



Retirement in a High-Inflation Era and the Impact on Social Security

While the US inflation rate has dropped significantly from its near 9% peak in June 2022, it continues to remain stubbornly above the Federal Reserve's 2% annual target. According to the latest July CPI report, the overall inflation rate currently stands at 2.7%, with core inflation (excluding food and energy) rising at a 3.1% rate. This indicates a slight acceleration from previous months—a concern that's compounded by continued uncertainty surrounding the long-term inflationary impact of higher tariffs.¹

What does this persistent impact of inflation have to do with Social Security? The answer is "a lot!" when you consider the important role that Social Security plays in protecting Americans' retirement security. Investors tend to underestimate the long-term value of Social Security when planning for retirement income. However, considering that the current maximum monthly benefit at full retirement age is \$4,018, over a 25-year retirement that translates into an impressive \$1.2 million of income (adjusted for inflation).

This importance is further elevated when you consider how few workers these days can rely on a pension for additional predictable retirement income. Just two generations ago, the vast majority of American retirees (84%) were covered by some sort of employer pension plan. That number has now dropped to just 15% for non-government workers.

Understanding the Impact of Inflation on Fixed Income Retired Households

Inflation can significantly reduce purchasing power in retirement, making it harder to cover essential expenses like food, housing, and healthcare. Fixed income retired households face particular challenges as inflation acts as a silent tax on their financial security, systematically eroding the value of their savings and benefits over time.

While some benefits like Social Security include annual cost-of-living adjustments (COLAs) to offset inflation, other fixed income sources such as pensions and some annuities often do not. This can result in meaningful erosion of purchasing power which, over time, may force retirees to withdraw more from savings to maintain their current lifestyle—potentially shortening the lifespan of their retirement savings.

For example, for every \$1,000,000 in savings, if inflation averages 3% per year, the purchasing power of that \$1,000,000 will be reduced to about \$742,000 after 10 years, assuming no investment growth. This means you would need approximately \$1,344,000 after 10 years to maintain the same level of purchasing power as \$1,000,000 today.

Keep in mind that some key costs in retirement, such as healthcare expenses, have historically risen much faster than the overall inflation rate—further stressing income needs for retirees and creating additional challenges for those on fixed incomes.

The 2025 Social Security COLA Increase and Benefits Adjustments

Each year, the Social Security Administration makes a cost-of-living adjustment to help offset inflation. The 2025 social security COLA increase for Social Security benefits increased by 2.5%. To calculate each year's adjustment, the government compares the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) from the third quarter of the previous year to the third quarter of the current year. That percentage increase then becomes the COLA applied to Social Security benefits for the following year.

Social Security benefits in 2025 will reflect this 2.5% adjustment, with COLA adjustments typically announced each October and beginning with the December benefit payment (which is paid out in January). While COLAs are an invaluable tool that helps benefit recipients maintain their purchasing power, the adjustment methodology faces ongoing scrutiny for potentially understating the inflation experienced by retirees.

The CPI-W reflects spending patterns of working-age individuals, which may not accurately capture the expense categories that dominate retirees' budgets. Healthcare costs, for instance, represent a larger portion of retirees' spending than the general population, yet may be underweighted in the COLA calculation.

High-income earners should carefully consider the overall impact of these benefit increases. Combined with other retirement income, the added benefit income could possibly push individuals into a higher tax bracket or result in a higher percentage of their benefits becoming taxable.

Social Security Reform & Its Effects on Retirement Income Planning

The Social Security fund's solvency has been a looming concern for many years, and the impact of recent inflation has served to accelerate that concern. Social Security reform discussions have intensified as policymakers grapple with the program's funding challenges amid inflationary pressures.

According to recent analysis, if Congress acted today to restore Social Security's long-term solvency, they would need to either cut benefits by 22% for current and future beneficiaries, or increase the payroll tax to 16% (up from the current 12%), or implement some lesser combination of the two. The closer the fund moves towards insolvency, the more dramatic these potential changes become.

By 2035, the Social Security trustees project, the number of eligible Americans 65 and older will rise by nearly 20% while the total population will increase by only about 5%. This demographic shift creates additional pressure on the system's sustainability.

Whether through a mix of benefit cuts and higher payroll taxes, or the removal of the taxable earnings cap for Social Security (currently \$176,100), Congress will need to take action soon as both inflation and an aging population base continue to exert unsustainable pressures on the system. Potential reform approaches include:

- Raising or eliminating the payroll tax cap

- Adjusting the full retirement age
- Modifying benefit calculation formulas
- Changing the COLA calculation method

These potential changes create significant retirement income risks from Social Security legislative uncertainty that must be factored into comprehensive retirement planning.

We saw similar inflation-driven reforms when Congress passed the SECURE 2.0 Act in 2022, which introduced several policy reforms for 401(k) and IRA retirement plans—changes that primarily focused on increasing contribution limits and adjusting rules to help savers and retirees counteract the loss of purchasing power.

Navigating Retirement Income Risks in a High-Inflation Era

Social Security funding crisis and implications for high-income households extend beyond direct benefit impacts to include broader economic effects that influence overall retirement security. The intersection of inflation pressures and funding challenges creates a complex planning environment requiring adaptive strategies to maintain purchasing power throughout retirement.

Understanding how Social Security reforms could alter high earner retirement planning becomes crucial as many proposed reforms specifically target higher earners through various mechanisms. High-income households may face particular exposure to legislative changes, making flexible retirement planning strategies essential.

The outlook for Social Security's solvency in an inflationary economy presents unique challenges. Higher inflation increases benefit payments through COLA adjustments while potentially affecting the wage growth that funds the program through payroll taxes. This dynamic could influence the timeline for trust fund depletion and the urgency of reform measures.

Depending on individual health and circumstances, delaying Social Security claiming can be a valuable strategy. Assuming full retirement age is 67, waiting until age 70 to start benefits could increase monthly payments by 24%—providing a guaranteed increase that often exceeds inflation rates and helps maintain purchasing power over time.

Adapting to Social Security Policy Change in 2025

By its nature, inflation undermines retirement security, reducing the purchasing power of savings as the same amount of money buys fewer goods and services over time. Social Security policy impact on high-income earners may be particularly pronounced as reform efforts often focus on this demographic.

Social Security benefits receive annual COLA adjustments, but these may not always keep pace with rapid price increases. The result is an ever-shifting confluence of factors that require thoughtful and responsive retirement income planning strategies to ensure savings and income sources maintain their value going forward.

As economic conditions continue to evolve, the importance of professional guidance in navigating these complex interactions becomes increasingly important. Comprehensive retirement planning must account for the dynamic relationship between inflation, Social Security policy changes, and overall retirement security.

Now is a good time to check in with your BLBB financial advisor to share new events in your life that may require adjustments to your financial plan.

¹ Unless otherwise noted, information throughout this article comes from <https://www.ssa.gov/>

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