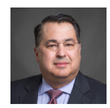
# Financial Stress Is a Predictor of Financial Wellness

Discover how financial wellness can enable retirement savings.

June 2022



**Joshua Dietch**
*Head of Retirement Thought Leadership*

### KEY INSIGHTS

- Debt, particularly unsecured debt, correlates with financial stress.
- Retirement plan participants who report being stressed about debt are saving less for retirement than those who are not stressed.
- Promotion and adoption of financial wellness programs can help reduce financial stress and may lead to greater savings and better participant retirement outcomes.

The path to a successful retirement is paved by financial wellness. In the context of saving for retirement, to be financially well requires successful management of day-to-day finances, setting and making progress toward financial goals, and believing that these actions will result in a successful retirement. In our 7th annual Retirement Savings and Spending Study,[1] T. Rowe Price found that financial stress, specifically around debt, is a primary barrier to people's belief that they will be able to successfully retire.

In our study, we find that many workers saving for retirement struggle with financial wellness in a variety of ways, and our research suggests that some are deeply affected by struggle with it.

For example:

- One-third of respondents report that they struggle to stick to their monthly budgets.
- More than one-third of respondents with student loan debt struggle to repay it. Similarly, 20% of respondents struggle to repay other forms of debt such as credit card or home equity.
- One-quarter of respondents believe they will have to reduce their standard of living in retirement.

While many people do struggle, many are successful, and we felt it was important to develop a framework by which to measure both progress and success. To measure the behaviors necessary to achieve success in retirement, T. Rowe Price developed

[1] The T. Rowe Price Retirement Savings and Spending Study (RSS) is an annual study that has been conducted online since 2014. The study annually surveys approximately 3,000–4,000 participants who are currently contributing to a 401(k) plan or eligible to contribute and have a balance of at least $1,000. The survey also includes an additional 1,000–1,500 retirees who have retired with a Rollover IRA or left-in-plan balance. The study investigates saving attitudes and behaviors of plan participants and retirees. The 2021 RSS was conducted between June 9, 2021, and August 4, 2021, and included 3,844 plan participants and 1,332 retirees.

Black and Hispanic workers are **34%** and **40%** more likely to experience higher levels of debt-related stress than white workers.

the Retirement Behavior Index™. The index measures financial wellness in the context of saving for retirement on a scale of 0–100, with 0 being the lowest and 100 being the highest.[2] It measures how well those saving for retirement balance their day-to-day finances and the financial goals they set for themselves and how they see their future selves in retirement. Specifically, the index examines:

1. Management of day-to-day household financial behaviors (e.g., savings patterns and responsible credit use)
2. Setting and making progress toward personal financial goals (e.g., saving for retirement or paying down student loan debt)
3. Beliefs about what will be true about a person's future retirement (e.g., maintaining their standard of living or being able to withstand a financial shock)

In 2021, we used the same methodology in our paper, "Financial Wellness Through the Lens of Race and Ethnicity." This year, we applied the index methodology to better understand the impact financial stress can have on people's behavior and how they see their future retirements. Most importantly, we hope that by drawing attention to how the effects of financial stress can be quantified, we can help plan sponsors, financial professionals, consultants, and recordkeepers better assist savers to achieve success in saving for retirement.

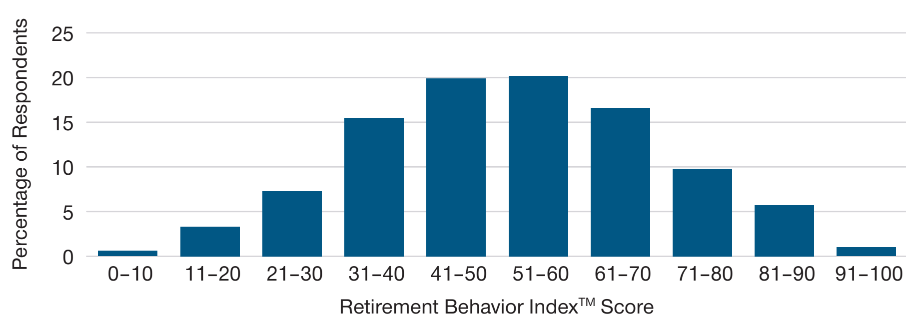
### Financial Stress Often Starts With Debt

It probably comes as no surprise that financial wellness and financial stress are two sides of the same coin. What our research found is that financial stress is a predictor of poor financial wellness. However, there are multiple causes of financial stress, and they affect people differently. In our research, we focused on stress emanating from debt, budgeting, savings (both retirement and nonretirement), managing investments, and health care costs. For those who struggle with financial wellness, stress most frequently stems from the inability to manage debt, budgeting, or lack of retirement and nonretirement savings. In contrast, those with higher levels of financial wellness report being more concerned with health care costs or managing their investments, suggesting that financial stress may emanate from managing wealth rather than managing debt or seeking to save.

