Financial Wellness Through the Lens of Race and Ethnicity

Employers have an opportunity to promote diversity, equity, and inclusion in defined contribution plans and help address broader social inequality.

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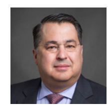
KEY INSIGHTS

- Societal inequality found in the broader labor market is also present in retirement savings.
- Black and Latinx retirement savers are more likely to have debt and less likely to own homes than white savers.
- Defined contribution (DC) plans such as 401(k)s are one of the few places where access to advice, guidance, and education in support of lifetime financial goals is supported equally.



Joshua Dietch
Vice President, Retirement Thought Leadership

Inequality in its many forms is now at the forefront of public discourse; companies and individuals alike are looking for ways to right past wrongs and not let the opportunity of this moment to pass. Private sector defined contribution plans such as 401(k)s are microcosms of both the companies that sponsor them and those who save for retirement in them and the country as a whole. DC plans have created tremendous wealth for millions of Americans saving for retirement. But have the benefits of these plans been realized equally? Or is the racial and ethnic inequality found in the broader labor market also present in retirement savings outcomes and overall financial wellness? There is no doubt that we have arrived at a unique but long overdue time. As employers determine how they may wish to build greater economic equity into their workforce from which all will benefit, the retirement plans they sponsor can help to serve that purpose and financial wellness.

As part of T. Rowe Price's 6th annual Retirement Savings and Spending Study,[1] we sought to better understand not only how well American workers are saving for retirement but their overall levels of financial wellness. The study offered new insights into how this wellness may differ depending on savers' race and ethnicity.

401(k) plans have benefited millions of people saving for retirement. Unfortunately, the benefits have not been shared equally.

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[1] The Retirement Savings and Spending Study was conducted online June 5–24, 2020. A total of 3,420 participants, who are currently contributing to a 401(k) plan or are eligible to contribute and have a balance $1,000, responded. The survey also included 1,007 retirees who have retired with a Rollover IRA or left-in-plan balance.

Among those who have access to 401(k)s, **81%** of the heads of white households participate in a DC plan compared with **70%** of Black and **63%** of Latinx heads of households.

In a related paper, we explored financial wellness through the lens of life stages and introduced a framework by which to measure financial wellness. Our framework measures household financial behaviors and progress toward financial goals and asks respondents what they believe will be true about their retirement.

We found that many Americans struggle with balancing short- and long-term financial goals. In our research, we identified predictors of greater financial wellness that include more substantial retirement savings, homeownership, and more proficient management of debt, among others. We were curious to what extent race and ethnicity also play a role. For this analysis, we will focus on white and Black races and Latinx ethnicity.[2]

The Investment Company Institute estimates that at the end of 2020, the U.S. DC system accounted for $9.6 trillion, and 401(k) plans represented $6.7 trillion of that figure.[3] However, it is also well understood that not everyone benefits equally from DC plans. And, based on our findings, the systemic social inequality found in the broader labor market carries through into retirement savings and overall financial wellness. For example, we learned that access to DC plans is unequal and that among those people who do have access, 81% of the heads of white households participate in a DC plan compared with 70% of Black and 63% of Latinx heads of households. Further, the median account balances for Black and Latinx heads of households were 45% lower than that of white heads of households.[4]

The findings are troubling but not surprising. The primary barriers to access to a 401(k) or other retirement plan is the size of one's employer and the benefit programs they offer. Further, income is correlated with education. Thus, if Blacks and Latinx lack equal access to quality education, it serves to not only limit access to well-paying jobs at larger employers but the benefits, like 401(k) plans, those employers offer.

Income level, in particular, can play an outsized role on the spending and savings behaviors that impact a person's financial wellness—including the ability or willingness to participate in a DC plan. A lower income naturally means less money for an individual to stretch across the many financial obligations they have. People with lower incomes may prioritize day-to-day needs or other longer-term financial goals (debt reduction, saving for a home, etc.) over retirement saving.

