How the Coronavirus Pandemic Is Affecting Retirement Saving

By offering financial wellness programs, plan sponsors can better serve participants who need financial help

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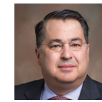


Joshua Dietch
Vice President, Retirement Thought Leadership

KEY INSIGHTS

- The coronavirus pandemic is exacerbating an already troubling societal retirement saving shortfall as workers look to long-term retirement savings to solve short-term financial problems.
- While the percentage of participants taking advantage of CARES Act provisions such as distributions and expanded loan options is low, doing so may undo years of retirement savings.
- Solutions like financial wellness can help shape future financial behaviors when balancing and reconciling short-term needs and long-term financial goals.

The coronavirus pandemic and resulting economic downturn are unlike anything 401(k) investors have ever experienced. Through May 2020, the Bureau of Labor Statistics estimated that over 20 million Americans lost their jobs. Though job loss has moderated somewhat with states reopening their economies, the impact year over year is still considerable.

Though different, this isn't the first rodeo for many retirement savers. The last significant economic contraction and bear market they faced was back in 2007–2009 during the global financial crisis. For the past 11 years, retirement savers have enjoyed a mostly uninterrupted bull market and the associated growth of their retirement savings during this time. Time can heal wounds, and many savers have had the opportunity to recover from the last crisis. However, are they really better off and more prepared to weather the economic uncertainty associated with the coronavirus pandemic?

Arguably, this time is different because retirement savers have recently suffered through extreme market volatility while also contending with risks to their physical well-being. Moreover, coronavirus-related health risks are driving economic risks with respect to employment and consumption. Absent a vaccine or an effective therapeutic regimen, it might be some time before the economy can return to a pre-pandemic level of growth or activity.

> "The coronavirus pandemic adds a new layer of uncertainty for those saving for retirement."

“Less than 10% of participants stopped or reduced their savings.”

Despite this, the one constant that remains true is the challenge that working Americans face in saving for retirement. The Employee Benefit Research Institute estimates that the current savings deficit of $3.68 trillion for workers ages 35 to 64 could increase an additional 4.5% to 11.2% due to this crisis.[1]

The long-term effects this pandemic will have on saving behavior are unknown at this point. However, we do know how 401(k) savers have responded to past economic downturns. Accordingly, we can use this data to envision how individuals may respond to triage their current financial circumstances. Moreover, these insights can also help plan sponsors and financial professionals identify opportunities to assist retirement savers who are struggling financially and provide tools that can help them become more resilient going forward.

A Pandemic Brings Policy Changes

The rapid onset and the depth of the coronavirus pandemic forced policymakers to confront the reality that direct assistance from the government and increased access to tax-advantaged, long-term savings intended for retirement were the only safety nets available to many workers.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law in March 2020. The act includes several provisions that offer financial relief to retirement plan participants who have been diagnosed—or have a spouse or dependent who has been diagnosed—with SARS-CoV-2 or COVID-19, the disease caused by the coronavirus, or who have experienced adverse financial consequences as defined in the CARES Act.

The key provisions include increased limits on loans, the ability to suspend loan payments for up to one year, and the creation of a new coronavirus-related distribution option that allows participants to withdraw up to $100,000 with special tax relief and a repayment option. These provisions were enacted in anticipation of savers facing economic hardships that would be swift and unlike anything previously experienced since the Great Depression.

