How America Saves 2021: Insights to Action

Data-based recommendations that can improve participant outcomes

Several initiatives implemented by retirement plan sponsors have many participants now better positioned to achieve financial well-being than at any time over the last two decades.

As chronicled in *How America Saves 2021*, the 20th edition of our annual examination of retirement plan data, increased adoption of target-date funds (TDFs), automatic plan design features, and advice solutions are among the reasons employee saving rates are rising. At the same time, a new focus has emerged. As thousands of workers retire every day, we are seeing plan sponsors increasingly adopting plan design features that can help participants spend wisely in retirement.

In this edition of *Insights to Action*, we dig deep into these trends, suggesting actions plan sponsors can take to help improve participant outcomes. Spanning four key themes identified from *How America Saves* data, we base our recommendations on the belief that strong plan design serves participants well in all stages of their financial journey.

Key themes

Automatic solutions

Moving beyond enrollment to boost retirement savings

Incorporate automatic retirement plan features beyond automatic enrollment—already used by a majority of plans—to increase the likelihood participants will achieve retirement saving success.

Participant advice

Delivering value in both calm and troubled waters

Consider an advice solution to help participants find retirement saving and spending success—regardless of market conditions—through portfolio, financial, and emotional value.

The retiree-friendly plan

Providing a home that positions participants for success

Make your retirement plan one that can shield participants from the pitfalls of going it alone and can give them a better chance of success in retirement.

Loans and withdrawals

Finding the right balance

Review your plan's loan and withdrawal options, taking care to understand the trade-offs inherent with access to retirement savings.

Automatic solutions

Moving beyond enrollment to boost retirement savings

Plan actions

1. **Implement automatic enrollment with automatic annual increases.**
2. **Default participants at 6%, or at least to the employer match.**
3. **Perform reenrollment, undersaver, and automatic increase sweeps.**

Factors driving the success of automatic enrollment

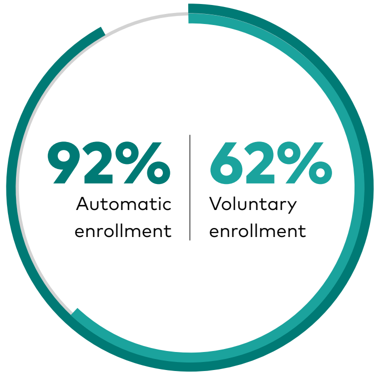
Having demonstrated the ability to improve retirement outcomes, we see continued growth for automatic solutions. That growth is likely to be driven by automatic features that go beyond enrollment—the traditional driver of growth among automatic solutions.

Plans that used automatic enrollment had a 92% participation rate in 2020, compared with 62% for plans with voluntary enrollment.

Employees who worked for firms with automatic enrollment saved more than 50% more for retirement in 2020 than those employed at firms with voluntary enrollment.

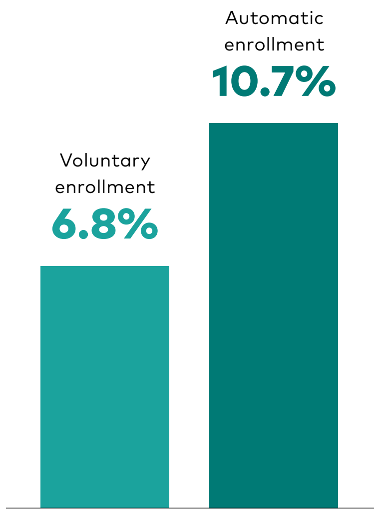
And improvements to automatic enrollment strategies continue.

Participation rates by enrollment type



Source: Vanguard 2021.

Comparing employee saving rates



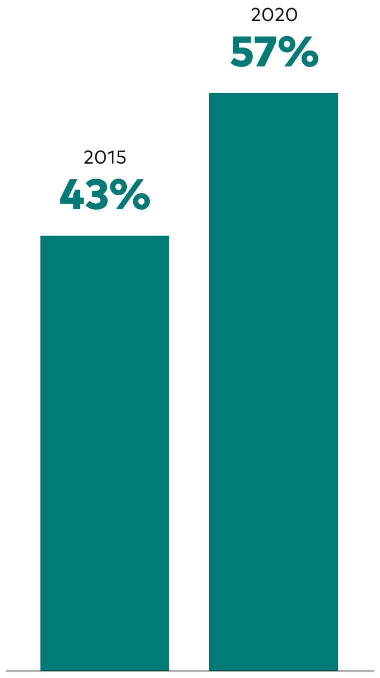
Source: Vanguard 2021.