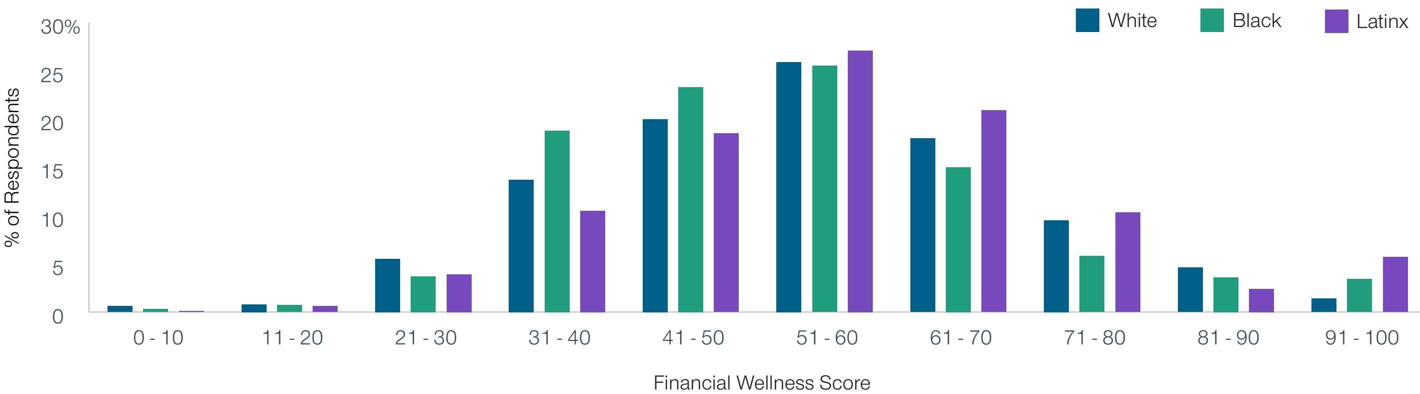
On average, Black and Latinx workers earn less than white workers. According to the Bureau of Labor Statistics, the median wage or salary for Black workers is 79% of that of white workers, and the median for Latinx workers is 73%.[5] Not surprisingly, this ultimately manifests itself in higher debt levels, lower homeownership rates, and lower DC plan participation and contribution levels.

An understanding of these challenges can help employers and financial professionals develop strategies to help Black and Latinx participants get the most benefit from DC plans. Employers and financial professionals can use insights from our own research to help meet the needs of all Americans who wish to thrive financially and retire securely.

[2] We focused on the races and ethnicities where we had nationally representative samples. Thus, we excluded Asians/Pacific Islanders.
[3] Retirement assets total $34.9 trillion in fourth quarter 2020, March 18, 2021. ICI.
[4] EBRI.org Issue Brief, March 11, 2021, No. 527.
[5] Bureau of Labor Statistics – Labor Force Statistics from the Current Population Survey, https://www.bls.gov/cps/earnings.htm#demographics.

Black Retirement Savers' Financial Wellness Trails White and Latinx Peers

(Fig. 1) Overall distribution of survey results examining household financial behaviors and progress toward goals.



Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

The Differences in Financial Wellness

In June 2020, we surveyed over 3,400 Americans who are saving for retirement in employer-sponsored 401(k) plans. One of the key objectives of the research was to better understand the level of financial wellness among the survey respondents. Using our framework that examines current household financial behaviors, progress toward financial goals, and what will be true about one's retirement, scored on a 0–100 scale, we found that the overall distribution of results follows a normal distribution, with the majority of those falling in the middle (Fig. 1). However, we see differences between white, Black, and Latinx respondents' scores. Specifically, Black respondents' scores tend to trail both white and Latinx respondents. We also found that whites' scores trailed that of Latinxs on average—an unexpected finding. However, this observation may be driven, in large part, by a significant cohort of well-educated and affluent Latinx women in our research sample.

In our related paper, we showed that even as financial capability (e.g., one's day-to-day financial behaviors and progress toward short-, intermediate-, and long-term financial goals) increases with age, pessimism about one's future retirement also increases. In addition, the factors that correlate with financial wellness are homeownership, retirement savings, and debt management. Education level also has a strong correlation. Last, while income is important, respondents' ability to save has greater impact on financial wellness than income, in and of itself. This is not surprising given that the ability to save money is reflective of a healthy financial behavior.