Our research found that financial stress is experienced disproportionately along racial and ethnic lines. Black

## Many Workers Saving for Retirement Struggle With Financial Wellness

(Fig. 1) Distribution of Retirement Behavior Index™ scores

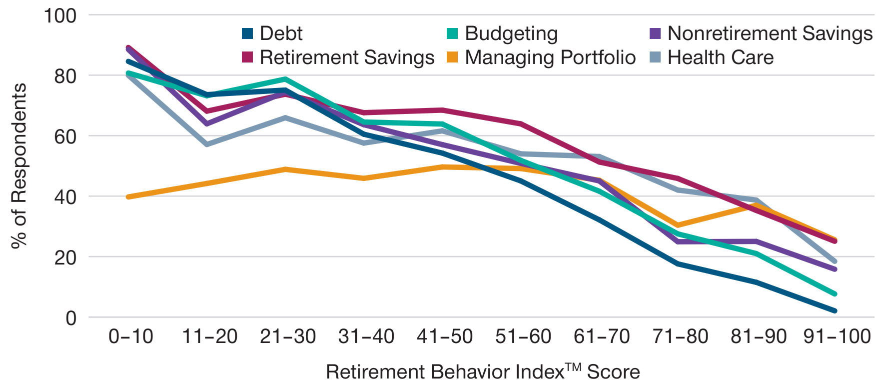



As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

[2] For more information on the Retirement Behavior Index™ and its methodology, please refer to the following **brief overview**.

## Debt, Budgeting, and Savings Are the Three Most Common Drivers of Financial Stress

(Fig. 2) Moderate to high levels of financial stress by source



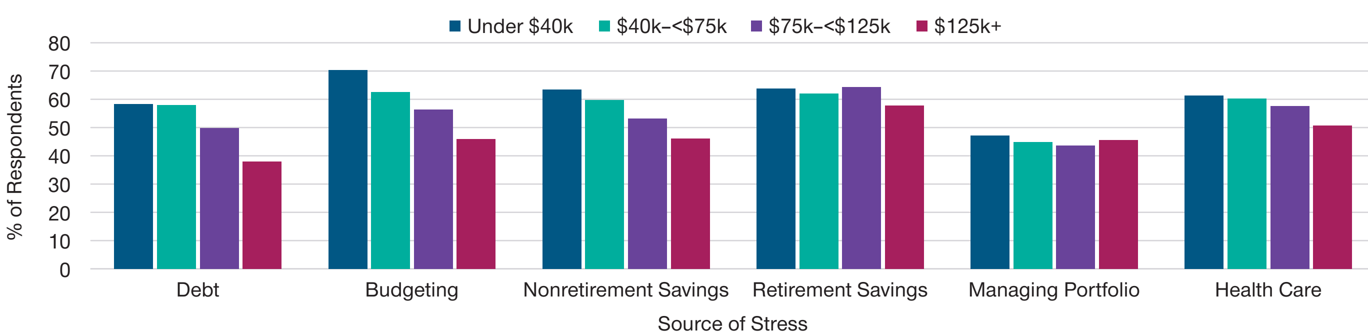

As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

and Hispanic workers are 34% and 40% more likely than white workers to experience higher levels of debt-related stress, as reported by 56% of Black workers, 59% of Hispanic workers and 42% of white workers surveyed.

Our research also found that a moderate to high level of stress often correlates with age. For example, younger workers (<30 years old) are more likely to experience moderate to high levels of stress relating to budgeting compared with older workers (>50 years old), 73% and 40%, respectively. A similar effect is seen for debt. However, younger workers are less likely to be stressed about retirement savings than those who are entering or are in the middle of their working years (30–49 years old), 50% and 65%, respectively. This demonstrates that relevance is a significant factor and that audiences have unique and often discrete needs—something to note for plan sponsors, financial professionals, consultants, and recordkeepers who may be considering strategies to address financial wellness.

