Half of Americans age 50+ carry medical expenses on their credit cards; prescription drugs and dental expenses were the highest contributors to this debt in 2012.[34]

> "For the past seven months, I've had two *emergency room* hospitalizations because of [rapid heartbeat] and my cardiologist said, 'Look, this isn't about [your heart condition]; you are anxious.'"
> – Focus Group Participant, Philadelphia

Escalating health care costs affect decisions made by employers, which in turn affect the security of middle-class workers who get their health insurance coverage through their employers. Faced with health insurance costs that doubled between 2001 and 2011, from $7,601 to $15,073, employers have used three different strategies to contain their overall labor costs: (1) reducing the number of employees or sharply limiting wage growth, (2) eliminating health insurance coverage, and 3) shifting the costs and risks associated with health insurance coverage to their employees.[35]

Insurance coverage has declined most dramatically among small employers and employers with high percentages of lower-wage workers.[36] Focus group participants noted the tenuousness of insurance coverage when one spouse lost a job or retired and they had to rely on the working spouse for coverage. Many reported barely hanging on until they were eligible for Medicare at age 65.[37]

Other research from the Middle Class Security Project described the consequences for the future retirement security of current workers if health care costs continue to rise as projected by the Centers for Medicare & Medicaid Services. This research projected two starkly different futures, depending on whether health care cost increases can be controlled or not. If health care costs continue to rise as currently projected, modest projected income increases for future retirees will largely be eliminated, as will progress toward eliminating poverty in old age. Under such scenarios, out-of-pocket health care costs will double for future retirees as a share of income—and these projections do not include costs associated with long-term services and supports due to age-related disabilities.[38]

A 2012 report from AARP's Public Policy Institute documented the mounting costs of health care and long-term services and supports during retirement years. Even though nearly all retirees age 65 and older have Medicare coverage, the percentage of income spent out-of-pocket in 2007 ranged from 11 percent among Medicare beneficiaries age 65–69 to 28 percent among those age 85 and older.[39] Nearly half (46 percent) of persons die with virtually no financial assets, largely because the costs of health care and long-term services and supports exceeded savings.[40]

Education

Educational attainment is one of the strongest predictors of middle-class security. Data from the Census Bureau indicate that workers with a post-baccalaureate degree had median incomes of $62,313 in 2009, compared to $18,432 among those with less than a high school education.[41] College graduates can expect to make 84 percent more than high school graduates over the course of their careers, or $2.8 million over a lifetime.[42]

The Middle-Class Tracking Index showed that households with at least a college education experienced higher levels of security and more stability when compared with those with less education on the overall measure of security, as well as on all five of the individual factors that make up the index.

For example, more than half of households with a college education were "income secure" (i.e., had incomes at least 500 percent of poverty) throughout the period of the study from 2004 to 2010. At the other end of the spectrum, more than half of the households with a high school education or less were "income vulnerable" (i.e., had incomes below 250 percent of poverty) throughout this period, meaning that relatively few would have qualified as "middle class" as defined by this research. The group in between, households with some post-high school education but less than a college degree, saw the biggest declines in middle-class security. This middle group, which represented 22 percent of households in 2010, experienced a huge decline of 51 percent in overall security, while its overall vulnerability skyrocketed by 68 percent.[43]

Looking to the future, other analyses for AARP projected that when current workers reach age 70, college graduates will have a median per capita household income of $47,300, compared with $31,600 for high school graduates and $20,900 among households that failed to graduate from high school. College graduates are also more likely to maintain their preretirement lifestyles, since their retirement incomes replace a larger percentage of their working year incomes both before and after considering medical out-of-pocket costs.[44]

Retirement Savings—and Debt

With the costs of basic living expenses such as housing, health care, and education rising faster than wages, it is not surprising that the participants in our focus group research expressed increasing difficulties in finding anything left over to save for retirement. Add in the stresses due to job losses and health crises, and the ability to prioritize saving for the long term becomes even more difficult. As one participant noted, "I haven't been able to put into [my retirement account] for the last two or three years because of my reduction in [work hours]." Indeed, many of these preretirement participants who should have been at the peak of their earnings and savings years noted that they were forced to dip into savings just make ends meet.[45]

