Helping Savers Stay Focused on Retirement

Financial wellness can help with prioritizing competing financial goals.

August 2021

KEY INSIGHTS

- Savers today struggle with making the connection between their current financial choices and secure retirements.
- Confidence about retirement declines as retirement approaches.
- Reinforcing the value of positive financial actions taken today will improve confidence and retirement outcomes.

Joshua Dietch
Vice President, Retirement Thought Leadership

Connections between the ability to adequately save for retirement and overall financial wellness are well documented. The Employee Benefit Research Institute (EBRI) estimates that, collectively, Americans face an almost $4 trillion retirement savings shortfall.[1] The retirement savings shortfall is not an isolated phenomenon; rather, it is an effect that is related to a broader and growing level of financial fragility, defined as the inability to come up with $2,000 within 30 days to meet an unexpected expense.[2]

The confluence of these two trends has consequences to those affected as well as employers who sponsor retirement plans and the financial professionals they look to for counsel to manage those plans. One cannot erase the retirement savings shortfall without simultaneously improving the financial resiliency and well-being of those who benefit from saving in defined contribution plans such as 401(k)s.

If these are the symptoms of an illness, then what is the antidote? As part of our ongoing research into the retirement savings and spending habits of Americans who save for retirement in 401(k)s, we decided to examine financial wellness. The basis of our analysis draws upon our 6th annual Retirement Savings and Spending Study,[3] a survey of 401(k) participants fielded in June 2020 during the coronavirus pandemic. Though the pandemic undoubtedly influences the findings, the data provides valuable insight on longer-term trends.

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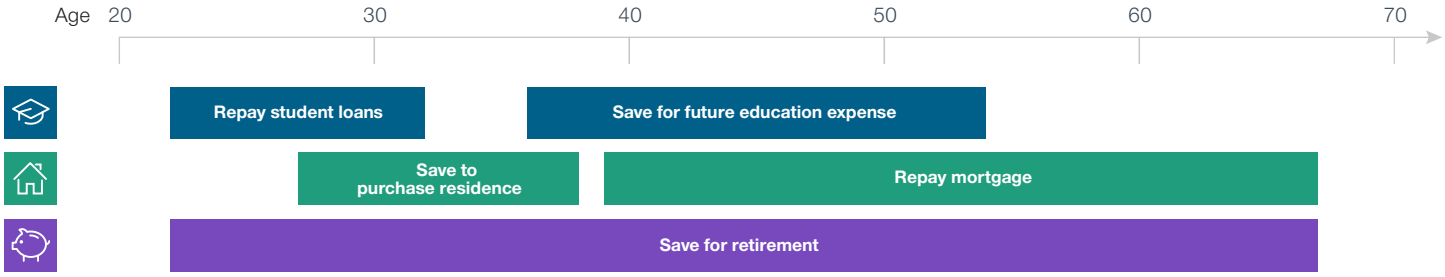
[1] VanDerhei, Jack, Ph.D., "Retirement Savings Shortfalls: Evidence From EBRI's 2019 Retirement Security Projection Model®," ebri.org. Issue Brief, March 7, 2019, No. 475, p. 11.
[2] Schneider, Daniel; Tufano, Peter; Lusardi, Annamaria, "Household Financial Fragility during COVID-19: Rising Inequality and Unemployment Insurance Benefit Reductions," December 21, 2020, p. 3.
[3] The Retirement Savings and Spending Study was conducted online June 5–24, 2020; 3,420 participants who are currently contributing to a 401(k) plan or eligible to contribute and have a balance of at least $1,000 responded. The survey also included 1,007 retirees who have retired with a Rollover IRA or left-in-plan balance.

Hypothetical Life Stage Financial Goals of Workers

(Fig. 1) Priorities that compete with retirement for today's dollars.



Source: T. Rowe Price.
Hypothetical timeline of debt repayment and savings goals.