As of year-end 2020, 57% of our plans were defaulting employees at rates of 4% or higher, up from 43% five years ago. Furthermore, one-quarter of our plans started participants at 6% or higher. That's more than double the number of plans from a decade ago.

And when it comes to retirement saving efficiency, our research demonstrates that opt-out rates for employees remained the same at 3% and 6%, so increasing the default should not raise concerns that participation could decrease.

These are some of the reasons most retirement plans now offer automatic enrollment. It's an impressive track record, providing incentive for plan sponsors to consider additional automatic features and help maintain the momentum. One such feature to consider: automatic increase.

Percentage of plans with a default rate of 4% or more



Source: Vanguard 2021.

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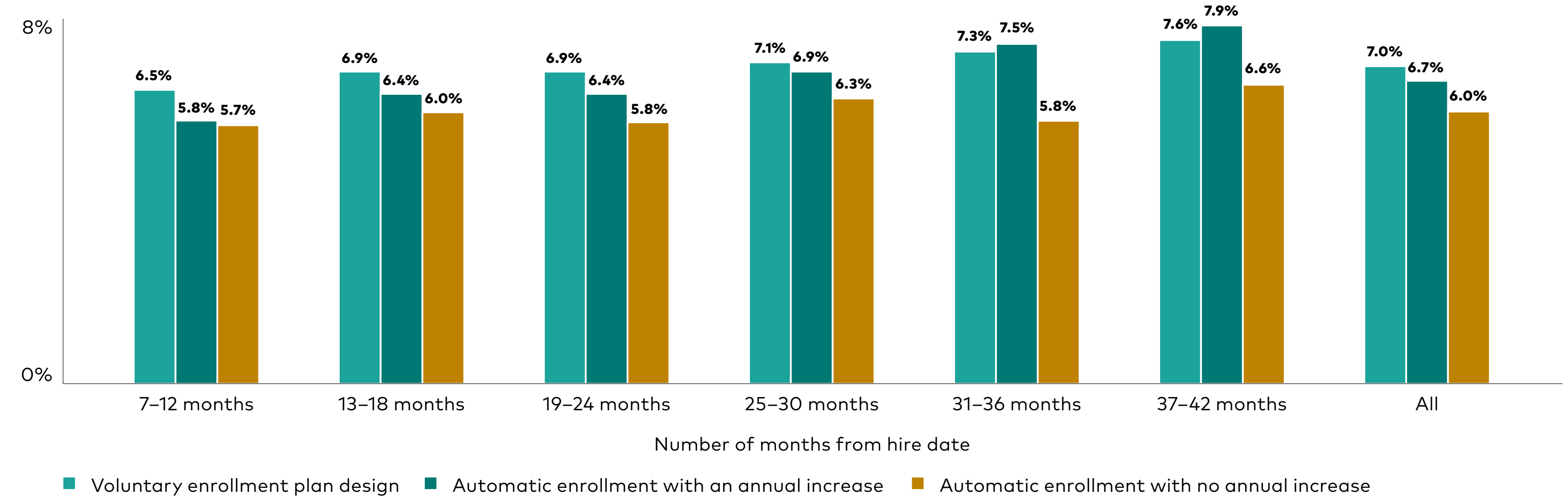
Building on success with automatic enrollment

Average participant contribution rates[1]



Source: Vanguard 2021.

Our research shows that participants enrolled in a plan with automatic increase save, on average, 20% to 30% more after three years in the plan, compared with participants in an automatic enrollment plan that does not automatically increase participants.

And because we believe retirement success hinges on participants reaching a target saving rate of 12% to 15% as soon as possible, an automatic increase feature—coupled with automatic enrollment at least at the match level—is a very powerful way to help participants reach their target.

Looking ahead, we believe regulation may also aid growth in automatic solutions. For example, the Securing a Strong Retirement Act, proposed legislation introduced in October 2020, would require automatic enrollment for participants in new defined contribution plans—an important acknowledgment that the feature benefits retirement security. Essentially a sequel to the Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019, it's intended to strengthen the retirement plan system. We support the expansion of automatic enrollment, which Vanguard research shows increases both saving rates and plan participation rates—especially among younger participants—and will continue to monitor the situation and shed light on any developments.