## Financial Stress From Debt, Budgeting, and Nonretirement Savings Strongly Correlates With Household Income

(Fig. 3) Moderate to high levels of financial stress by source and household income




As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

Women are **26%** more likely to experience higher levels of debt-related stress than men.

Last, it is important to state that people often feel the negative effects of moderate to high levels of financial stress unevenly. In addition to age, gender, race, and ethnicity, household debt and income are—unsurprisingly—also factors as to who is affected by financial stress and why.

Interestingly, there does not seem to be a strong correlation between marital status and financial stress, as married or partnered couples have similar levels of stress as the respondents who were single. That said, we do see significant differences between women and men. Women are 26% more likely than men to experience higher levels of debt-related stress, as reported by 51% of women and 41% of men surveyed. Women also experience higher levels of financial stress relating to budgeting, nonretirement savings, and health care expenses.

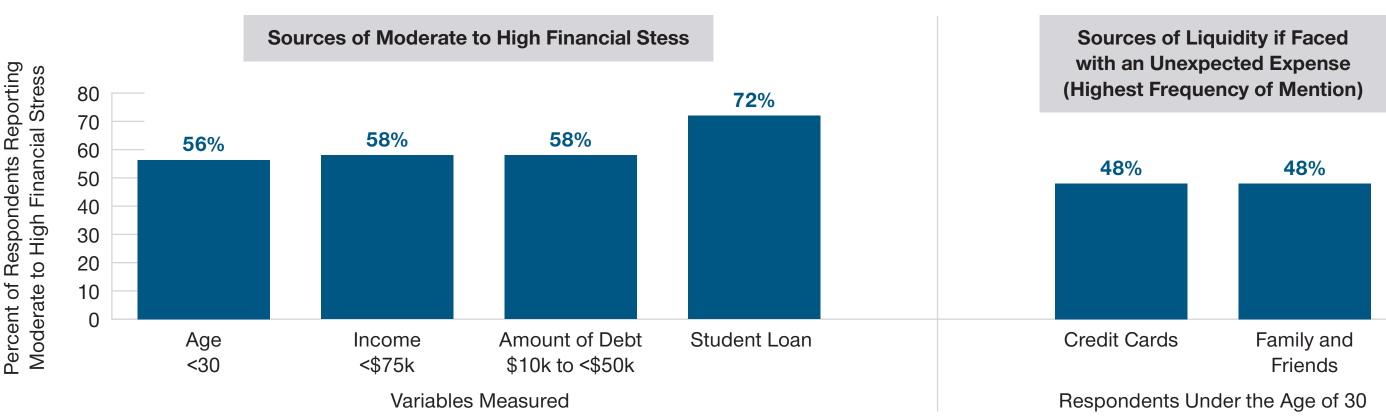
### Importance of Financial Resiliency

The prevalence of financial stress relating to debt, budgeting, and nonretirement savings leads us to conclude that many workers lack the resiliency (e.g., ability to pay) to overcome many common financial obstacles such as an auto repair bill or a trip to the doctor. Our research suggests that survey respondents are quite aware of their vulnerability and would like to take steps to address it. In fact, 88% of those we surveyed shared that saving for an emergency (such as losing their job or having an unexpected expense) was a major or minor financial goal. But almost one-quarter reported making not very much or practically no progress toward meeting their goal. Moreover, when asked how they might pay for an unexpected expense, only one-third of the workers we surveyed claimed they had an emergency fund specifically allocated to meet that need. More common is the intention to use debt such as a credit card (43%) to pay for an unexpected expense. The finding is consistent with research from the Federal Reserve that suggests that 48% of Americans either cannot pay or would have difficulty paying for an unexpected $400 expense.[3]

The role debt plays in financial stress is unique because not all debt is created equal. For example, those who report financial stress relating to debt are more likely to cite student loans, medical debt, or payday loans as sources of stress compared with credit cards, auto loans, or home equity loans. What we can infer is that the characteristics of some

## Debt Is Both a Source of Financial Stress and a Barrier to Financial Resiliency

(Fig. 4) Age, income, debt, and financial resiliency




As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

[3] Federal Reserve Bank of Minneapolis, https://www.minneapolisfed.org/article/2021/what-a-400-dollar-emergency-expense-tells-us-about-the-economy.