> "I've got six months' worth of savings [left]. I started with a year's worth, so I have been definitely living on my savings."
> – Focus Group Participant, Tampa

The experiences of these struggling middle-class individuals attest to disturbing trends in the ability to save for retirement and in the accumulation of debt. One project analysis found that "Increasing debt levels of younger people threaten their long-term financial security. As families incur higher levels of debt at younger ages, particularly education debt and mortgage debt, the ability of the family to save for future needs is delayed. If families cannot get out of debt during their working years, they will carry this burden into retirement and may not be able to fund their needs as they age. Data in this study indicate that more people are carrying mortgage debt than in the past, particularly at older ages, and the amount of that debt has also increased."[46]

Measures of the adequacy of retirement savings invariably show that high percentages of working families are not saving adequately for retirement.[47] One factor is a shift from employer-provided defined benefit pensions to defined contribution plans (such as 401(k) plans) where workers must take responsibility and risks for decisions related to how much to save, how to invest, and when to tap savings.[48] The percentage of workers covered exclusively by a defined benefit pension plummeted from 28 percent in 1979 to 3 percent in 2008; the percentage of workers with only defined contribution plans increased from 7 percent to 31 percent during that time, and the percentage with both types of retirement plans remained fairly constant with 10 percent in 1979 and 12 percent in 2008. As these data indicate, more than half of workers had no employment-based retirement plan at all.[49]

Social Security will continue to be the foundation of future retirement security for current middle-class workers, as these benefits are projected to represent half (51 percent) of their retirement incomes. One measure of the variability of outcomes for middle-class workers is an Urban Institute projection that nearly one-third (30 percent) of current middle-income workers will find themselves to be low income (lower third of incomes) in retirement—a risk that is even higher (36.5 percent) for older workers (45–54) due to the lasting effects of the recent recession. For these downwardly mobile middle-income workers, Social Security will be a critical bulwark of security; the Urban Institute projects that those benefits will represent 82 percent of their incomes.[50]

MIDDLE-CLASS SECURITY IN RETIREMENT TAKES A LIFETIME TO BUILD

Middle-class retirement security must be built over the course of a lifetime. Early adulthood (roughly ages 18 to 30) has become an increasingly unsettled time where young people are delaying entry into traditional middle-class adult roles, such as completing education, obtaining full-time employment and financial independence, moving out of the parents' home and buying a house, and marrying and starting a family.[51] Each of these life-course transitions have become impossible obstacles for increasing numbers of young adults, with long-range consequences for middle-class security extending to retirement security later in life.

With respect to employment, the Pew Research Center noted that "since 2010, the share of young adults ages 18 to 24 currently employed (54 percent) has been at its lowest since the government began collecting these data in 1948. And the gap in employment between the young and all working-age adults—roughly 15 percentage points—is the widest in recorded history." With respect to housing, young adults are not only delaying home purchases, they have become known as the "boomerang generation" —24 percent of 18- to 34-year-olds reported that they had moved back in with parents after living on their own.[52]

> "If [the next generation doesn't] save for retirement… they're going to be working all their life."
>
> —Focus Group Participant, Tampa

Though research cited above for the Middle Class Security Project confirms that obtaining a college degree may be the single most important step toward lifelong middle-class security, the rate of college graduation has not increased appreciably in the United States over the past several decades.[53] Many obstacles stand in the way of getting a college degree. Class segregation of housing can limit access in early years to good schools that open the pathway to a college education.[54] The yearly cost of college nearly doubled between 1995–96 and 2007–08, from an average of $12,400 to $22,400.[55] Those who manage to get a college education are increasingly emerging with substantial education debt, which nearly tripled from $363 billion in 2005 to $903 billion in 2012 and now exceed credit card debt in the United States.[56] Average education debt increased by 466 percent among households 25–49 between 1989 and 2010, and the percentage of households with education debt increased from 12 to 30 percent.[57]