Beyond *How America Saves:*
Automatic enrollment: The power of the default

[1] Jeffrey W. Clark, and Jean A. Young, 2021. *Automatic Enrollment: The Power of the Default*. Vanguard research, institutional.vanguard.com.

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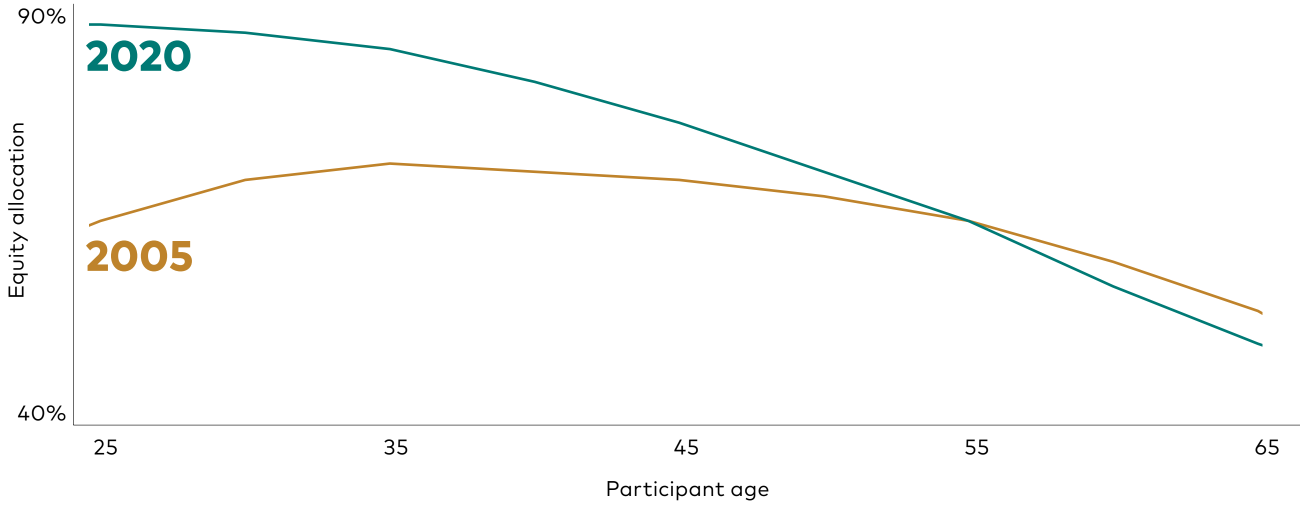
Automatic enrollment and TDFs: Encouraging balance

Most retirement plans (98%) with automatic enrollment default into a TDF. This trend yields benefits over time by getting more people into the plan with a proper asset allocation. For example, participants start saving early with a higher equity allocation, which should enable them to fare better in the long run.

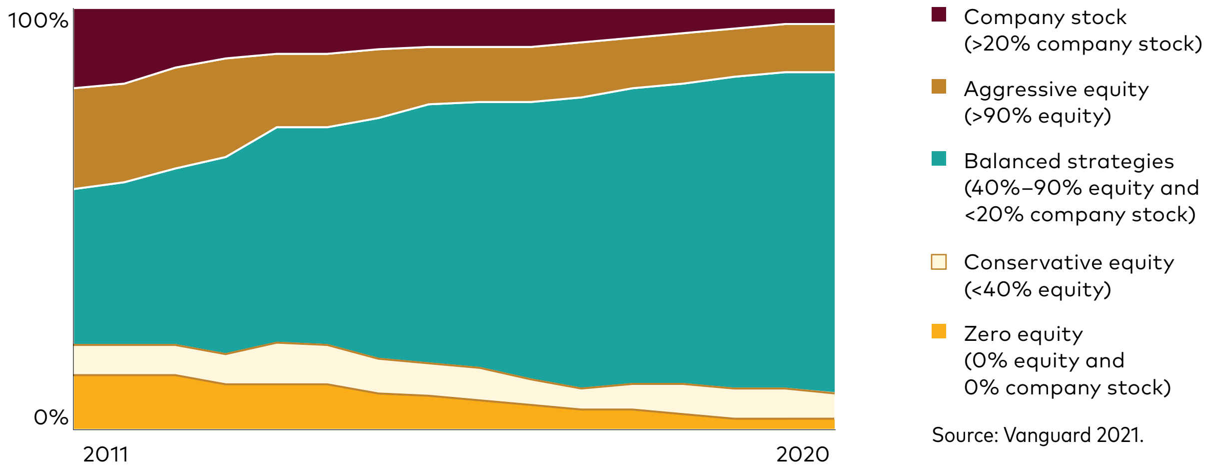
The rising use of TDFs is also having a positive effect on portfolios by helping to reduce extreme allocations.