Participants’ Reaction to Economic Threats

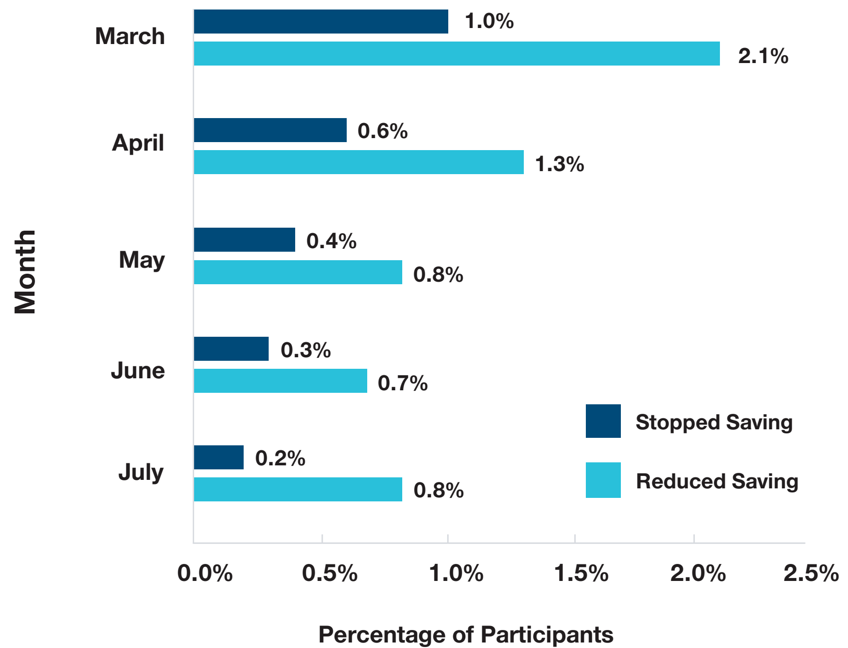
As a recordkeeper, T. Rowe Price services more than 2.2 million retirement plan participants on behalf of their employers. Though the coronavirus pandemic has yet to run its full course, there are both encouraging and disconcerting signs.

First, it appears that most participants are largely staying the course in terms of their long-term savings strategies. Since early March through the end of July, only 2.5% of participants have suspended salary deferrals and only 5.6% have reduced their savings rate. Most who stopped or reduced savings did so early in the crisis, and subsequent activity has moderated, likely due to stimulus payments and enhanced federal unemployment benefits that temporarily buoyed households affected by the crisis.

[1]EBRI Issue Brief No. 505, Impact of the COVID-19 Pandemic on Retirement Income Adequacy: Evidence from EBRI’s Retirement Security Projection Model®, April 21, 2020.

Participants Were More Likely to Save Less Than Stop Saving for Retirement

(Fig. 1) Monthly activity of participants who stopped saving or reduced savings rate in 2020

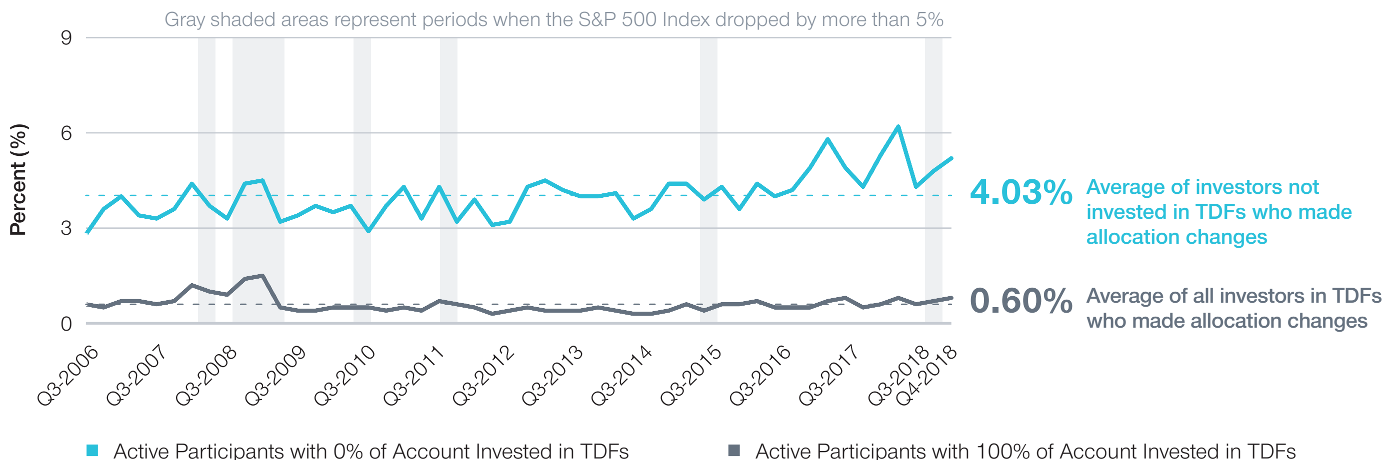


Source: T. Rowe Price Retirement Plan Services, March 1–July 31, 2020. Plans with assets greater than $25 million.