People with higher budget-related stress report saving **25% less** than those with lower levels of financial stress.

forms of debt are indicative of hardship rather than day-to-day household finance. Our research also suggests that there are factors such as age and income that may be correlated with how people perceive debt. For example, we know that younger workers tend to earn lower wages than older workers. Younger workers are also more likely to have student loan debt. Thus, it is not surprising that those who hold student loan debt report moderate to high levels of financial stress. Financial fragility comes fully into view when this group is asked about what resources they have available to them if they were to face a financial emergency. Almost half said they would rely on both credit cards and friends and family; far fewer cited said they would turn to an emergency fund.

This is not the only example of the challenges that people face with financial resiliency. Other types of potentially burdensome debt, in addition to student loan debt, include payday loans and medical debt. Managing this debt is critical to achieving financial wellness. Regression analysis reveals that debt-related stress is a strong predictor of Retirement Behavior Index™ scores, as is stress related to budgeting. People can save for retirement and achieve financial wellness, but they must examine day-to-day spending, set and make progress toward financial goals, and envision the outcome they can achieve in retirement by prioritizing the future over today.

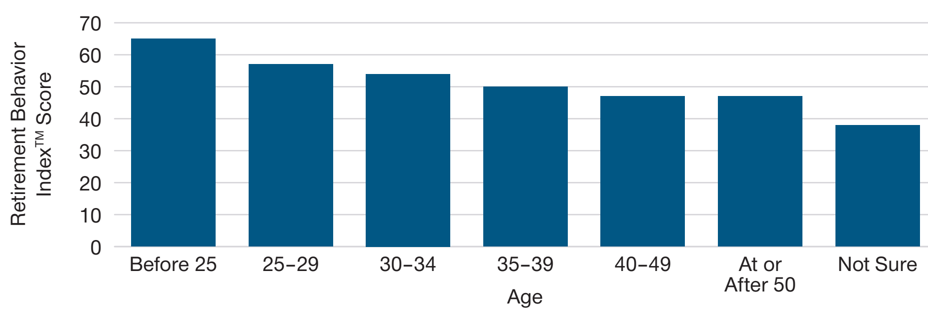
### Plan Design Can Impact Financial Wellness

Exploring the relationship between financial wellness and retirement savings revealed a profound relationship between the two. Practically speaking, saving for retirement requires delaying consumption. Moreover, and importantly, it calls for people to prioritize their future self over their present self. There are ways, both big and small, that the plan sponsors, financial professionals, and consultants they work with can encourage this, but the most impactful in our view is plan design.

It's well known that the retirement industry can help through use of automatic enrollment, automatic escalation and implementation of target date strategies as qualified default investment alternatives (QDIA), often coupled with both automatic enrollment and automatic reenrollment. These strategies have been effective in getting employees to begin saving, save at meaningful levels, and invest their savings in age-based and risk-appropriate investment strategies. However, what is less well understood

## Starting to Save for Retirement Early in the Working Years Can Lead to Long-Term Financial Wellness

(Fig. 5) Financial wellness and age started saving for retirement




As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

Workers under 30 years old are **72% more likely** than workers over 50 years old to use help managing their debt.

is the relationship between savings and financial wellness.

What our research found is that Retirement Behavior Index™ wellness scores are inversely correlated with the age that a person starts to save for retirement. The earlier a person starts to save, the more likely they are to be financially well over the long term. The data show a beneficial effect of automatically enrolling young and often lower-paid workers, who might not otherwise choose to participate, in retirement plans.[4]

The benefits of starting to save early and achieving long-term financial wellness are often self-reinforcing. Often overlooked, but not to be forgotten, is the effect of time. Those who start to save early benefit from years of saving and the potential of compounding returns that those who start later do not benefit from to the same degree. The longer participants are distracted from saving, the more challenging financing retirement becomes. Thus, reducing financial stress to enable the capacity to save is an imperative.

Our analysis found that financial stress is correlated with savings. Those with higher levels of financial stress are likely to be saving less than those who report having a low or practically no levels of stress. The same is true with budgeting. Those who report higher levels of budget-related stress also report saving 25% less than those with lower levels of budget-related stress.

Not surprisingly, when discussing the merits of financial wellness programs, the conversation often turns to identifying the return on investment (ROI) on implementing them. Our research suggests that the ROI of these programs, as measured by reduced financial stress and increased savings rates, can be significant given the correlation between financial stress and savings rates.