Average equity exposure by age



Source: Vanguard 2021.

Portfolio construction trends



Source: Vanguard 2021.

Participant advice

Delivering value in both calm and troubled waters

Plan actions

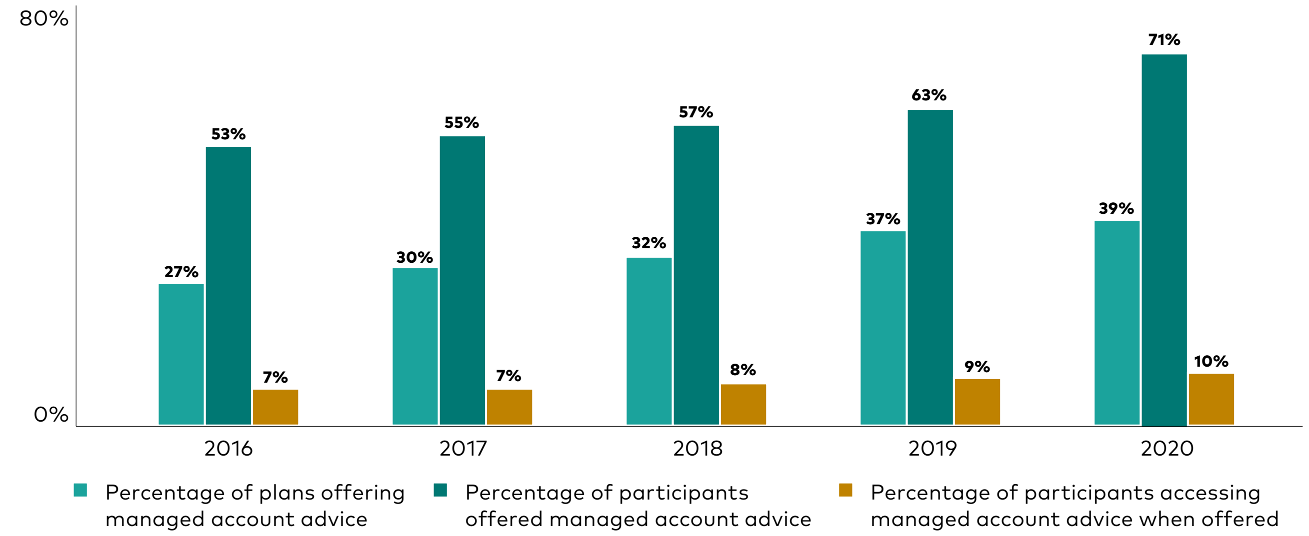
1. **Offer advice and guidance.**
2. **Consider the fees, features, and value of any advice offer before deciding.**

Plan sponsors are increasingly choosing to offer an in-plan advice option, and more participants are signing up—trends that we expect to continue.

Why do we believe the use of advice will continue to grow?

Recent Vanguard research shows that advice can add meaningful portfolio, financial, and emotional value.

Managed account advice



Source: Vanguard 2021.

Value of advice framework

Portfolio value
Optimal portfolio construction and client risk-taking

Financial value
Attainment of financial goals

Emotional value
Financial peace of mind

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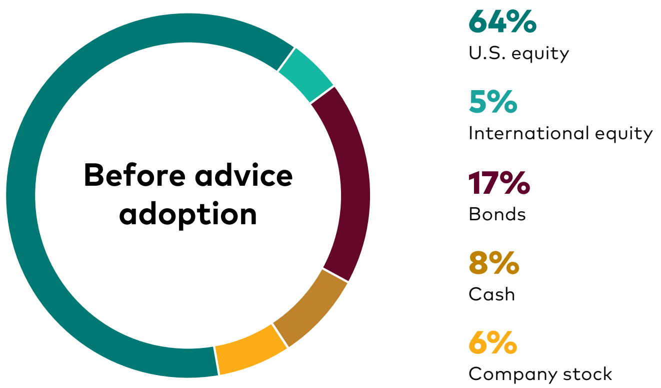
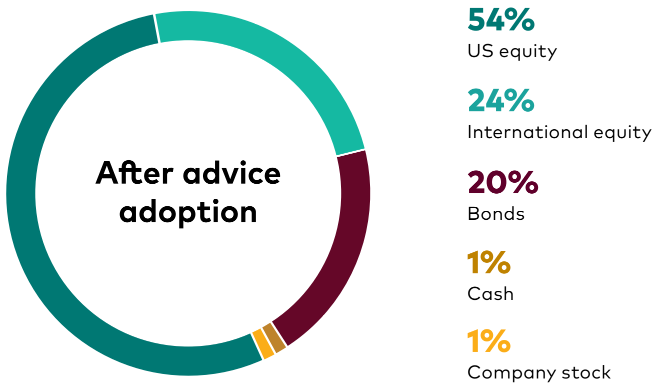
Portfolio value