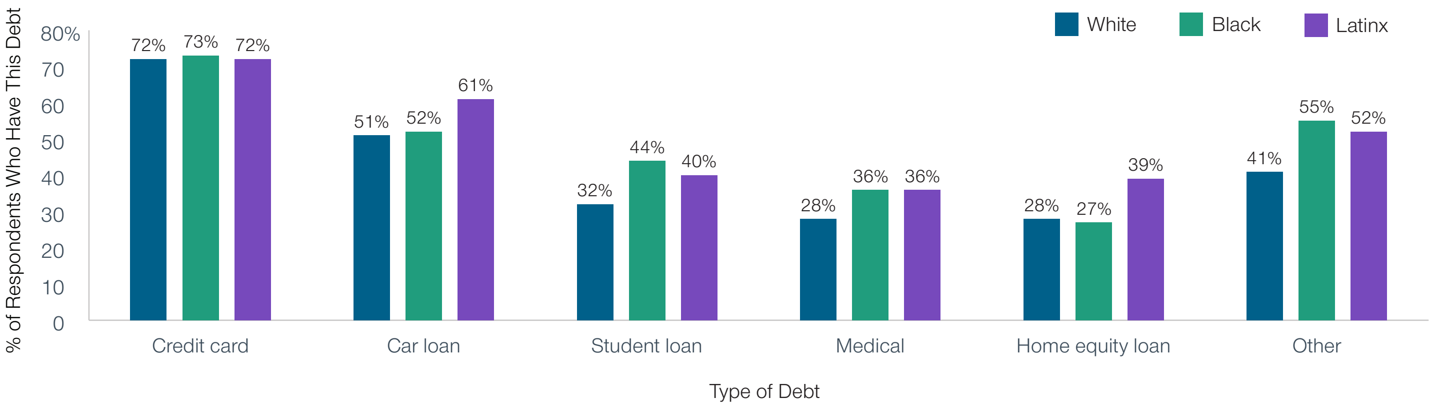
Drivers of Financial Wellness

As mentioned, financial wellness is correlated with higher levels of retirement savings, lower levels of debt, and home ownership. Black respondents are saving 44% less than their white counterparts,[6] and they are more likely to have student loan, medical, and other types of debt.

[6] The impact of the level of savings is correlated with financial wellness and is also dependent on age.

Types of Non-mortgage Debt

(Fig. 2) Black and Latinx respondents have higher incidences of debt.



Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

Median Deferral Rate (% of Wages)

White	Black	Latinx
9%	5%	8%

Black respondents are also far less likely than whites to own a home. While contribution rates for Latinx respondents are higher than Black respondents, they too are more likely to have relatively high levels of consumer debt and are most likely to have withdrawn equity from their home.

The data also suggest that challenges to saving for retirement may vary between different races and ethnicities and this has implications for employers, financial professionals, and retirement recordkeepers. For example, when asked, 20% of white, 26% of Black, and 30% of Latinx respondents reported having difficulty in paying required monthly bills. Thus, budgeting guidance and tools may be valued more by some than others. There are, of course, other more systemic factors that may drive some of these observations. Still, they find their way into how people save for retirement and work toward financial wellness. Thus, all stakeholders in the DC system must acknowledge the effects and seek remedies.

Focus on Retirement

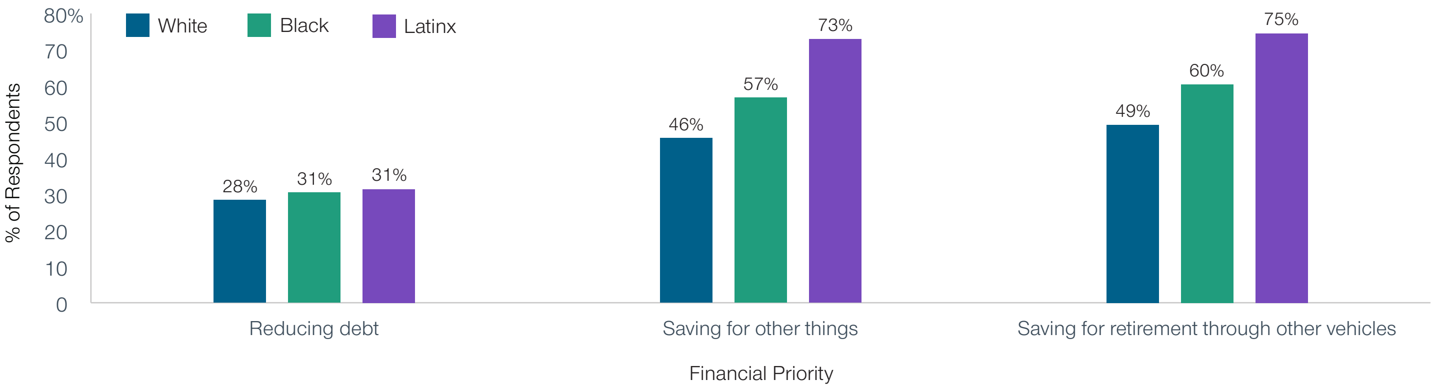
Common to all is the importance of saving for retirement. As we have shown, the level of retirement savings has the single highest impact to one's financial wellness score. Interestingly,