Education debt can make it harder to qualify for loans to purchase a home and may be contributing to the fact that the share of 29- to 34-year-olds getting first-time mortgages was significantly lower during the past two years than it was ten years ago.[58] But increasing student debt is just part of a larger trend of mounting debts among households in the middle adult years. Between 1989 and 2010, total indebtedness increased by 89 percent among middle-class households age 25–49, from $46,410 to $87,644 (2010 dollars).[59] This distress among younger families is also mirrored in the Middle-Class Tracking Index, which found that overall security was lower among middle-class households age 25–44 than among preretirement households age 45–64 and declined more—dropping by 47 percent among younger households, compared with a 40 percent decline among the preretirees.[60]

The substantial decline in security among preretirees, even if it is somewhat lower than for younger households, is part of a troubling picture for middle-class workers about to enter retirement. The Middle-Class Tracking Index found that preretirees were most vulnerable on income—where the share of households with incomes under 250 percent of poverty increased from 16 to 27 percent—and the share who were housing cost-burdened increased from 28 to 34 percent.[61]

According to research for this project conducted by the Urban Institute, retirement security prospects are most grim for older workers (45–54 in 2012) because they have fewer years in which to recover from the recent Great Recession. This research projects a median per capita income of $29,500 (2011 dollars) for these middle-class households when they reach age 70—only marginally higher than the $28,800 among current retirees. It concludes that older workers will be less likely to maintain their working-age lifestyles, as their retirement incomes are projected to replace a smaller share of their preretirement income (70 percent) than current retirees (80 percent). Indeed, 37 percent of the middle-income workers age 45–54 are projected to be downwardly mobile to lower income status in retirement.[62]

Racial and Ethnic Minorities—A Lifetime of Obstacles to Middle-Class Security

For racial and ethnic minorities, building middle-class security across a lifetime can be like running an obstacle course: Many have comparative disadvantages that often start at birth and are reinforced at each stage of life. The Brookings Institution found that the gap in successfully achieving benchmarks on the pathway to middle class status widened between whites and minorities at each stage of life. At age 5, 68 percent of white children were ready for kindergarten, compared with 61 percent of Hispanic children and 56 percent of black children—but by age 40, 68 percent of whites had achieved middle-class security, while only 52 percent of Hispanics and 34 percent of blacks were similarly successful.[63] Racial and ethnic differences continue to be strong predictors of key dimensions of middle-class security, such as educational attainment—Asians (49.7 percent) and whites (31.1 percent) had much higher levels of college education than blacks (17.6 percent) and Hispanics (12.6 percent) in 2009.[64]

Research by AARP's Middle Class Security Project documents the difficulties that racial and ethnic minorities have encountered in achieving and maintaining middle-class security. The Middle-Class Tracking Index found that among households of all income levels, white households were nearly three times as likely to be secure overall as black households (38 percent to 13 percent) and more than twice as likely as Latino households (17 percent) to be secure in 2010. More than half of black (59 percent) and Latino (57 percent) households had incomes below 250 percent of poverty, meaning that relatively few had achieved middle-class income levels. The recent recession was particularly devastating to racial and ethnic minorities who had achieved a measure of middle-class security. Overall security dropped by 50 percent among middle-class black households between 2004 and 2010, compared with a 37 percent decline among whites and a 29 percent decline (from a much lower base) among Latinos.[65]

A Threat to One Generation Undermines Security for All

Building middle-class security is not a solitary enterprise; individuals cope with its challenges at each stage of life in the context of family relations that span generations. The risks and costs associated with middle-class status are experienced in terms of how they affect everyone in the family[66]—the escalating costs of a home in a good neighborhood affects access to good schools that put children on a track to success; escalating health insurance costs affect the ability to protect one's family when illness hits; the skyrocketing costs of college education impose debts not only on young people trying to make it into the middle class but increasingly on their parents and grandparents as well; and the necessity of two incomes affects the ability to provide family caregiving to young children and to aging parents.