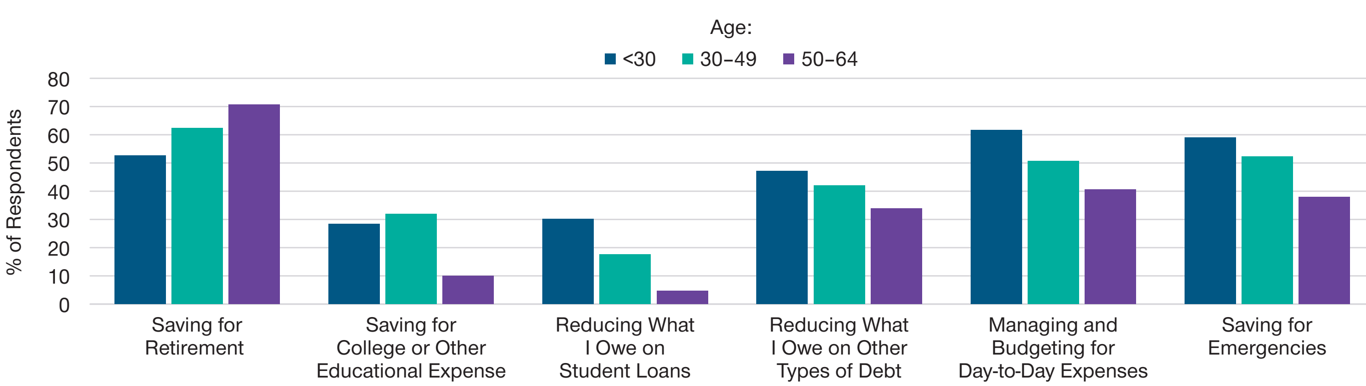
### How to Improve Workers' Financial Wellness

The 7th annual Retirement Savings and Spending Study and the Retirement Behavior Index™ reveal much about how financial stress, particularly stress about debt, can negatively impact saving for retirement. Fortunately, there is much that the retirement industry can do to help employees improve their near- and long-term financial well-being.

In our research we asked respondents to identify major financial objectives, and we found that the prioritization of objectives changes with age. For example, saving

### Financial Priorities Change With Age

(Fig. 6) Select major financial goals




As of August 2021.
Source: 7th annual Retirement Saving and Spending Study.

[4] For more information on the long-term benefits of auto-enrollment adoption, please refer to Auto-Enrollment's Long-Term Effect On Retirement Saving, https://www.troweprice.com/retirement-plan-services/en/insights/savings-insights.html.

for retirement, while important to most, is more important to those on the precipice of retiring than those who are further away from it. This insight is confirmed by the saving behavior among the more than 2 million plan participants that T. Rowe Price has on its recordkeeping platform. In contrast, reducing student loan debt appears to be less of a concern as that debt is paid off. This demonstrates that meeting participants where they are is critical for employers seeking to create a well-designed financial wellness program.

While financial priorities may change with time, it is also important to consider how likely employees are to engage with financial wellness programs and what they may use them for. For example, when delivering a program designed to help employees manage debt or budgeting, it is important to know that older workers are less likely than younger workers to use a program. In fact, our research shows that if their employer were to offer help managing debt or budgeting, younger workers (<30 years old) would be more likely to use these programs than older workers (50+). Further, tools such as calculators are likely to be more widely used than educational meetings or webinars or even one-on-one guidance, potentially signaling that privacy and utility are major considerations.