Financial Wellness and Life Stages

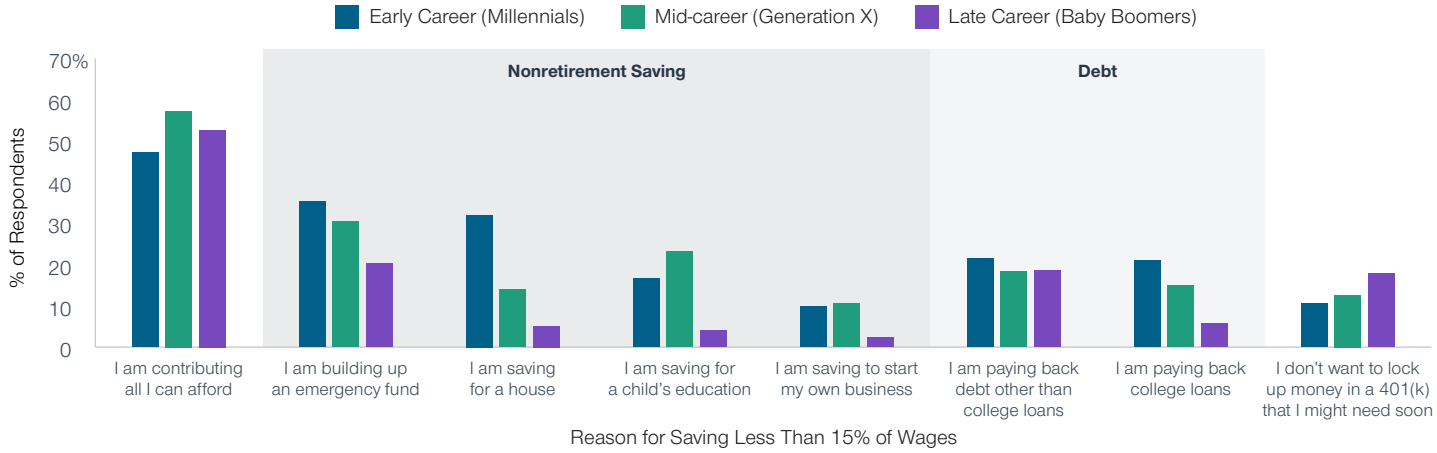
Saving for retirement is often viewed as a slow and steady process. The hope is that over decades someone has saved "enough" to feel financially secure in retirement. But saving for retirement is not the only financial goal workers have. Many workers, like the 401(k) participants surveyed in our study, also have common financial goals and milestones, like repaying student loans, starting a family, purchasing a home, or saving for a child's education.

When these financial goals occur also matters. Specifically, if progress toward these goals is delayed, many lack the financial resources to bear multiple heavy financial burdens at once. Not surprisingly, many struggle to balance short-term and long-term financial goals and obligations. If retirement is far off in the future and there are bills due today, the competing priorities of today will almost always win.

This concern is not abstract; 29% of the participants we surveyed admitted they are not saving enough for retirement. Of those, slightly more than half shared that they were saving all they could afford (Fig. 2). Other competing savings needs and debt are also significant barriers to saving more for retirement, but the significance of these barriers often changes over the course of one's

What Gets in the Way of Saving for Retirement

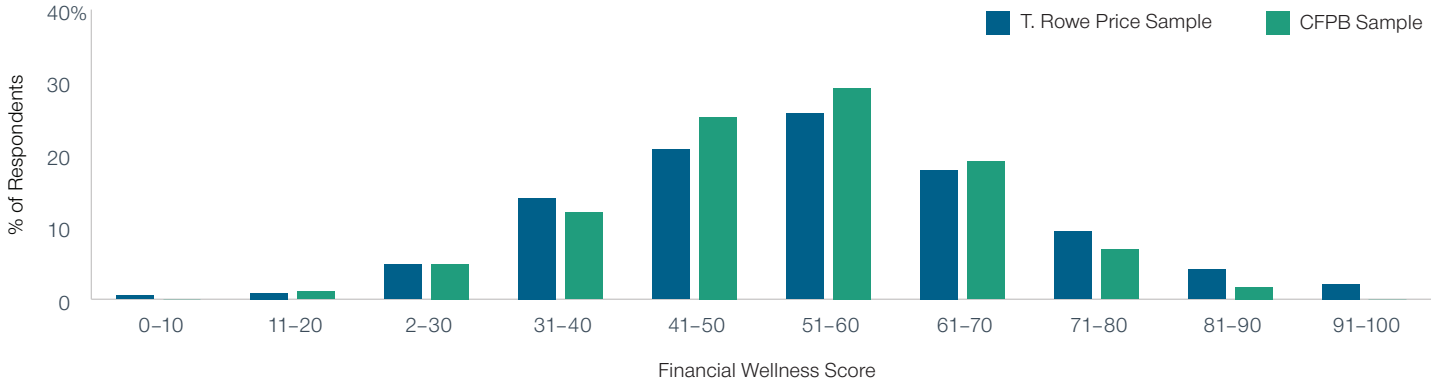
(Fig. 2) Debt and other goals vary during life stages.