"With my grandchildren, what I try to do is to buy them clothes so their parents don't have to."
– Focus Group Participant, Philadelphia

Family composition has a strong impact on middle-class security, as evidenced by the Middle-Class Tracking Index. Married couples without children, many of whom are undoubtedly empty nesters, were the only family type that saw an increase (more than 5 percent) in security between 2004 and 2010—58 percent of these households were secure overall in 2010. At the other extreme, only 9 percent of single-parent households were secure overall in 2010—more than two-thirds (68 percent) were vulnerable. In general, married households were more secure than singles, and each type was less secure if they had children.[67]

The increasing economic and social stresses of young adult years have broader ramifications for extended families—especially for their parents who experience increasing stress as they are preparing for their own retirement. For example, increased college costs are often borne by preretirement-age parents, as are increasing education debts. Nationally, student loan debt borne by borrowers age 50–59 tripled between 2005 and 2012 from $34 billion to $106 billion, and student loan debt among those 40–49 also nearly tripled from $54 billion to $154 billion.[68] Moreover, preretirement parents are opening their homes to "boomerang children" who are having trouble finding employment or affordable housing,[69] and increasing numbers are also serving as surrogate parents or caregivers to their grandchildren when their adult children need help with those responsibilities.[70]

Caregiving responsibilities also extend to spouses and parents who need long-term services and supports to deal with the disabilities that become more common with advanced age. The vast majority of these supports come from unpaid family caregivers. Family members are called upon to do tasks that are often physically arduous, emotionally draining, and technically complicated—generally with little professional support or training. The value of such support to the person receiving assistance in terms of their physical and emotional well-being cannot be quantified. But the value to society is enormous—research by AARP's Public Policy Institute estimates that the national economic value of the services provided by unpaid family caregivers was $450 billion in 2009.[71]

Despite the value of these supports, the costs are too often borne by unpaid family caregivers, typically women in their forties and fifties. Most caregivers are trying to hold down jobs and deal with other family responsibilities at the same time that they may be called on to deal with the care needs of aging parents at any time of the day or night.[72]

Research on working caregivers age 50 and older found that two-thirds had made some adjustments to their employment because of their caregiving responsibilities. Such adjustments include taking time off, taking a leave of absence, cutting back work hours, or turning down a promotion. One in ten caregivers quit a job or took early retirement, which can have major negative effects on economic security.[73] Family caregivers (age 50 and older) who leave the workforce to care for a parent lose, on average, nearly $304,000 in wages, Social Security, and pension benefits over their lifetimes.[74] In addition, reduced wages because of caregiving responsibilities can result in lower Social Security benefits, pension benefits, and savings in retirement accounts. Taking on the role of caregiver for aging parents in midlife may substantially increase the risk of living in poverty and receiving public assistance in old age, especially for women, who more often than not are the caregivers.[75]

Conclusions and Recommendations

Nearly all Americans consider themselves middle class, but many feel their middle-class security slipping away. This sense of loss is not just a feeling: Statistical analysis of economic trends reveals a shrinking and precarious middle class. The upwardly mobile, can-do attitude that has characterized our nation is now threatened by a complex set of circumstances that, if left unchecked, may result in a changed American landscape.

These frightening trends span across generations. Young people are struggling to pay for an education and establish themselves in the workforce; workers are scrambling to save for retirement, beset by rising health care costs, mounting debt, job losses, and difficulty paying their rent or mortgage. And a secure retirement is no longer a given. Many who were approaching retirement saw their savings and assets—financial and housing—decimated by the economic crisis of 2008. Some may have recovered from that loss, but many have not. Each generation is put in further jeopardy by coming to the aid of others in their families who are struggling to get by.

Focus group participants reported fighting to hold on until they could qualify for Social Security and Medicare—our nation's bedrock social programs that, historically, have helped to solidify middle-class security and serve as a lifeline for those whose circumstances are precarious. But current and future retirees now face increased financial risks with the shift toward defined contribution retirement plans and health plans that require greater out-of-pocket liability.