Consider how portfolio construction improved after retirement plan participants chose a managed account. For these participants, managed account advice eliminated extreme equity allocations and improved international and fixed income diversification.

Asset allocation changes before and after advice adoption[2]





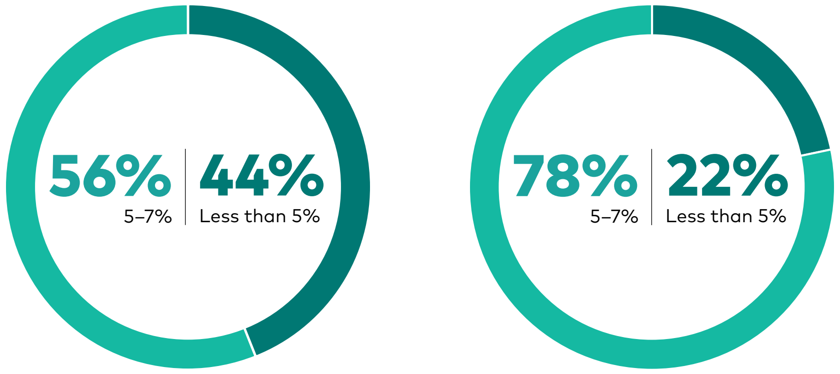
Source: *The Value of Managed Account Advice*, 2018.

Financial value

Expected real returns (net of fees)[3]

Before using managed account advice

After using managed account advice



Source: *The Value of Managed Account Advice*, 2018.

By using managed account advice, 7 in 10 participants increased their projected ten-year retirement wealth by an average of 23%, net of investment and advice fees. This increase can be attributed to higher expected returns due to increased equity exposure and, for a subset, increased saving rates.

[2] Cynthia A. Pagliaro, 2018. *The Value of Managed Account Advice*. Vanguard research, institutional.vanguard.com.

[3] Cynthia A. Pagliaro, 2018. *The Value of Managed Account Advice*. Vanguard research, institutional.vanguard.com.

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Emotional value

Investing is an emotionally charged activity that can lead people to act in ways not in their best self-interest. But through careful behavioral coaching, advice can help retirees remain calm and focused on their long-term plans, even when markets turn volatile.

To demonstrate the importance of behavioral coaching, Vanguard developed an estimate to measure the value of emotional elements such as trusting or personally connecting with an advisor. Based on a survey of more than 500 investors in Vanguard Personal Advisor Services®, our advice service for individual investors, emotional outcomes account for 45% of total perceived value.