Percent of Respondents Who Own Their Home

White	Black	Latinx
82%	58%	78%

The Barriers to Saving for Retirement Vary by Both Race and Ethnicity

(Fig. 3) Reasons cited for not saving 15% of wages in workplace retirement plans.



Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

55% of respondents believe, despite inadequate levels of saving and high levels of debt, that they are saving enough to enjoy a comfortable retirement. The remaining 45% are either aware they are not saving enough or are unsure if their retirement plan contributions are sufficient.

If almost half do not feel they are saving enough, what is standing in their way? While income plays a significant role, the reasons vary overall, suggesting that non-targeted approaches to closing savings gaps may not be effective.

For example, Black and Latinx respondents are more likely to say that they are saving for retirement in vehicles other than employer-sponsored plans. They could be saving in IRAs or may plan to rely on family as a source of financial support in retirement. Black and Latinx respondents are also more likely to cite that they are saving for things other than retirement, such as buying a house or building up an emergency fund. Last, both Black and Latinx respondents were more likely to cite reducing debt, which we have already shown they have higher incidence of, as a barrier to retirement savings.

These barriers highlight that more personalized approaches to solving financial wellness may direct resources where they are most valuable. As an industry, we could do a better job in doing this for all people, regardless of race, ethnicity, or gender.

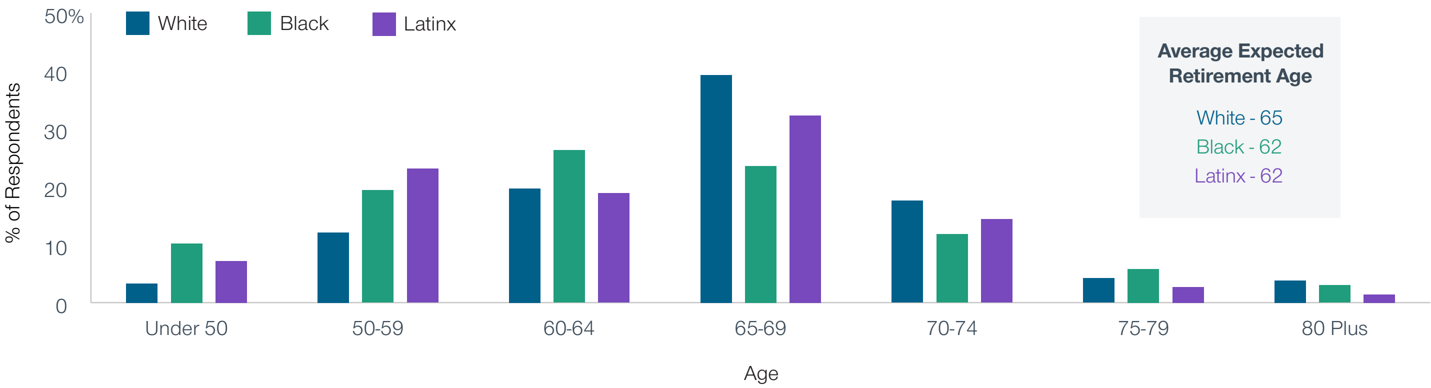
Connecting Actions Taken Today to Future Retirements

Knowing that the barriers to saving for retirement affect races and ethnicities differently, one might assume that it would also affect one's outlook on when one expects to retire. In general, there are many factors that influence when one wants to retire or needs to retire. For example, health, level of education, income, and vocation may all play a role. More specifically, someone whose job requires a lot of physical labor may retire earlier than office-based workers due to physical limitations.