Secondly, participants historically have not traded due to market volatility. That remains true today. That said, not all participants are equal. Participants (Figure 2) who were 100% allocated to target date investments (e.g., many who were auto-enrolled) were less likely to trade than the general plan population. In contrast, those who were not invested in any target date investments were far more likely to transact. Further, these investors were most likely to be harmed by trying to time the market, particularly since the market has recovered from the

Target Date Funds (TDFs): Lower Exchange Activity During Market Volatility

(Fig. 2) Percent of investors that made an allocation change, September 30, 2006–March 31, 2020

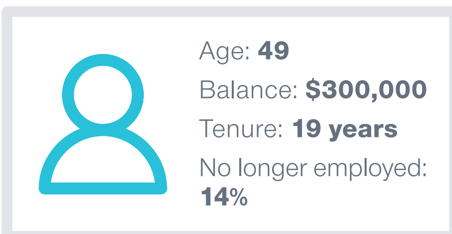


Source: T. Rowe Price Retirement Plan Services.

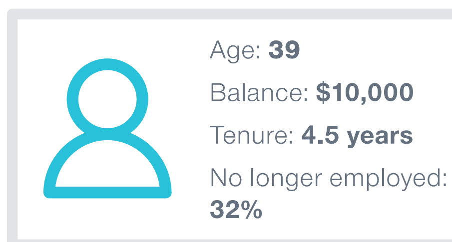
Loans and Coronavirus-Related Distributions Can Undo Years of Retirement Saving

Profile of an average participant who took a coronavirus-related loan

Profile of an average participant who took a $100,000 coronavirus-related distribution



Profile of an average participant who withdrew 100% of their funds in a coronavirus-related distribution



Source: T. Rowe Price Retirement Plan Services, March 1–July 31, 2020. Plans with assets greater than $25 million.

lows reached in March 2020. Though plan design has proven useful to many, some investors still succumbed to the often counterproductive instinct to seek safety in times of uncertainty.

CARES Act Loans and Distributions Could Have Long-Term Consequences

When policymakers cleared a path to allow those who are eligible to use their retirement savings with fewer penalties and restrictions, most resisted the temptation to do so. Although two-thirds of T. Rowe Price's clients[2] have adopted at least one of the CARES Act provisions to date, only 6% of participants have either taken a coronavirus-related loan, a coronavirus-related distribution, or have suspended their loan repayments.

Additionally, our data show that 8.2% of participants with an outstanding loan have taken advantage of CARES provisions to temporarily suspend a repayment. Also, 53% of those who have suspended their loan repayments have also taken a coronavirus-related distribution. These figures may rise as defaults in mortgages, auto loans, and other forms of debt increase as the crisis continues.

Although the absolute number of participants taking coronavirus-related distributions is relatively low, the profile of today's transactions suggests that participants who decide to tap retirement accounts may be unwinding years of retirement savings progress.

- Of those who have taken a coronavirus-related distribution, 21% have withdrawn the maximum (the lesser of 100% of the vested account balance or $100,000).
- Average loan amounts are three times higher for participants taking advantage of CARES Act higher loan limits.

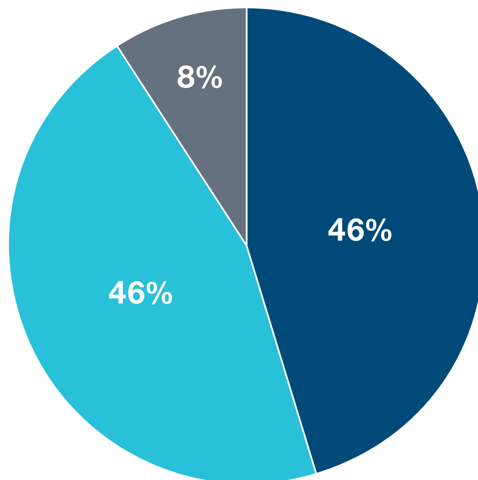
The economic impact of this crisis will not be fully understood until the pandemic has fully run its course.