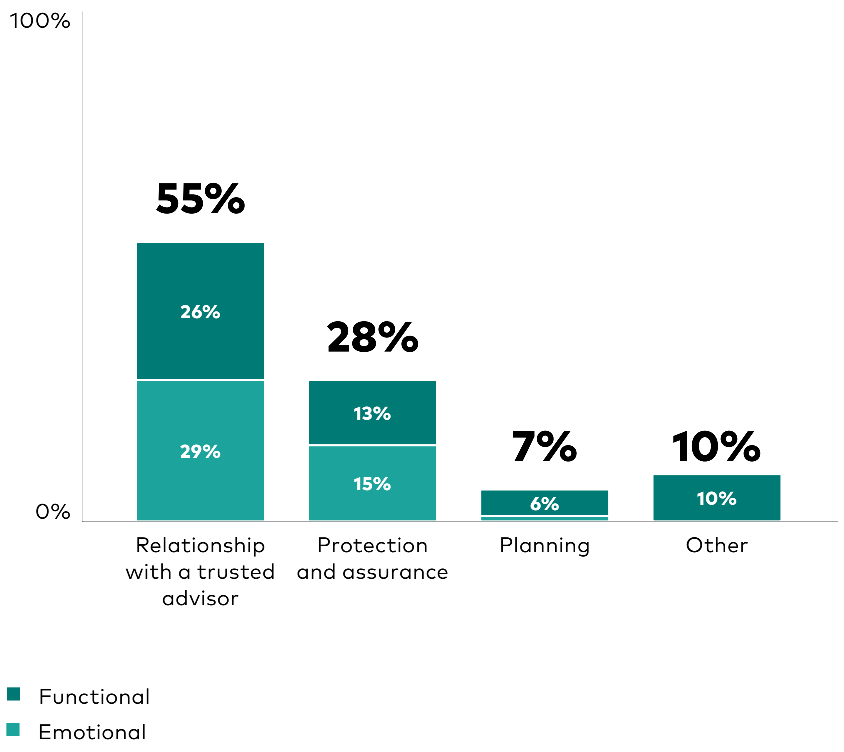
Another 55% of value is associated with functional aspects of the relationship such as portfolio management, financial planning, and other services.

Bottom line: Each participant has unique circumstances and many lack the financial planning skills, time, or interest to make appropriate investment decisions. Considering these factors, advice can benefit every participant.

Beyond *How America Saves:*
Assessing the value of advice

Emotional vs. functional value of advice[4]

2018 survey of Vanguard Personal Advisor Services clients



Source: *Assessing the Value of Advice*, Vanguard, 2019.

[4] Cynthia A. Pagliaro, and Stephen P. Utkus, 2019. *Assessing the Value of Advice*. Vanguard research, institutional.vanguard.com.

The retiree-friendly plan

Providing a home that positions participants for success

Plan actions

❶ **Allow for installments and flexible withdrawals for retirees.**

❷ **Provide valuable modeling and spending tools.**

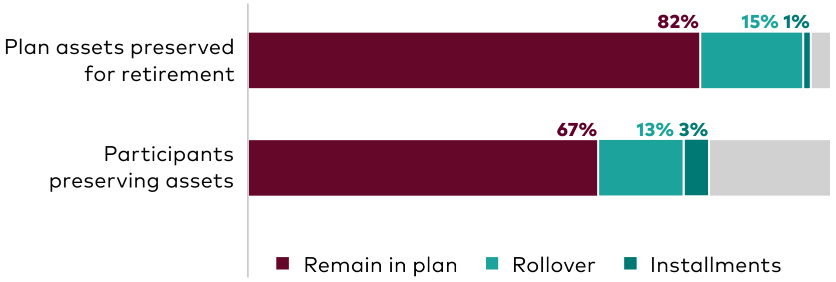
❸ **Offer an advice option that includes solutions regarding retirement income.**

Getting retirement plan participants to save more remains a priority, but plan sponsors are increasingly paying attention to ensuring participants have the necessary tools to help them spend wisely in retirement.

Demographics are key here. Baby boomers are retiring at a rate of 10,000 a day through 2029, when the youngest will reach age 65. And as more participants reach retirement, many find themselves asking: What should I do next?

- How much can I spend each year to enjoy my retirement but not worry about running out of money?
- How can I ensure tax efficiency? In other words, which account should I spend from to minimize taxes and/or maximize spending or a legacy?
- When should I claim Social Security?
- Do I need additional guaranteed income beyond Social Security?

Distribution of assets



Source: Vanguard 2021.

Simply stated, retirement preparation isn't straightforward. Eight in 10 workers would like help converting savings into income.[5] That said, most participants seem reluctant to leave their plan after separating from their employer, a possible outcome of feeling overwhelmed.

During 2020, about one-quarter of all participants could have taken their account as a distribution because they had separated from service in the current year or prior years. Most of these participants (83%) continued to preserve their plan assets for retirement by either remaining in their employer's plan or rolling over their savings to an IRA or new employer plan.

In terms of assets, 98% of all plan assets available for distribution were preserved, and only 2% were taken in cash.

[5] 2020 Retirement Confidence Survey Summary Report, EBRI, April 2020.

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We believe this behavior should be encouraged as participants can be well served by staying in their employer's retirement plan through retirement.