### What About Advice?

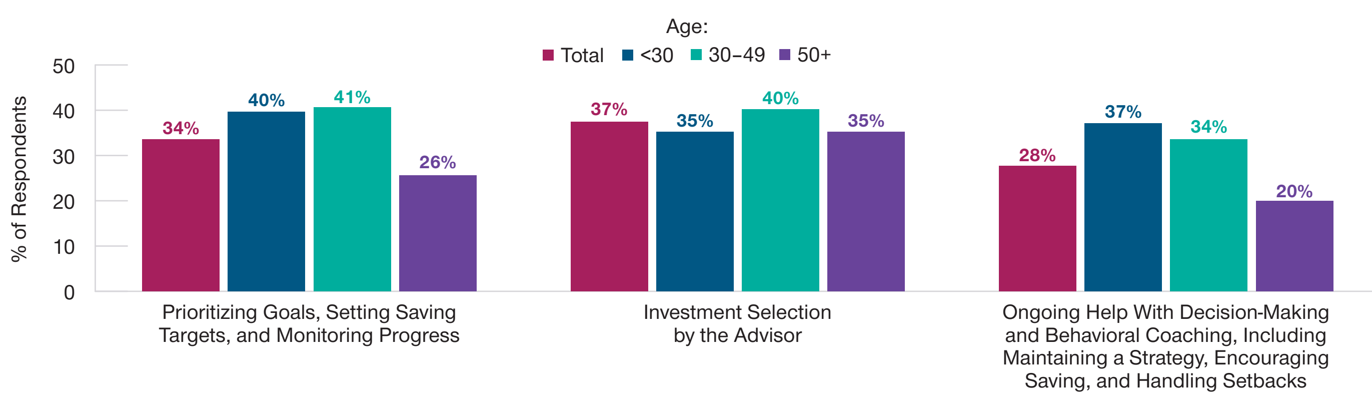
If financial wellness is principally about helping people help themselves, then advice takes it a step further and offers both prescription and, potentially, fulfillment. A conventional knock on advice is that people are unwilling to pay for it. What we found is that almost 70% of our survey respondents were either paying for advice or would consider doing so. However, attitudes about advice and for what vary greatly by age.

Our research points to an advice divide. The first generation of 401(k) participants have come through the system in ways that are fundamentally different from those who have entered in the past 10–15 years. For those over the age of 50, their first exposure to saving for retirement did not include auto-enrollment, default savings rates, or the QDIA. Instead, they chose to participate in their employer's plan, picked a deferral rate, and allocated their own assets. Today's retirement plan participants are different. Most are automatically enrolled in their employer's plan at a default savings rate and invest in their employer's chosen QDIA.

Today, most participants view the worksite as the place where they receive financial assistance or advice. Further, employees are increasingly looking to their employer—and, by extension,

## Younger Workers Have Greater Interest in Advice That Encompasses Financial Wellness

(Fig. 7) Select major financial goals




As of August 2021.
Source: 7th annual Retirement Savings and Spending Study.

their employer's retirement plan—as a resource for help with financial wellness needs. This includes not only investment advice, but information on debt management, budgeting, emergency savings, and more. Moreover, our research suggests that they are increasingly open to the potential of paying for this guidance. This is particularly true of Black and Hispanic respondents, 52% of whom shared that they would consider paying for advice in the future.

### Solutions to Help Reduce Financial Stress and Increase Retirement Savings

This shift in the position and role of the retirement plan as a vehicle for financial wellness poses an opportunity to plan sponsors, financial professionals, consultants, and recordkeepers. This opportunity centers on helping plan participants improve their day-to-day household financial behaviors, make greater progress toward the financial goals they set for themselves, and improve how they view their future self living in retirement. In fact, based on our study results, 78% of employees rely on their workplace for advice and support on how to achieve lifetime financial goals. Central to this journey is saving for retirement.

This opportunity is not without challenges. Insights from both the 7th annual Retirement Savings and Spending Study and T. Rowe Price's Retirement Behavior Index™ demonstrate the ill effects that financial stress can have not only on day-to-day household finances, but also on longer-term goals such as saving for retirement. Next, we discuss actions worth considering to meet both the opportunity and the challenge.

## Employers and Financial Professionals Can Help Improve Employee Financial Wellness by:

### Using Plan Design to Increase Participation and Savings and Improve Investment Allocation

- 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.
- Integrating QDIAs with plan design features like reenrollment to reengage employees who have previously opted out of saving or resetting investment allocations to help ensure allocations are both age-based and risk-appropriate.
- Considering plan design and other innovations such as matching student loan debt repayments or establishing an emergency savings program, which can sit alongside the retirement plan.

### Increasing Access to Financial Wellness Programs

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.
- Interventions that educate participants of their alternatives when they attempt to take actions that may be detrimental to their long-term financial well-being, such as lowering deferral rates, taking loans or hardship withdrawals, or opting out of participation.
- 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.).

- Services (e.g., emergency savings, consumer debt management, student loan repayment assistance, financing, and transactional processing, etc.) that help savers overcome behavioral friction and automate emergency savings and/or debt repayment.
- Delivery 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 way 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 potential impact on future outcomes.

## FINAL THOUGHTS

Financial wellness takes on different forms at different times over life's stages. Though saving for retirement is always present, there are more pressing, near-term needs that can threaten to de-prioritize retirement saving in the moment.

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

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