Our nation must take action to reverse these trends by developing public policy solutions in key areas and offering tools to help consumers plan for a financially secure future.

Policy Solutions

Health Care

Increasing Access to Affordable Health Insurance Coverage**—**At last count, nearly 41 million adult Americans did not have any health insurance coverage, and 29 million had inadequate coverage that required high out-of-pocket spending.[76] Improving access to affordable health insurance is essential to shoring up middle-class security. The Affordable Care Act (ACA) takes an important step in that direction by ensuring that everyone, regardless of their health status or age, will be able to get coverage. It also creates new marketplaces, called health insurance exchanges, where people who do not have health insurance through work will be able to shop for coverage. For those who qualify, financial assistance will be available to help with the cost of premiums. The ACA establishes standards for affordability and an essential benefit package to ensure that health care costs are not overly burdensome and that coverage is adequate. Health insurance exchanges are scheduled to begin operation in 2014, with enrollment to begin in 2013.

The following public-sector actions will help to ensure that families successfully access coverage through this new market-based system:

- Provide adequate consumer outreach and promotion efforts, as well as enrollment assistance, so that consumers are aware of their health insurance options and able to navigate the system;
- Preserve premium assistance to low- and moderate-income families so that affordability is not jeopardized;
- Provide adequate federal funding to support the start-up and oversight of exchanges; and
- Continue to review compliance with the new market rules to ensure that discrimination based on health status or age does not occur.

***Slowing the Growth in Health Care Costs*—**A major finding of this project is that health care costs have soared, and now consume a growing share of middle-class budgets, across age groups. Higher premiums, unpaid medical bills, and use of credit cards to pay for medical costs are alarming trends that must be reversed. If escalating health care costs are not brought under control, the economic security of both current and future retirees may be jeopardized. These problems run throughout the health care system and not just with public health insurance programs; focusing only on Medicare and Medicaid will not solve the problems.

***Improving Quality and Consistency in Health Care and Reducing Waste*—**We need to reexamine the incentives currently embedded in our health care system and transform delivery and payment mechanisms to reward high value health care. It is well documented that the United States spends more on health care than comparable Organization for Economic Cooperation and Development (OECD) countries, yet compared to them, it has below average life expectancy and higher infant mortality.[77] Health spending in the United States is elevated because the prices of drugs and certain health services are higher and payment structures encourage the use of more services. The use of new and expensive technologies without sufficient evidence that they improve health outcomes contributes to the problem. An archaic system of paper records and the inability of providers to communicate and coordinate care electronically also lead to inefficiencies. Some experts believe that as much as 30 percent of current spending does not contribute to better health, and manifests as unnecessary or inefficient services, excessive administrative costs, missed prevention opportunities, and fraud.[78]

The focus should be on the patient, with payments providing incentives for better care and patient outcomes. The ACA moves in that direction by testing innovative payment and delivery system initiatives in Medicare that promote greater accountability among providers. The law rewards providers for offering better care and provides financial incentives to encourage more team-based approaches to care, to improve care coordination, and to offer incentives to improved outcomes. More can be done; for example:

- Transform the payment system from fee-for-service to one that pays for a bundle of services or an episode or care. Other new payment approaches could encourage provider coordination and accountability, such as through accountable care organizations. One option for Medicare would be to expand and quickly bring to scale the payment and delivery system initiatives that were included in the ACA, if and when they are successful in promoting quality and prudent resource use.

- Ensure greater performance and price transparency in the overall marketplace. This has a twofold benefit: First, it gives consumers and other health care purchasers the information to make the best possible decisions, and second, it stimulates competition among health care suppliers and could potentially bring down prices or improve performance. In the context of Medicare, greater performance transparency could spur competition among providers and plans and could improve the efficiency of the program.
- Invest in administrative and data collection systems. It is imperative that we build the infrastructure to enable providers to communicate with each other electronically, as that will support higher value care and better decision making.
- Reduce medical errors while ensuring just compensation for injured patients in a transformed medical malpractice system to reduce defensive and unnecessary services.