Respondents could choose more than 1 reason for saving less than 15%.
Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

Workers' Financial Wellness Follows a Normal Distribution

(Fig. 3) Comparison of T. Rowe Price's financial wellness framework and Consumer Financial Protection Bureau's Well-Being Scale.



Sources: T. Rowe Price 2020 Retirement Savings and Spending Study (RSS) and Consumer Financial Protection Bureau (CFPB).

lifetime. Accordingly, meeting savers where they are with timely financial wellness programs can help savers address these challenges.

How Can We Quantify and Measure Financial Wellness?

Ideally, saving for retirement is a persistent activity throughout one's working years. Moreover, the financial actions we take today, coupled with the financial goals we set for ourselves and progress made toward them, will affect the outcomes we experience in retirement. Connecting the present to the future, in our view, forms the basic framework of financial wellness. After all, form follows function. Naturally, we were curious to learn how the workers we surveyed in our study perceived their own financial wellness and what correlated with it.

Using our framework, we developed a 0-100 measurement scale to assess the financial wellness of our survey population of workers saving for retirement in their employer's 401(k) plan. Ours is not the only measure of financial wellness. Perhaps the most well known of these financial wellness measures is the Consumer Financial Protection Bureau's (CFPB) Well-Being Scale. It is a 10-question survey, using a similar 0–100 scoring that asks respondents to reflect on their financial situation and finances. It does not, however, explicitly reference retirement and is primarily oriented to the respondent's present condition, which we sought to remedy with the creation of our financial wellness framework.

We found a similar distribution of results when we compared our framework with the CFPB's Well-Being Scale (Fig. 3). This confirmed the usefulness of capturing current behaviors and progress toward specific financial goals and how those actions translate into how someone sees their future self in retirement.