Participants benefit from fiduciary oversight. The rigor plan sponsors take with their participants' best interests in mind provides some assurance that their investment choices match the level of risk investors are willing to take. Plans also offer institutional pricing that's not available in retail IRAs. The price difference can be significant, sometimes 50 bps or more. The higher fees can reduce participants' principal and income stream in retirement.

For plan sponsors, the added scale builds bargaining power that can be used to advocate on behalf of the plan. Sponsors can also be confident that they are supporting the complete scope of financial well-being for participants during retirement.

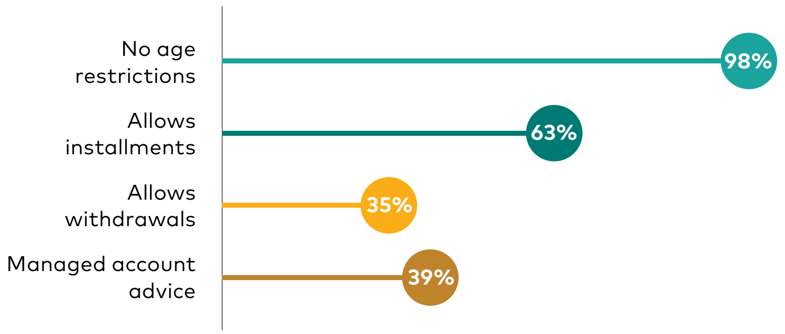
Helping participants in retirement starts with ensuring the retirement plan is retiree friendly.

This means ensuring the plan doesn't force participants out at a certain age, allows installments, and permits flexible withdrawals for those participants who would otherwise need to take all of their money out of the plan.

Then, to make sure your participants have the tools to spend wisely in retirement, ensure the plan's fund lineup supports retiree goals, provides spending guidance with simple implementation, and offers advice services.

So, how retiree friendly are plans today? The numbers have gotten better, but there is still room for improvement.

Percentage of plan design elements in use



Source: Vanguard 2021.

Importantly, plan sponsors considering investment options should keep in mind that retirement income can't be solved with a one-size-fits-all solution. Instead, we believe a better approach is an inclusive range of products, cutting-edge research, and advice provided through a fully integrated client experience that supports the complete scope of financial well-being for participants.

Consistent with this vision, we would expect to see things such as the continued development of TDFs for do-it-yourself participants that provide additional equity landing points that coincide with different retirement spending objectives. And advances in technology will continue to expand the availability of advice.

Beyond *How America Saves:*
How a retirement income solution multiplies the power of you

Loans and withdrawals

Finding the right balance

Plan actions

1. **Limit participants to one loan outstanding at a time.**
2. **Consider plan savings sweeps to help participants who may have accessed assets in 2020.**
3. **Set minimum limits for hardship withdrawals. Restrict withdrawal frequency to twice per year.**
4. **Set a "cooling off" period of 30 days to 6 months between loan payoffs and taking a new loan.**

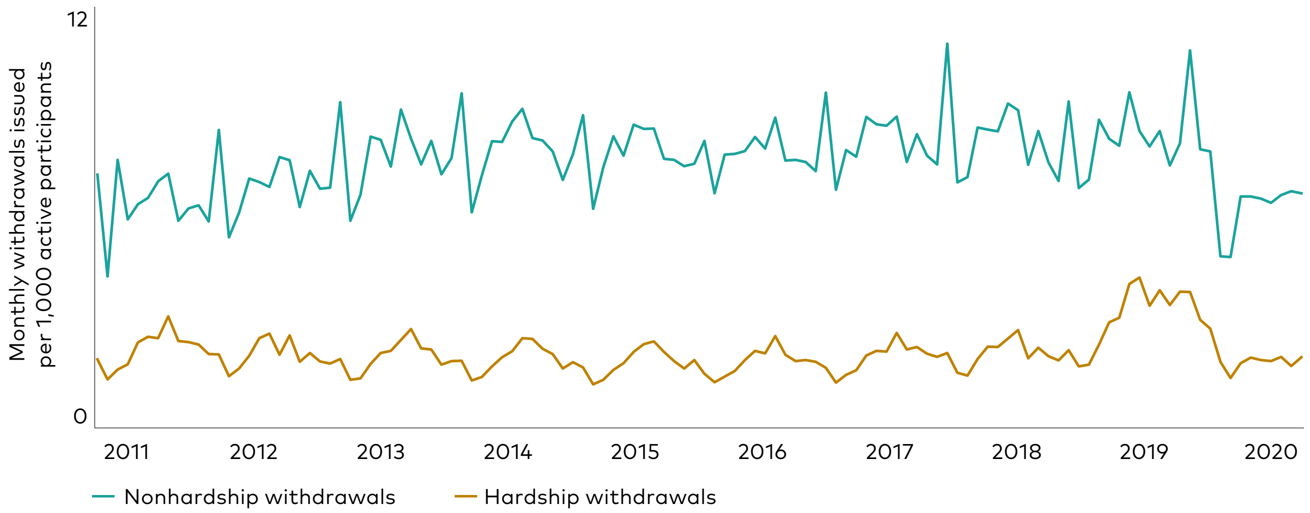
We recognize that in times of financial emergency, participants may look to access retirement funds. And while we believe doing so before retirement should be a last resort, we also believe plan sponsors should consider reasonable plan rules that balance the needs of participants facing financial emergencies with the goal of preserving plan assets for retirement. Keep in mind that loans can serve as a source of emergency liquidity and, when paid back, are not detrimental to long-term retirement savings.