Some of these changes would require the clinical community and consumers to assume new roles, and transformation may be slow in some areas. The need for change is imperative, however, and the rewards would accrue to all users, not just those who are middle class.

Making Prescription Drugs More Affordable— A recent Congressional Budget Office report[79] found that beneficiaries with access to prescription drugs reduce Medicare spending, due to better treatment adherence and health maintenance. Thus, in addition to reduced spending on drugs, making prescription drugs more affordable would help reduce spending on medical services. While some of the following options specifically address the cost of prescription drugs in the Medicare program, others will serve to make them more affordable across the board.

- Expand generic prescription drug use, as well as accelerate the availability of generic drugs. Prices for brand-name prescription drugs are highest in the United States compared to other OECD countries, whereas generic drug prices are one of the lowest.[80] Substituting generic drugs for brand-name drugs could potentially save billions of dollars for the U.S. health care system.[81]
- Reduce the exclusivity period for biologic drugs. Brand-name biologic manufacturers are currently granted 12 years of market exclusivity, which the Federal Trade Commission has concluded is excessive and may actually reduce innovation. Some have suggested the exclusivity period be shortened to five years.
- The Medicare program currently benefits neither from the rebates required for other public programs like Medicaid nor from the ability to negotiate prices upon which all private insurance programs rely. Reducing the cost of prescriptions under Part B and Part D will lower the federal deficit by lowering program costs. Requiring the same rebates for Medicare that currently are required for Medicaid could save more than $100 billion over 10 years.

Investing in Public Health—Transformation in our health care system should not be restricted to addressing illness and poor health. Steps can be taken to prevent or delay the onset of illness or disease by investing in and maintaining good population health. The gains from having a healthier population extend beyond the health care system. For example, a healthier workforce will be more productive. Investments in health and wellness programs, and in public education to encourage healthy behaviors, could improve overall population health and help consumers have an active role in decision making about their care. Federal and state governments should support proposals to require adequate and affordable mental health coverage, and mental health services should have parity with other health coverage in both public and private insurance programs. States should ensure adequate funding for mental health services and develop comprehensive and coordinated delivery systems.

Addressing the Costs of Long-Term Care—The costs of long-term care are unaffordable for middle-income Americans. Without a national program to provide affordable access to these services, our nation's primary solution is to rely on family caregivers, many of whom endanger their future economic security by dropping out of the workforce or reducing their work hours to provide care. When families cannot shoulder this responsibility, many people with long-term care needs must spend their life savings, ultimately turning to Medicaid as a last resort. Policies to help family caregivers include—

- Offering tax incentives to defray some of the costs of caregiving;
- Allowing Social Security credits for family caregivers;
- Promoting workplace practices that provide more flexibility to workers in their schedules and use of leave;
- Expanding the categories of workers covered by the Family and Medical Leave Act to allow more workers to take unpaid leave for caregiving;
- Protecting caregivers from workplace discrimination; and
- Assessing caregivers' needs and addressing them through public and private sector programs.

Policies to improve the availability in Medicaid of services in home and community settings would improve the quality of life for many people who need long-term care, as well as reduce public expenditures by relying less on more costly nursing home services. But a more adequate national solution to helping middle-class families pay for long-term services and supports could yield benefits to economic security, health, and well-being for the millions of people who need these services and for their families.

Retirement Income

Social Security has been a public policy success, providing a floor of economic stability for retired workers, workers who become disabled, spouses, and dependent children for decades. But Social Security was never intended to be the sole source of retirement income. The other two components—savings and pensions—should work hand-in-glove with Social Security to provide a secure retirement. Yet the traditional employer-provided pension has eroded and retirement savings have not increased enough to fill the gap.