Participants who have consistently demonstrated a wide set of healthy financial behaviors over time may find themselves in a more comfortable position without having to adjust their savings rates. For them, saving from an early age, keeping expenses under control, thinking constructively about investment risk, and building emergency savings to avoid tapping retirement accounts for nonretirement needs all play a part in supporting financial resilience.

[2] T. Rowe Price Retirement Plan Services. Plans with assets greater than $25 million.

Factors Affecting Retirement Date

(Fig. 3) Unforeseen circumstances often influence timing of retirement



Why did you retire earlier or later than planned?

REASONS FOR RETIRING **EARLIER**

- Changes in my spouses's or my health **32%**
- Emotionally ready to retire earlier than anticipated **26%**
- Financially prepared earlier than anticipated **23%**
- Job loss **22%**

REASONS FOR RETIRING **LATER**

- Continue to receive health or other benefits **41%**
- Still enjoy working **31%**
- Not financially ready **30%**
- Maximize income **28%**
- Unsure what else to do **28%**

Source: 2019 T. Rowe Price Retirement Savings and Spending Study.

The Challenge of Planning for Retirement

Today's combination of a public health and economic crisis demonstrates how truly difficult planning for retirement can be. Even under the best of circumstances, there a large number of unforeseen variables that can influence the decisions one has to make. In its 2019 Retirement Savings and Spending Study, T. Rowe Price asked retirement savers about their expectations regarding their future retirements.

The results are telling, not just in the context of when the questions were asked, but also how the answers might change considering today's coronavirus public health crisis.

Our analysis of those who weathered the global financial crisis during their working years (Figure 3) shows that they did not retire when planned due to circumstances or catalysts (e.g., decline of heath, financial need, job loss, etc.) beyond their control. Interestingly, expected retirement age increases as people get older, which demonstrates the difficulty of planning for a point in time that is dependent upon many unknown variables (as shown in Figure 3).

So, what do today's workers expect?

One of the key considerations for deciding when to retire is financial security. A full third of the workers surveyed are concerned that they will have to reduce their standard of living in retirement. For many, Social Security will play a vital role in ensuring that nondiscretionary (e.g., food, health care, housing, transportation, etc.) needs are met.

For all generations, the earliest one can claim Social Security is at age 62. To receive full benefits, both millennials and Generation X must wait until they are age 67. Baby boomers, depending on the year they were born, can claim as early as age 66. To receive the maximum benefit, all must wait to age 70.

Ironically, millennials expect to retire earlier than the generations preceding them despite their skepticism of future Social Security benefits. This and past Retirement Savings and Spending Studies suggest that millennials will likely adjust their expectations as they near retirement.

Millennials Want to Retire Early Despite Reservations About Social Security's Future

(Fig. 4) Claiming benefits before full retirement age also will decrease monthly benefits for millennials and Gen X

Generation	Planned retirement age	Percent who "strongly agree/agree": "I don't expect any Social Security benefits when I retire."
Millennials (Age 23–38)	63	52%
Generation X (Age 39–54)	66	47%
Baby Boomers (Age 55–73)	67	14%

Sources: Pew Research Center, Social Security Administration, and 2019 T. Rowe Price Retirement Savings and Spending Study.

How Plan Sponsors Can Help Those in Financial Hardship

Our 2019 study also revealed a continuing undercurrent of financial fragility among workers saving for retirement, highlighting the fact that many workers lack nonretirement savings, emergency or otherwise, and cannot absorb unexpected financial hardship.