Trends in retirement savings access

Throughout 2020, overall loan initiations decreased by more than 20%, with significant declines in April and May when many parts of the economy were closed due to the pandemic. We speculate the decline in loan use is partly attributable to a decrease in consumer spending, along with a decline in housing transactions between April and June.

Additionally, overall numbers in both traditional hardship and nonhardship withdrawals trended lower in 2020, compared with the previous two years. Coronavirus-related distributions (CRDs) are excluded from this analysis.

In-service withdrawal trends



Source: Vanguard 2021.

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The impact and implications of the CARES Act

As COVID-19 sent shock waves through the global economy, Congress in March 2020 passed the largest economic relief effort in modern American history—the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Incorporated within the bill were several provisions that provided flexibility for retirement savers, including CRDs. Individuals affected by the coronavirus[6] were able to withdraw up to $100,000 from their retirement plan penalty-free, until December 30, 2020. In addition, the income tax due on these distributions is allowed to be spread over a three-year period, and investors have three years to return the funds to their account.

Analysis of Vanguard defined contribution (DC) recordkeeping data shows a modest portion of workers did access their retirement savings in 2020, but that the vast majority of participants remained steadfast on their retirement journey.

Plan sponsors were given the option to permit CRDs throughout 2020. Of our sponsors, 73% permitted their participants to access retirement funds if needed.

Of the participants offered the option to withdraw assets, 5.7% accessed a portion of their savings. Of those who initiated a withdrawal, 69% took one distribution, while 31% initiated multiple distributions over the nine months.

The flexibility provided by the CARES Act allowed workers with retirement savings to respond to unforeseen circumstances through these additional financial options. While this added flexibility is helpful to many, it is encouraging that a majority of participants did not access their retirement savings during this crisis and are "staying the course" on preparing for retirement.

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Source: Vanguard 2021.

Beyond *How America Saves:*
Revisiting the CARES Act and its impact on retirement savings

[6] An "affected individual" is defined by the CARES Act as someone:

- Who is diagnosed with COVID-19 by a CDC-approved test,
- Whose spouse or dependent is diagnosed with COVID-19 by a CDC-approved test, or
- Who experiences adverse financial consequences as a result of being quarantined; being furloughed, laid off, or having work hours reduced as a result of COVID-19; being unable to work due to lack of child care due to COVID-19; closing or reducing hours of a business owned or operated by the individual due to COVID-19; or
- Other factors as determined by the Treasury Secretary.

Final thoughts

Over the last two decades, continued adoption of automatic solutions has increased employee savings and the use of professionally managed allocations. Thoughtful retirement plan designs are helping participants both save for retirement and spend in retirement. These and other trends are chronicled in *How America Saves*. But how should we interpret these trends? What do they mean for plan sponsors going forward? We hope we have at least partially answered these questions in our 2021 edition of *Insights to Action*.

The four key themes and recommended plan actions were identified by Vanguard Strategic Retirement Consulting (SRC). SRC helps DC plan sponsors optimize their plan design, develop fiduciary best practices, and ensure regulatory compliance. SRC also shares insights on investor behavior and collaborates on strategic communications.

Our complete analysis of Vanguard 2020 DC plan data can be found at institutional.vanguard.com. If you would like to learn more about the key themes surfaced in *Insights to Action*, or any of the data from *How America Saves*, please reach out to a Vanguard representative.

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