As a result of these trends, a growing number of retirees depend on Social Security for the largest portion of their income. Almost one in four Americans age 65 or older relies on Social Security for nearly all of their family income today.[82] And among all older adults, half have an annual individual income of less than $20,000.[83] Economic security in retirement must be addressed holistically through strengthening Social Security, increasing retirement savings, and fostering opportunities for older Americans to work longer.

Social Security—Social Security is the foundation for a secure retirement among middle-class retirees. In fact, for most retirees, it is the only source of retirement income that is protected from inflation and guaranteed to last a lifetime. And while the program faces long-term challenges that must be addressed, any change to achieve solvency must take into account changing demographics and the important role that Social Security plays in retirement income. Solvency is, in and of itself, not sufficient. The focus must be on economic security in retirement.

Policymakers should also recognize that Social Security benefits are already being reduced on a schedule set by Congress in 1983. The age at which a retiree can get full benefits was 65; it currently is 66 and is gradually increasing to 67, for persons born in 1960 or later. An increase in the "full retirement age" is an across-the-board cut in retirement benefits for future retirees. Several principles should guide any reform to Social Security:

- Social Security must continue to protect workers and their families in the case of lost wages due to retirement, disability, or death.
- Benefits must continue to be progressive, guaranteed for life, and protected from inflation.
- Social Security must continue to provide the foundation for a secure middle-class retirement and should be improved for those most vulnerable.

Retirement Savings—As workers struggle to maintain a middle-class lifestyle, it has become increasingly difficult for them to save toward their retirement. Yet such saving must be encouraged, especially as defined benefit pension plans have become scarce. Possible strategies include—

- Develop and implement a targeted public educational campaign to increase public awareness of the importance and benefits of saving;
- Expand the percentage of workers with access to a payroll deduction savings plan at work;
- Encourage employers to adopt retirement savings plan design features, such as automatic enrollment and automatic increases in contribution rates, that maximize employee participation and contributions;
- Increase the incentives for middle-class families to save in a retirement account;
- Discourage early withdrawal of retirement savings assets; and
- Promote opportunities for workers to take distributions in the form of lifetime income streams.

Encouraging Work—It generally takes two incomes today for a family to achieve and maintain a middle-class life style, leaving many struggling to juggle family and work responsibilities. Government policies to ensure that workers' pay and other benefits are sufficient to cover essential living expenses—a living wage—would go a long way toward strengthening the middle class. Greater investment in quality, affordable day care would enhance the employment options of women. And public sector job creation programs could help workers retain employment during economic downturns.

Workers who lose their jobs not only see their wages disappear; they often must tap savings and retirement accounts, seek loans, and use credit cards to make ends meet. These strategies can be disastrous if savings are exhausted and loans and credit card debt cannot be repaid. The unemployed risk losing their homes, their hopes for a financially secure retirement, and a middle-class way of life.

In a rapidly changing global economy, workers are likely to require frequent skills updating throughout their working lives in order to remain competitive. Without the skills employers seek, they risk job loss, long-term (and for some, permanent) unemployment, and reemployment at lower wages with fewer benefits and little job security. These trends argue for greater investments in education. Other actions that could encourage work include the following:

Workplace Flexibility—More flexible work options such as alternative work schedules, flextime, telecommuting, and job-sharing, along with paid leave and prorated benefits and compensation, would make it easier for parents and others with caregiving responsibilities to remain employed. Public and private employers should provide more flexible work options and not be allowed to penalize employees who must take time from work for caregiving and other family issues.

Work Sharing—A policy that can ease the pain of unemployment for some workers is called short-time compensation (STC), also known as work sharing. An alternative to layoffs, STC programs enable employers to reduce work hours and spread the remaining work among employees who might otherwise be terminated. Short-time workers receive prorated wages and partial unemployment compensation insurance.

Training and Retraining—There are many options to strengthen the country's workforce development system to help workers remain employed and employable with middle-class incomes, including—

- Development of training and retraining programs, including more apprenticeship programs, that provide workers with skills leading to jobs in high-growth industries and high-quality occupations that pay well, provide employee benefits, and enable workers to continue to develop new skills while employed;
- Adequate funding of training and retraining programs and financial aid (along the lines of Pell Grants) to workers and jobs seekers without the resources to pay for training;
- Appropriate performance measures for judging the success of job training programs; and
- Greater financial support for college costs to reduce the burden of student loans.