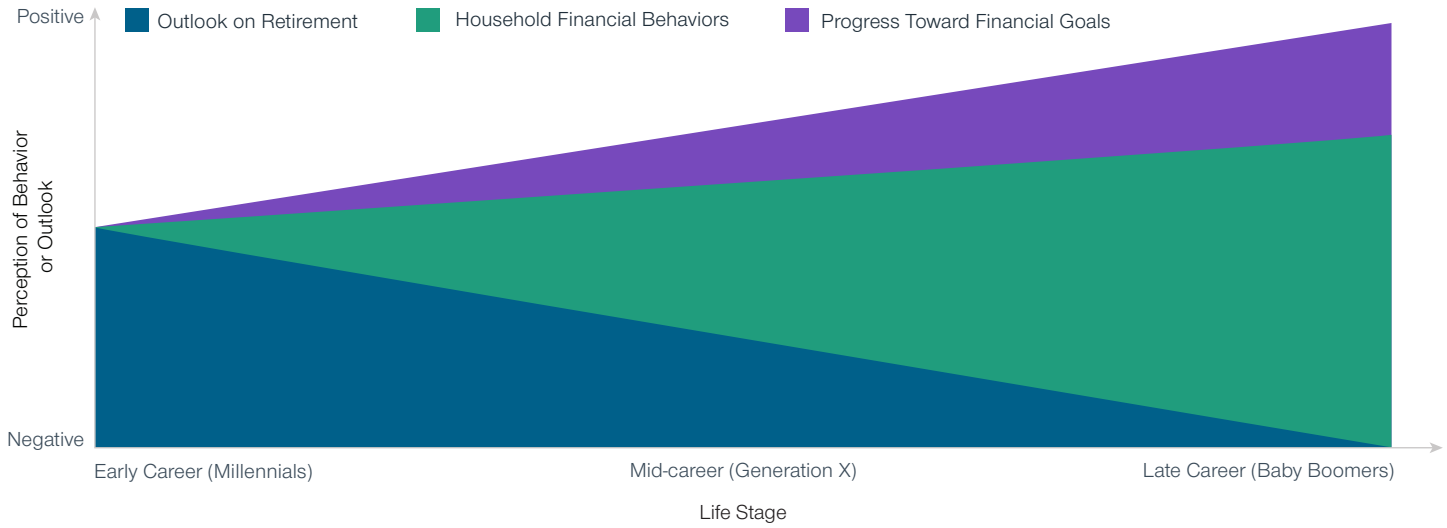
Financial Wellness in Context

Our data suggests that many savers not only struggle with achieving financial wellness today, but they may also more fundamentally struggle with connecting the dots between the actions they take today and how those actions will affect their retirement outcomes in the future.

In our study, we found that financial capability is consistently better among older respondents, reflecting generally higher incomes but also suggesting a learning trend and improving financial skills over time. However, despite greater

While Financial Capability Increases With Age, Confidence About One's Retirement Declines

(Fig. 4) Older workers have a dimmer outlook on retirement, despite progress with goals and healthy financial behaviors.



Not to scale. For illustrative purposes only.
Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

financial capabilities and simply having had more time to save for retirement, older respondents reported lower confidence and perception about their future retirement prospects, with scores significantly lower than the measures of their present actions would suggest. Thus, we believe that individuals may not fully appreciate and correctly value the impact of their present actions, either good or bad.

Houston, we may have a problem with perception.

Strong financial wellness scores are most highly correlated with more substantial retirement savings, home ownership, and proficient management of debt—both credit card and student debt, for those who have it. Our results are not surprising but are still incredibly instructive. The data suggests that those who struggle with saving are likely to value present consumption more than deferred consumption.

While we observe that financial capability generally increases with age, the importance of starting to save early in one's career and saving persistently is reinforced by the observed effect of age. Simply put, by holding savings constant, an older respondent's confidence decreases as they near retirement which results in a lower financial wellness score than a younger respondent. Starting to save early and saving often is a winning strategy.

How Employers, Financial Professionals, and Recordkeepers Can Use Financial Wellness

What can employers and financial professionals do? Well, a lot. There are multiple avenues to addressing savers' needs—be it through plan design, the use of personalized communication and messaging, or simplifying processes and removing behavioral friction from transactions that will benefit retirement savers.

All these strategies play a part in meeting savers where they are. Seven in 10 participants surveyed say they rely on the company that manages their workplace retirement plan to help them achieve their lifetime financial goals.

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Employers and financial professionals can incorporate financial wellness by:

Choosing plan design features (e.g., auto-enrollment, auto-escalation, matching formulas, vesting, employer contributions, etc.) that both nudge and incentivize plan participation and saving among the employee populations least likely to do so.

Offering programs that help employees assess their point-in-time financial health, and set, monitor, and prioritize meaningful financial goals, such as:

- Targeted, personalized communications to engage nonparticipants and participants to inspire them to take financially healthy actions, such as increasing savings or paying down high interest rate debt.
- Educational programs and tools that help employees budget their monthly living expenses to align the income with both debt management and savings goals (e.g., emergency savings, retirement, home purchase, etc.).
- Offering services (e.g., emergency savings, consumer debt management, student loan repayment assistance, financing, and transactional processing, etc.) that help savers overcome the behavioral friction and automate emergency savings and/or debt repayment.
- Delivering of services through multiple modes of engagement that span from digital to in-person so that those who seek counseling or coaching can do so in a manner that best meets their needs.
- Ongoing measurement and assessment tools that reinforce healthy behaviors and highlight the long-term benefits of healthy financial actions taken today and their impact on future outcomes.

FINAL THOUGHTS:

Financial wellness takes on different forms at different life stages. Though saving for retirement is always present, more pressing, near-term needs threaten to deprioritize retirement saving in the moment.

Employers, financial professionals, and recordkeepers are all stakeholders in ensuring that plan participants achieve balance between short-term and long-term financial objectives, increase financial resiliency, and make the connection between the actions one takes today and the outcomes that are achieved in the future.

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CCON0083396 (8/2021)
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