Forty percent admitted that they would use credit cards if faced with a financial emergency, and one-third admitted carrying credit card balances month to month. Workers not only need help to plan for retirement, but also need help with more day-to-day needs, such as having an emergency fund, managing debt, or other more general financial wellness needs.

The good news is that plan sponsors and financial professionals have an opportunity to help. Between 40% and 60% of the workers surveyed expressed interest in receiving help from their employer or retirement plan recordkeeper with financial objectives to determine savings goals, prioritize or track progress toward saving for retirement or college educations for their children, reduce debt, and manage day-to-day expenses.

Yet despite the apparent need for guidance and advice, less than half of 401(k) participants surveyed are using financial professionals, and most say that they prefer to gather information and make their own financial decisions. This could be a result of believing that traditional financial professionals wouldn't help them because they don't have enough assets to become a client or that financial professionals wouldn't meet their needs. Instead, most participants look to the company that manages their employer's 401(k) plan, likely due to the ease of use or availability and the relationship with their employer.

Times of crisis often serve to crystalize thoughts and spur action. In that vein, the coronavirus pandemic has served as a catalyst to advance ongoing conversations between retirement and benefits professionals and their service providers. The result is increased interest in adopting programs that can directly address the root causes of financial hardship and provide programmatic remedies such as emergency savings, debt management, and other financial wellness programs that can serve both an employer's and their employees' long-term best interests.

> "...62% of 401(k) plan participants said they rely on the company that manages the 401(k) account to help them achieve their lifetime financial goals."

Participants are hungry for information from a trusted source. And 62% of 401(k) plan participants in 2019 said that they rely on the company that manages the 401(k) account to help them achieve their lifetime financial goals. That sentiment has been confirmed this year based on a closer look at participant online behavior. Consumption of T. Rowe Price's educational content on the participant website has increased 126% compared with the same five-month period last year. More than half of the content being viewed on the participant website relates to financial wellness.

Workplace retirement plans and individual retirement accounts account for two-thirds of financial assets among our annual survey respondents. Because the CARES Act has afforded retirement plan participants greater access to their savings, it's important for plan sponsors and financial professionals, as stewards of retirement plans, to be more vigilant about how participants may be willing to withdraw or borrow from their futures to fix their short-term financial hardships.

There are consequences to taking money out of retirement accounts. It is often said that the winning retirement planning strategy is to start saving at an early age and continue to save throughout one's working life. Simply put, slow and steady wins the race. Contributions made early in one's career can compound and grow over a time period that can extend to over 40 years. One can always save more later, but delaying saving comes at a price. It will require more money because there is less opportunity for compounded growth.

At T. Rowe Price, we study retirement behavior in the hopes that our findings can inform ways to help people make better decisions today and understand how those choices can affect their tomorrow. Plan sponsors and financial professionals have a unique opportunity to help employees better balance competing financial priorities during this financially vulnerable time. Some potential solutions include offering:

- 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 employee populations least likely to do so.
- Programs that help employees assess their point-in-time financial health and create personalized actions that they can take to improve their financial well-being (e.g., track progress, set goals, etc.).
- 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.).
- Modeling tools that allow employees to consider the trade-offs in making financial decisions such as taking on debt, making large purchases (e.g., housing or automobiles), or allocating resources toward savings goals or toward paying down debt.
- Education in a variety of formats from digital to in-person so that those who seek counseling or coaching can do so in a manner that best meets their needs.
- Finally, educational messages that continually stress alternatives to retirement accounts during times of financial hardship are critical. Because the CARES Act has made it possible for larger loans and coronavirus-related withdrawals, it's important to caution against using retirement savings for short-term financial emergencies.

Planning for retirement is challenging. Having financial resources beyond one's retirement assets is essential to staying on a steady path toward achieving one's retirement savings goals.

Employers, particularly those who auto-enroll their plan participants, have a tremendous impact on people's decision to save and stay the course. Still, there is more that can and should be done to address the undercurrent of financial fragility that has become all too apparent during the coronavirus pandemic.

If there is a silver lining to be found, it may be that both employer interest in providing and employee interest in using financial wellness programs have intersected.

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