Whatever the reasons, we do see that Black and Latinx respondents expect to retire earlier than white respondents. On average, white respondents cite 65 as their anticipated retirement age, while the average anticipated retirement age for both Black and Latinx respondents is 62. There could be some very logical reasons why these ages are selected,

Expected Retirement Age Varies by Both Race and Ethnicity

(Fig. 4) Black and Latinx respondents expect to retire earlier, despite lower savings rates.



Source: T. Rowe Price 2020 Retirement Savings and Spending Study.

as 62 is the earliest that one can claim Social Security and 65 coincides with Medicare eligibility. Regardless of race or ethnicity, all must entertain the possibility that they may live another 20 to 30 years in retirement.

Unfortunately, our research suggests that the combination of inadequate savings and greater amounts of debt will result in many not being able to retire on their own financial terms and may require a reduced standard of living in retirement. Still, these are challenges that employers, financial professionals, and recordkeepers are well positioned to address.

What Can Be Done?

The DC plan sits at a unique crossroads. It may be the sole place where workers of all races and ethnicities have access to financial education and tools without regard to their income or wealth. In other words, if you have access to a plan, it is a democratizing force for good. Still, that is not good enough.

Our research suggests that the worksite is the primary place that all respondents look to for advice and support for their lifetime financial goals. In fact, 83% of white respondents said so, and that figure rises to 92% and 90% for Black and Latinx respondents, respectively.

> Underrepresented minorities are an audience eager for advice, but we miss an opportunity if we don't meet them where they are with steps they can take.

There is no magic to solving the equity gaps that flow into retirement plans. Solutions start with correctly diagnosing the challenges and finding the right mix of strategies that employers and financial professionals, in partnership with a recordkeeper, can do to help these retirement savers become financially healthy. This includes helping them become more adept at managing day-to-day expenses, saving for both short- and long-term financial goals—such as emergency and retirement savings—and managing debt.

Opportunities to Do Better

The first step in this journey may be as simple as seeking input from underrepresented minority employees about what would be helpful to improve financial wellness. The more clearly one understands which factors of inequality are impacting participants with respect to retirement savings and financial wellness, the better employers will be at addressing them.

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> *Vice President, Retirement Thought Leadership*

Specific actions employers can take include:

Incorporating plan designs that prioritize participation and the use of incentives to increase contribution rates (e.g., auto-enrollment, auto-escalation, matching formulas, vesting, or employer contributions).

Implementing programs that help employees set, monitor, and prioritize meaningful financial goals and creating personalized actions that can improve one's financial wellness and preparedness for retirement, including:

- Use targeted, personalized communications to engage nonparticipants and participants to take specific actions based on factors known about them—e.g., nonparticipation or not taking full advantage of a company match.
- Offer automated services (e.g., emergency savings, consumer debt management, student loan repayment assistance, financing, and transactional processing) that help savers overcome the behavioral barriers to saving.
- Promote the tax benefits of saving in 401(k)s and the availability of additional incentives such as the Savers Credit as a means of promoting both plan participation and increasing long-term retirement savings.
- Offer education and tools that build financial capability and offer measurement so that participants can see the effect of progress (e.g., building an emergency fund, saving in an HSA, or reducing student loan debt).
- Use communication mediums that align to targeted audiences and messengers that reflect them. Employee populations are often diverse. Some participants may be more likely to engage and act if the messenger reflects their own self-image and communicates in the way they communicate with others.
- Deliver services through multiple modes of engagement that span from digital to in person so that those who seek to use the education, tools, or services offered to them can do so in a manner that best meets their needs.

FINAL THOUGHTS:

401(k) plans have benefited millions of people saving for retirement. Unfortunately, the benefits have not been shared equally. Financial wellness is a means to an end. The goal is to help people connect healthy financial behaviors and progress made toward financial goals to the retirement outcomes they seek in the future. The good news is that employers, financial professionals, and recordkeepers have the know-how to improve the financial outcomes of those who save in their employer's plan. As stakeholders to the DC system, it is time we redouble our efforts and do so.

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