Consumer Issues

In an increasingly complex world, the need for financial capability is more important than ever. But too few middle-class Americans have the knowledge and tools they need to evaluate mortgage and other debt products, investment options, or retirement planning tools. Understanding how to manage one's resources in the present, plan for the future, and minimize or avoid debt can make the difference between a secure future and a perilous slide out of the middle class.

As families bear more responsibility for planning and financing their own retirement, knowledge about saving, investing, asset allocation, and risk and the ability to make decisions in their own best interest become vital. Understanding financial concepts and how to implement financial strategies is becoming more important for families of all ages. Comprehensive financial planning can help families examine their long- and short-term financial goals, assets, investments, retirement savings, debt, and insurance coverage—life, health, disability, and long-term care. This type of planning can help people protect against unexpected events that can threaten financial security: job loss, health crises, or death of a spouse. Financial planners can help clients develop asset allocation strategies that are appropriate for their age and risk tolerance, and suggest ways to improve the strength of their balance sheet. Unfortunately, access to this type of financial advice is often limited to wealthier families.

Escalating costs for higher education have led to a surge in education loan debt over the past two decades. This debt is burdening not only the younger generation, but their parents and, in some cases, their grandparents as well. Families need to know the costs and understand the long-term burden of having to repay large amounts of student loan debt.

The following policies would help middle-class Americans:

Comprehensive Financial Planning—The government, as well as private and nonprofit sectors, should develop strategies to deliver comprehensive financial planning advice to people of all income levels. Online tools and employer-sponsored programs should be considered.

Debt Management—Increasing debt by families of all ages is a growing challenge. Policies and regulations that enhance borrower understanding and protect consumers from predatory products should be developed for all types of debt. In addition, better tools to assist consumers with managing their debt burden are needed.

Education Costs and Funding—Tools such as student loan calculators should take into account the age of the borrower. Older people who take on this form of debt may face special concerns. Federal student loan debt can be garnished from Social Security payments if it has not been repaid. Additionally, outstanding defaulted federal student loan debt will disqualify an older borrower from obtaining a federally insured reverse mortgage unless the debt is repaid.

Housing Counseling—Programs that educate people about the home-buying process, mortgage finance options, debt burden, and homeowner obligations should be encouraged for all first-time homebuyers. Consumers should understand how mortgages work and know who to contact if they are having financial difficulty. Such information can help prevent future foreclosures by providing more rapid assistance to borrowers who are having difficulty meeting their loan obligations.

Consumer Protections for Older Americans—Consumers need a fair financial marketplace as they borrow, save, and invest. The risks and benefits of financial products should be clearly explained in a form that consumers can reasonably be expected to read and understand. Federal and state governments should create a legislative and regulatory framework for consumer financial products that establishes a fair, transparent, and competitive marketplace so consumers can build financial security for their lifetime.

Elder Financial Exploitation Prevention—Older Americans are more vulnerable to financial exploitation and abuse than the younger population. They often are targeted by scammers because they are more trusting and have accumulated assets over a lifetime. Government at all levels—federal, state, and local—should focus on preventing, detecting, and prosecuting elder financial abuse.

Conclusion

Middle-class security in retirement takes a lifetime to build, but it can disappear in an instant. High medical or long-term care costs, a drop in home values, an unanticipated loss of assets, mounting debts—often due to helping parents, children, or grandchildren—an unexpected job loss, or falling victim to an unscrupulous marketer all can derail one from a secure and comfortable middle-class retirement. When a family's economic fortunes begin to falter, it can send ripple effects across the generations. A core belief of our society has been that each generation should do better than those that went before. If we want this security and upward mobility to be part of our nation's future, we must all take action together: policymakers, businesses, and Americans of all ages.

ENDNOTES

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